McKinsey Global Survey Results:

Assessing innovation metrics

A recent McKinsey Global Survey shows that companies are satisfied, overall, with their use of metrics to assess innovation portfolios—though many findings suggest that they shouldn't be. The companies that get the highest returns from innovation do use metrics well; these organizations tend to assess innovation more comprehensively than the others.

Even in the current economic turmoil, innovation remains a high strategic priority for most companies, and many see it as a strong contributor to growth. Yet many also struggle to measure the performance of their innovation portfolios. In a recent McKinsey Global Survey,[1] we asked senior executives which types of innovations their companies pursue, which ones they measure and with what metrics, what goals they have in using metrics, and how satisfied they are with the metrics they choose.

Companies reporting the highest contribution to growth from their innovation projects tend to be more interested in pursuing and measuring their innovations as a portfolio and therefore use metrics across the whole innovation process. In the end, they are more satisfied than others with the ability of such metrics to help their organizations do everything from aligning individual performance incentives to improving innovation performance to communicating with investors.

[1] Conducted in October 2008, the survey had 1,075 respondents, all C-level or other senior executives, representing a full range of regions and industries.

Jean-François Martin

The McKinsey Quarterly

Sixteen percent of the respondents say that their companies don't use any metrics to assess innovations. Among those that do, most are satisfied overall, though the findings suggest they aren't effectively using these metrics as well as they could. Most notably, companies are much likelier to rely on metrics for outputs than for inputs, so they aren't assessing the whole process of innovation. Forty-five percent don't track the relationship between spending on innovation and shareholder value. Further, although many companies are satisfied with their use of innovation metrics in general, far fewer are satisfied with specific uses, such as aligning individual performance incentives.

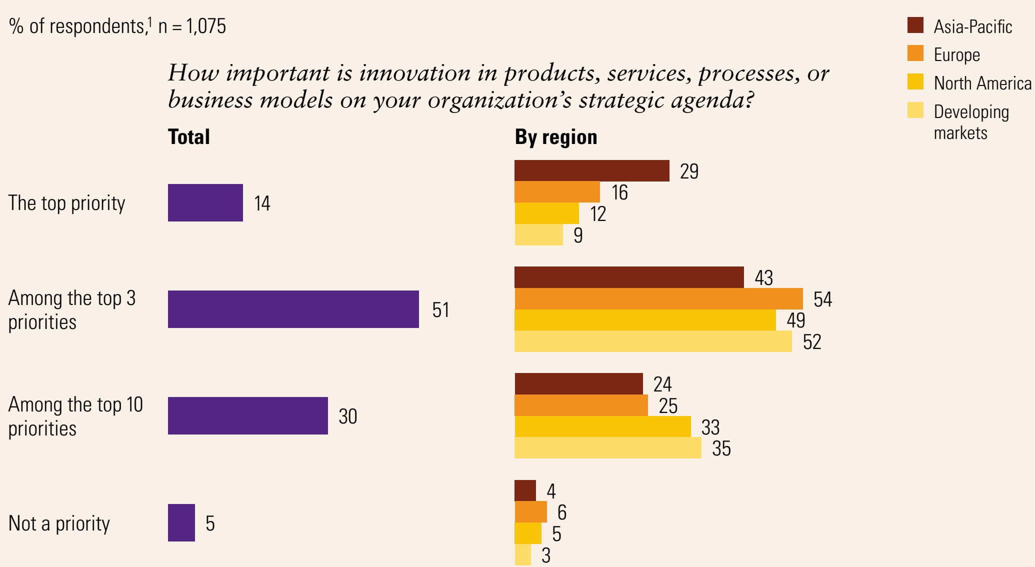
What gets measured and why

Innovation is a high strategic priority for most companies (Exhibit 1). However, this survey shows slightly fewer senior executives either selecting it as the top priority or placing it among the top three than those who responded to a similar question last year:[2] 65 percent now, compared with 70 percent in 2007. This drop may reflect the fact that the latest survey was in the field after the credit crunch and stock market turmoil had begun to reorder many companies' priorities.

[2]In September 2007, a McKinsey Global Survey asked, "Over the next three to five years, how important will innovation as a major driver of growth be on your leadership team's agenda?" See "How companies approach innovation: A McKinsey Global Survey," mckinseyquarterly.com, October 2007.

