Successful innovators do not all follow the same strategy. What matters most is deciding what kind of innovator you are—an R&D-driven leader, or a follower gaining the necessary know-how by acquisition or partnering—then putting all your resources behind that decision.
It’s no secret that successful innovation leads to profitable growth. Yet it doesn’t seem to matter if you spend a lot on R&D (the key proxy for measuring investment in innovation) or a little—both can boost sales. So what exactly drives successful innovation?

New Accenture research in Europe reveals that what matters is a clear and decisive focus. Companies without a targeted innovation strategy enjoy neither enhanced stock market performance nor flourishing sales. The key challenge is to decide just what sort of innovator you are—a leader, spending heavily on R&D to break new ground, or a follower, spending less on R&D but nonetheless gaining the necessary know-how by acquiring or partnering. How you weigh that decision, moreover, will depend on the industry in which you operate.

**Common ground**

When Accenture investigated the innovation strategies of more than 200 European companies from six major industries—chemicals, steel, utilities, oil and gas, pharmaceuticals and telecommunications (see sidebar, at the top of page 5)—we found that successful innovators in all six sectors share some important characteristics.

Strong innovators, for example, are more inclined to pursue superior sustainability strategies. Indeed, the relationship between the two is symbiotic—a focus on sustainability drives innovation. A keen appreciation of resource constraints, for example, leads to product and process improvements and to greater supply chain efficiencies.

Moreover, companies in pursuit of sustainability tend to proactively integrate stakeholders in the innovation process, an approach that encourages innovative solutions that are more sustainable. Bayer, the German chemicals and pharmaceuticals company, for example, is a leading innovator that also ranks high in sustainability indices (see sidebar, at the top of page 6).

In addition, we found that the most successful innovators across all six sectors have a high proportion of board members whose nationalities are different from the company’s. This factor is particularly significant for companies in complex, global and highly regulated industries like pharmaceuticals and telecommunications, which require especially deep insights into both local and global competitive conditions.

**Key differentiators**

Indeed, though we found innovation to be increasingly important for all companies in all the industries we studied, we also discovered significant, industry-specific differences in their approaches to innovation.

Steel and utilities companies, for instance, believe that innovation is becoming more important for their businesses. For utilities in particular, this is scarcely surprising. The sector was heavily regulated in Europe until very recently (and in some countries still is), and companies generally paid scant attention to innovation in the past. Utilities are starting to catch up though—witness such “green” energy initiatives as E.ON’s decision last year to partner with DONG Energy and Masdar to build what will be the world’s biggest wind farm, located in the United Kingdom.

There are also important differences between sectors when it comes to the relative significance of process versus product innovation—though perhaps for fairly obvious reasons. As providers of new drugs, leading pharmaceuticals companies might be expected to focus on product innovations—and they do.
New-product discovery looms large for telecommunications providers as well, probably because being able to offer the ability to download music and games as well as cell phone apps has become such an important differentiator. By contrast, the innovators in the European steel sector, for which streamlining and improving production is widely regarded as the best way to boost performance, have chosen to upgrade their processes. The leading Turkish integrated steelmaker, Erdemir Group, for example, recently announced plans to optimize its entire supply chain using state-of-the-art logistics software.

**International strategies**

The pharmaceuticals and telecom sectors pursue by far the most internationalized innovation strategies (see chart, above). Moreover, both industries outstrip the other four in their use of M&A to gain innovative know-how externally.

And the pharmaceuticals, telecom and chemicals sectors rely on ideas for product innovation that emanate from local customers in local markets more than the other three industries (see chart, page 4).

(Continued on page 5)

**Centralize or decentralize?**

Companies in the oil and gas, the utilities and the steel industries tend to centralize their research and development activities, while pharmaceuticals and telecommunications companies are usually more decentralized.

**Deviation from average; average = 2.07***

<table>
<thead>
<tr>
<th>Industry</th>
<th>Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chemicals</td>
<td>-0.07</td>
</tr>
<tr>
<td>Oil and Gas</td>
<td>-0.28</td>
</tr>
<tr>
<td>Pharmaceuticals</td>
<td>+0.07</td>
</tr>
<tr>
<td>Steel</td>
<td>-0.29</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>+0.52</td>
</tr>
<tr>
<td>Utilities</td>
<td>+0.05</td>
</tr>
</tbody>
</table>

* Values range from 1 (more decentralized) to 3 (more centralized)
Source: Accenture analysis

(Continued on page 5)
Innovation and M&A

Mergers and acquisitions are an important source of specific innovation expertise and complementary technology for pharmaceuticals and telecommunications companies.

Deviation from average; average = 3.67*

Where the action is

Chemicals, pharmaceuticals and telecommunications companies tend to base their innovation centers close to new customer markets so that they can keep up with ever-changing customer wants and needs.

