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Innovating in the digital economy

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It is all about creating and capturing value, building networks, and scaling up quickly

It is a simple question: How do you innovate in the digital economy? The answers are perhaps less straightforward given the breakneck speed of digitalisation and the many disruptions caused by COVID-19 and "slowbalisation" – 'country of origins' requirements imposed by USA causing logistics complexity. Throw in the shift away from just-in-time supply chains to build in robustness and responsiveness, and things become even murkier.

The main challenge, says **Arnoud De Meyer**, Professor Emeritus at SMU's Lee Kong Chian School of Business (LKCSB), is to be 'first to scale', citing the examples of Uber, Airbnb and other digital platform companies whose business models are "not that innovative but they became successful because they could offer scale and thus positive network effects".

However, innovation is always about value creation and value capturing, and the first rule involves listening to users of your product or service, advises Prof. De Meyer.

"I say 'user' and not 'customer'," he elaborates, adding that the 'customer' in a B2B environment is often the procurement department instead of the 'user' which might be the "machine operator or engineer, or a financial specialist using a software". "In a B2C environment, such as a hospital, for example, the patient may be the user but the customer is usually the insurance company.

"In Western Europe, the buyers of cars are usually men. But the people who use the cars most are women, who bring the kids to school and go grocery shopping. Very often we don't listen enough to the experiences of women using the car.

"I challenge you to make sure you listen to your user."

CAPTURING VALUE

Prof. De Meyer made those comments at a recent LKCSB Business Partnerships Unit webinar titled "Managing Innovation in the Digital Economy" where he added that leadership with a clear vision and strategy for innovation is crucial to "be able to say 'No' to opportunities so you don't get distracted in some of the innovation activities".

He also highlighted the advice from Gary Pisano's 2015 Harvard Business Review article, "You need an Innovation Strategy":

1. How will innovation create value for potential customers?
2. How will the company capture a share of the value its innovations generate?

3. What types on innovations will allow the company to create and capture value, and what resources should each type receive?

“Innovation comes with risk,” Prof. De Meyer notes. “When I was doing consulting on innovation management, I always asked CEOs this question: ‘How many of the innovation projects that you currently have under development do you think will succeed?’ If their answer was anything above 65 percent, I would say, ‘You guys are not innovating. You’re just taking the safe route of routine innovation.’”

Elaborating on the four types of innovations (see Figure 1), Prof. De Meyer says: “If you really want to be innovative, you need to go into the quadrants of radical, disruptive, or architectural innovation. But it’s calculated risk. Cold-blooded calculation. You should know that, under no circumstances, will an innovation project be guaranteed to succeed.”

FIGURE 1

Requires new business model	Disruptive	Architectural
Leverages existing business model	Routine	Radical
	Leverages existing technical competency	**Requires new technical competency**

Only when that is decided can imagination and creativity come into play, Prof. De Meyer explains. “You need to first create that context and vision, you need to have that awareness and willingness to take risk. You need to have the input of the users before creativity can blossom, and you have the sandboxes for your young people to come up with the most out-of-the-blue ideas. That’s why creativity is not the first item for innovation."

IT’S ALL ABOUT ECOSYSTEMS

As for generating ideas for innovation, Prof. De Meyer looked back at his time at Cambridge University around whose campus “there were lots of very effective and rapidly growing startups” but whose CEOs most people would struggle to name, unlike those at Silicon Valley such as Facebook (Mark Zuckerberg) and Google (Larry Page and Sergey Brin).

“These companies were working in a more collaborative network, very different from what we saw at Silicon Valley [from 2006 to 2009],” observes Prof. De Meyer. One of these companies was computer processor company ARM, which SoftBank acquired in a US$32 billion deal in 2016. “ARM is quite a small company but it built up a network of chip designers, manufacturers and distributors, OEMs, and software developers.

“Why did SoftBank pay US$32 billion? No doubt they wanted the design and the evolution of the design of the processors, but they also wanted to have the network.”

Prof. De Meyer reflected on how ARM built their networks and found in business literature, again in the Harvard Business Review, James Moore’s “Predator and Prey: A New Ecology of Competition” in 1993. In it was this point:

> *“A business ecosystem is a network of organisations and individuals that co-evolve their capabilities and roles and align their investments so as to create additional value and/or improve efficiency.”*

“There are three elements that are important," says Prof. De Meyer. "It’s about additional value that you couldn’t create on your own. Secondly, it’s about a network of organisations and individuals. Thirdly, it’s about co-evolving your capabilities and roles, and aligning your investments.”

These observations were made in 1993, and some five years later in China Alibaba started its path towards becoming the behemoth it is today by building ecosystems. Haier, China’s white goods giant, outplaced and made most its middle management into small entrepreneurs and created ecosystems around them to come up with new products. The Guardian newspaper, Prof. De Meyer added, did something similar by building an ecosystem of news suppliers and publishing houses to sell marketing and promotion opportunities.

“We saw that ecosystems had huge advantages. You could bring partners together with diverse capabilities, which enables you to learn from each other. It is flexible because you can enable partners to adjust activities quickly to changing circumstances. You can let partners go and bring in new partners when you need new capabilities.

“It has relatively low asset intensity, you don’t have to spend enormous amounts of money on assets. And because you work in loosely coupled networks, it allows for rapid scaling up, which is what we want to do.”

Prof. Arnoud De Meyer was the main speaker at the SMU LKCSB Business Partnerships Unit webinar “Managing Innovation in the Digital Economy” held on 22 June 2021.

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