Exhibit 1

A strategic priority



[1]Respondents who answered "don't know" are not shown.

The kinds of innovation companies take up are diverse. Yet no matter what form of innovation they pursue, far fewer companies measure it than pursue it (Exhibit 2).

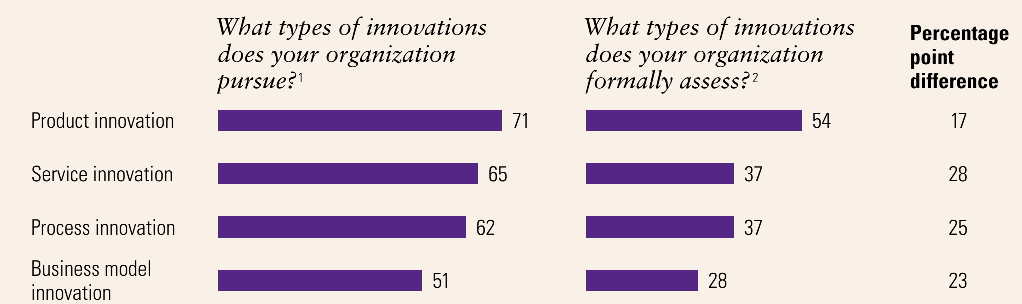
Even at companies that actively pursue innovation, 16 percent of executives say their companies don't formally assess innovations at all

Respondents say that their companies use about eight metrics, on average, to assess innovations. They cite three main reasons for doing so: to provide strategic direction for innovation activities, to guide the allocation of resources to innovation projects, and to diagnose and improve overall innovation performance.

Exhibit 2

A lack of measurement

% of respondents, n = 1,075



[1] Respondents who answered "other" are not shown.
[2] Respondents who answered "other," "none," or "don't know" are not shown.

How metrics are used

Although the goals of companies would suggest the need to emphasize the overall innovation process, that process is rarely the focus of the metrics companies use most. When asked which metric is the single most important among those used, executives are much likelier to cite a few simple outcome metrics than input metrics or performance metrics, such as time to market or time to breakeven (Exhibit 3). When respondents indicate the three metrics they use most, the order is the same. There are surprisingly few differences among companies in different industries or regions.

Exhibit 3

Outcome metrics are in wide use

[1] Respondents who answered "other" are not shown.
[2] Metrics ranked no. 1 by less than 2% of respondents are not shown.

At companies that track the relationship between shareholder value and spending on innovation, the three most important metrics are all externally focused: revenue growth, customer satisfaction, and the percentage of sales from new products or services. At companies where innovation is the most important strategic priority, the top three metrics are a somewhat more comprehensive mix: customer satisfaction, the number of ideas in the pipeline, and R&D spending as a percentage of sales.