Deviation from average; average = 3.31*

* Values range from 1 (less important) to 6 (very important)
Source: Accenture analysis
About the research

There were 226 publicly listed European companies in our peer set—the largest (in terms of revenues) in each of six core industries: chemicals, steel, utilities, oil and gas, pharmaceuticals and telecommunications. Accenture chose these sectors because they were either important industries in Europe or were particularly R&D-intensive. Our criterion for innovation success was stock market performance as measured by each company’s market-to-book ratio. Our measure of innovation was R&D expenditure.

We used regression analysis of the available financial data to determine the relationship between R&D expenditure and performance; the influence of R&D expenditure on sales growth; the degree to which equity markets value internationalized innovation activities (as measured by the market-to-book ratio); and the influence of foreign board membership on innovation strategy.

We also used regression analysis to establish the relationship between a company’s outlay for R&D and its commitment to sustainability. Our proxies for the latter included ranking in the Dow Jones Sustainability Indexes and the FTSE4Good Index Series; membership in the Global Reporting Initiative, which is linked to the United Nations Environment Programme (UNEP); and other corporate social responsibility reporting initiatives, including the United Nations Global Compact.

We supplemented this quantitative investigation with a questionnaire, which we sent to the companies in our six core industries. It was completed by 70 of them—a response rate of more than 30 percent. The respondents told us how important innovation is to them and whether it is growing in importance; whether their focus is on product or process innovation; the importance (or not) of an international innovation strategy; whether or not customers participate in developing their innovation strategy; the significance of foreign know-how in developing that strategy; and whether they seek to acquire specific innovation expertise or technologies.

This article on innovation is part of a more comprehensive, evidence-based analysis of European companies on the path to high performance. The complete “Phönix Report” will be published in early 2010.

(Continued from page 3)

These three sectors need to keep abreast of—and ideally ahead of—developments in very diverse markets. Chemicals companies, for example, often produce very specific solutions for specific customers, hence the importance of local customer involvement in product design and engineering. For their part, leading pharmaceuticals innovators pursue M&A to acquire valuable patents or to penetrate otherwise inaccessible markets. It also makes sense to buy know-how in an industry where product innovation can be slow to materialize and is subject to a high failure rate, which is a good way to describe pharmaceuticals.

Similarly, for a telecom company seeking profitable expansion in desirable markets, it would be logical to either buy existing expertise—Deutsche Telekom, for example, has been engaged as a minority stakeholder in the Greek telecommunications group OTE since 2008—or to acquire it via partnership. The Spanish telecom provider Telefónica, for instance, recently reached agreement with six leading technology providers to develop so-called fourth-generation mobile technologies in six of its global markets.

Or consider Nokia, which is leveraging the ideas of both customers and employees worldwide in a quest for an innovation advantage. The Finnish company recently set up an intranet soapbox called Blog-Hub, for example, that allows employees (anonymously, if they prefer) to tell management just what’s on their minds—input that Nokia believes will yield some smart new ideas.

Investors favor a decentralized, global approach for innovation.
Bayer: Setting standards for sustainable innovation

If sustainability is your goal, it helps to be an innovator—and vice versa.

Bayer, the German chemicals and pharmaceuticals giant, strives for “sustainability in everything we do”—and with considerable success.

The Leverkusen-based company has been listed in the Dow Jones Sustainability World Index, which measures sustainability according to economic, ecological and social criteria, for 11 consecutive years. And it is the first firm in the European chemicals and pharmaceuticals sectors to appear for five years straight in the Carbon Disclosure Leadership Index, which ranks companies’ efforts to tackle climate change.

Bayer, moreover, is just as well known as an innovator. Indeed, innovation has been the company’s hallmark since it was founded, in the mid-19th century, to develop synthetic dyes for the textile industry. In 1899, for example, having added pharmaceuticals to its product portfolio, Bayer introduced Aspirin, which had been created by one of its chemists two years earlier.

It is the application of innovation to the challenges of sustainability, however, that really distinguishes the German company. Despite the economic crisis in 2009, Bayer increased R&D spending to the record level of approximately €2.9 billion, and the company’s operational business groups delivered key examples of sustainable innovation.

Bayer MaterialScience, for example, has patented plastics developed from plant materials that enhance the durability of cell phones, furniture and toys. Its components for solar power modules have won awards for sustainability, as have its innovative technologies for chlorine production. In January 2009, the division began constructing a pilot facility for carbon nanotubes—strong and resilient yet lightweight components that help make rotor blades for wind turbines more energy efficient, transport vessels lighter and sports equipment stronger.

Meanwhile, Bayer CropScience has endowed a chair for sustainable development at North Carolina State University, which is also one of its external R&D partners. And in March 2009, Bayer HealthCare, in an initiative of its new research and development center in Beijing, partnered with Tsinghua University to form the Bayer-Tsinghua (Institute of Biomedicine) Research Center of Innovative Drug Discovery.

For further reading

Innovation and cost reduction: “Why less is the new more,” this issue, page 26

Innovation in telecommunications: “Open innovation: How to create the right new products, the right way,” Outlook, October 2009


Innovation as a business discipline: “How to get the most from your best ideas,” Outlook, September 2008

For these and other articles on innovation, please visit accenture.com/Outlook
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