

Welcome to the February Innovation Update briefing which takes a new look at innovation in tough times:

Innovation Briefing: What 2009 Will Reveal - The Story So Far?

Looking into short term changes and developments is a common New Year activity for many across the media and trends arena: You probably saw many articles in the press in January. Although we spend much of our time looking over the short term horizon for the larger more substantial drivers of change for innovation, we also get asked for our perspectives for the more here and now. Especially in the current economic environment, companies and governments alike have been asking for our views of what should be their priority areas of focus and what should be changed as many of the assumptions upon which decisions were made have themselves changed.

In this light, two months into 2009, we thought it would be useful to share three of the seven short term perspectives Social Technologies had at the start of the year ... and also see how they were faring in these shifting times and what associated innovation implications they offer:

Are we depressed?

Of course, the biggest single question hanging over the year is the unknown depth of our economic difficulties. Is this an ordinary recession? A super-recession? Or might we find ourselves in a new depression? Already, we're seeing some significant consequences of the economic meltdown, such as changes in the finance system and new roles for government. These and other effects will linger for years. Long-running trends have been interrupted: world trade is expected to drop for the first time in a quarter century, and US retail sales are expected to decrease for the first time since 1995, when the National Retail Federation began tracking them. If the world heads into a true depression, changes in economic patterns, social issues, and consumer values would last a generation, just as they did for those who weathered the economic storms of the 1930s. So far, the worst outcome still appears unlikely.

From an innovation point of view, it is clear that many companies are cutting back on R&D and marketing expenditures and, as we noted in the Financial Times last week, several organisations are using this as an opportunity to innovate around their business models for short term impact. That said, in several lucky sectors the recession is a cash-flow blip while in others it is far more of a potential cliff. As governments and banks start to gain alignment and some of the cash injections take hold, we see many organisations planning for an upturn in innovation activity after the summer as they put projects back on track to take the lead in 2010.

How deep does green go?

This economic downturn will test Americans' commitment to sustainability. Will it all be abandoned if times get tougher and energy prices continue to drop? Aspects perceived as luxuries-from organic food to carbon offsets-may be set aside if consumers feel pinched. On the other hand, investments made now could promote sustainable practices that save resources and money over the long -term. Already we're hearing that the Obama administration's stimulus package will include funding to make federal buildings more energy-efficient, which is expected to save \$2 billion annually.

Whether associated with the new administration's perspectives or the way in which it has had to react to the economic challenges, it is clear that sustainable development is fast becoming actions as well as words. However the key concerns from an innovation perspective here cover both scope and approach. Take for example the support for the automotive sector around the world that was covered in last month's briefing. In an interview on the BBC to celebrate 25 years of Virgin Atlantic, Richard Branson highlighted that if you really want innovation around the sustainability agenda, then rather than giving \$100bn to prop

up broken businesses with the stick of clean-tech, it is more effective to give \$1bn to 100 start ups focused on creating the next generation of high efficiency vehicles. Surely, the same philosophy across the board would do well to seed greater innovation.

The Chinese model under stress

Our analysts have been writing about possible discontinuities for China for a while now, and we are seeing some of the warning indicators we've discussed in the past. China's growth is slowing as the economic downturn hurts global demand. As Chinese workers lose their jobs, it begins to call into question China's basic social model: rising prosperity in return for popular acquiescence to authoritarian Party rule. We may see just how far this bargain between China and its citizens can be strained. The consequences of instability in China would go well beyond that country's borders: to begin with, it is the world's manufacturer, and a disruption in production would affect the supply of countless consumer goods.

*As Hillary has set out to woo China in the past week, it is worth also looking at how some of the excellent insights in Niall Ferguson's 2008 book, *The Ascent of Money*, are playing out. In the final chapter, *From Empire to Chimerica*, he highlights the interdependence of the two superpowers and how neither can prosper without the other. What China makes, America buys - and this has increasingly been with money borrowed from China's workers who need to keep making stuff to support growth. From an innovation perspective, one area will be important to watch carefully over the next few months as China continues its economic rise. Can it shift up from economic control of the world's natural resources through acquisition of companies and assets at rock bottom prices to where it actually construct and deliver higher value product offerings? Some Chinese manufacturers are already agreeing currency exchange rates outside the official rates, and as this accelerates, the flow of money between China and America could have paradigm shifting impact on where innovation happens and where it has economic benefit.*

Like any other corporate activity, innovation is not sacrosanct in a downturn. But unlike most other areas of strategic focus, it has greater power to act as a catalyst for a more sustainable future. The challenge in the current environment is in simultaneously maintaining the long term focus while also being more effective in the short term in terms of application and impact. And, at the same time, to do this within a fast shifting economic environment where the context of why, how, who and where matters just as much as what to innovate.

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