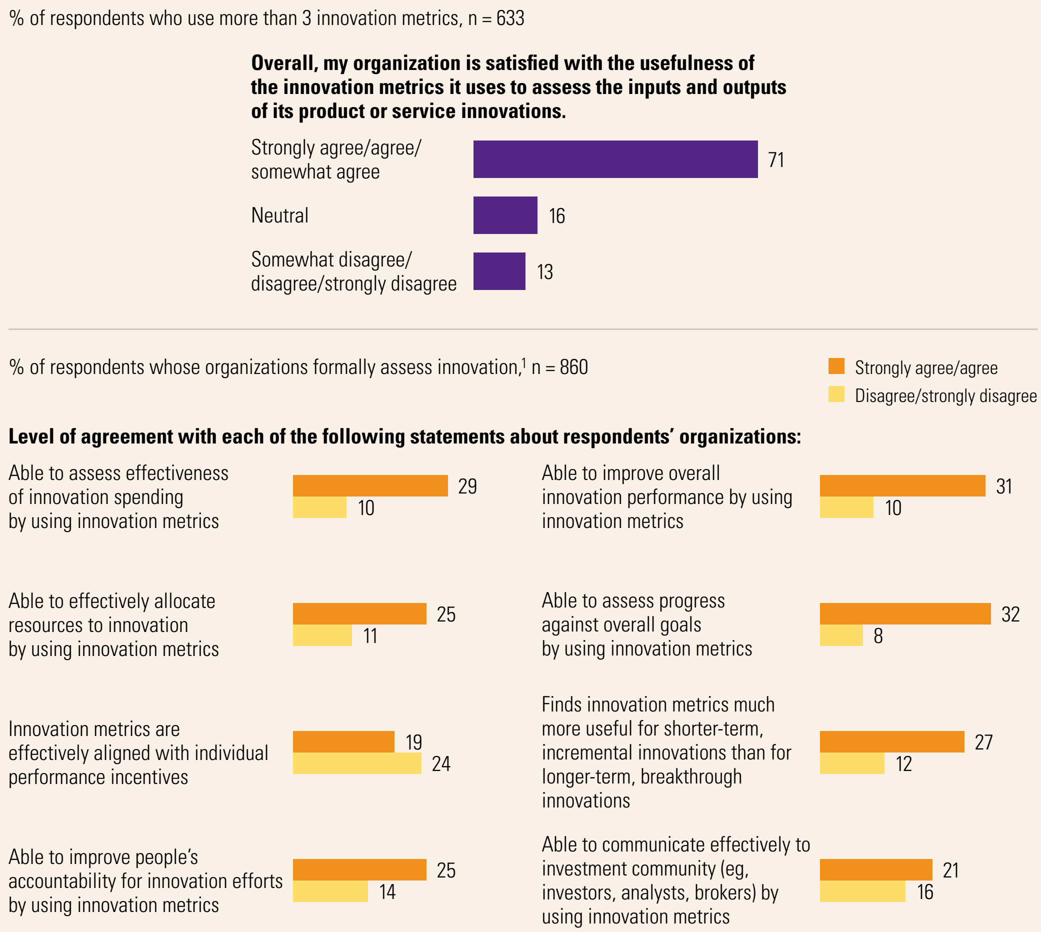
In addition, though companies typically assess their performance in most areas relative to that of their peers, many companies don't do so with innovation metrics. One reason may be that competitive data on the innovation metrics that companies use most frequently aren't always available. In any case, 49 percent of the respondents say they don't benchmark themselves against competitors on any of the innovation metrics they use, while 43 percent say that they do.

Regardless of the combination of innovation metrics respondents use and why, more than 70 percent of them say they at least somewhat agree that their organizations are satisfied with the usefulness of these metrics (Exhibit 4). Most notable, though executives are satisfied overall, less than a third agree or strongly agree that they are satisfied with any specific use of these metrics. Companies may be tracking more innovation metrics than they can put to good use.

Nearly 40 percent of executives disagree to some extent with the statement that innovation metrics are aligned with individual performance incentives

Exhibit 4

Significantly useful



[1]Respondents who answered "somewhat agree," "neutral," or "somewhat disagree" are not shown.

Following the money

Just over half of all respondents say their companies are spending about the right amount on innovation, given its strategic importance. (Interestingly, 7 percent say their companies are spending too much.) When asked how annual innovation spending is determined, the largest number of respondents say that their organizations consider the available opportunities (Exhibit 5).[3]

[3] This is consistent with one of the 2007 survey's findings: only 27 percent of senior executives said then that their processes for planning budgeting, strategy, and growth (including innovation) were fully integrated. See "How companies approach innovation: A McKinsey Global Survey," mckinseyquarterly.com, October 2007.

Exhibit 5

How innovation money is allocated

% of respondents whose organizations formally assess innovations,[1] n = 860

Which of the following methods, if any, best describes how your organization's annual spending on innovation is determined?

[1] Respondents who answered "other" or "don't know" are not shown.

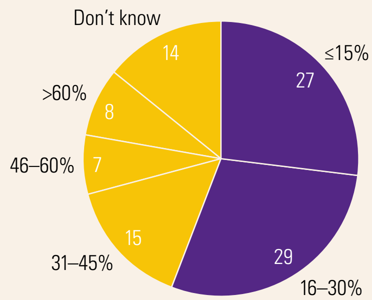
Less than a third of the respondents' companies track the relationship between spending on innovation and shareholder value (and nearly a quarter don't know whether or not they do so). However, innovation is generally seen as a strong contributor to organic growth (Exhibit 6), probably indicating that companies find their innovations worthwhile overall. This interpretation is consistent with a finding from another McKinsey survey on innovation, in which 58 percent of the respondents, when asked about a single major innovation at their companies, said that the innovation had been very or extremely successful.

Exhibit 6

A key factor for organic growth

% of respondents whose organizations formally assess innovations, n = 880

What portion, if any, of your organization's annual organic growth over the past 5 years can be attributed to your overall innovation portfolio?



Innovation, metrics, and growth

One group of respondents both reported higher organic growth rates than their competitors did and said that at least 31 percent of their organic growth comes from innovation. These respondents have a somewhat different approach to using innovation metrics. In general, they have a greater interest in pursuing and measuring their innovations as a portfolio: they are more likely than other respondents to pursue and measure all types of innovation, and nearly a quarter (far more than other executives) say that creating a balanced portfolio of innovations is one reason they use metrics. High performers are also much less likely—29 percent, compared with 37 percent of other respondents—to say that they base their innovation spending on the relative attractiveness of individual projects.

These high-performing organizations use, on average, only one more metric than all respondents do. But they are likelier to use metrics across the whole innovation process, such as assessing the number of people actively devoted to innovation, the number of new ideas sourced from outside the organization, and the percentage of innovations that meet their development schedules. Like the companies of most other respondents, the high-performing ones also track the financial returns from innovation in general and customer satisfaction with specific innovations.

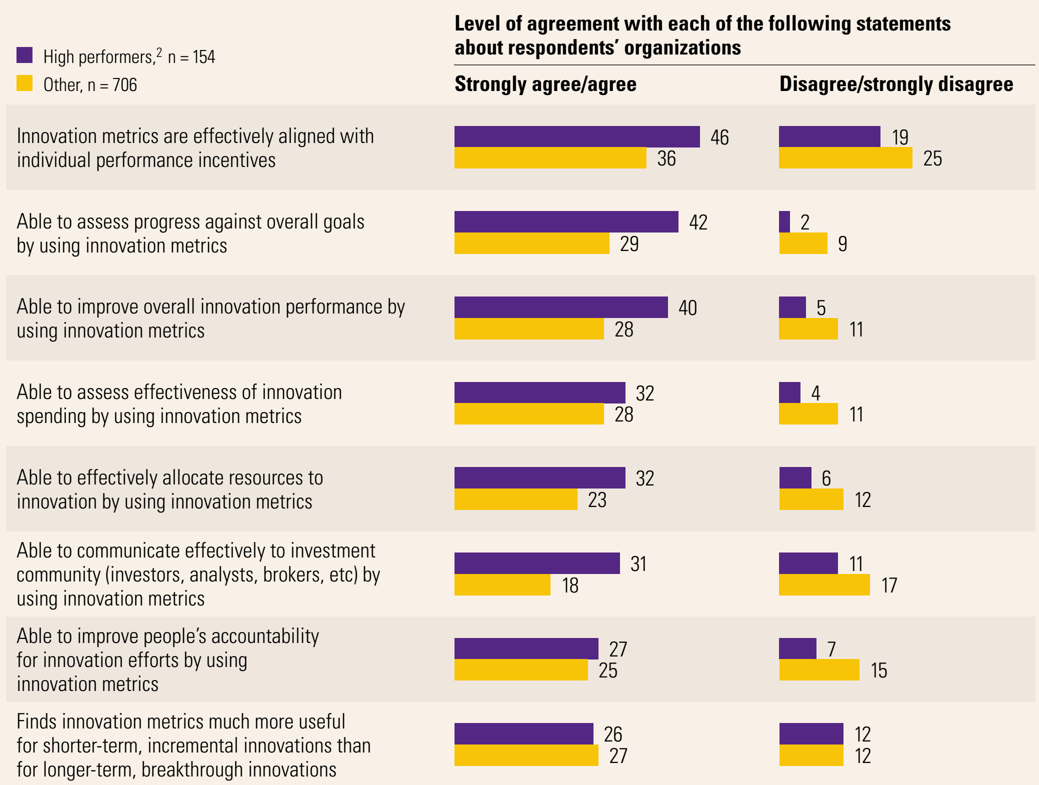
Just less than a third of high performers assess the potential of the entire innovation portfolio, and among those 70 percent say that this is their single most important innovation metric

Finally, high performers are satisfied with their use of metrics across a wide range of activities, including allocating resources, aligning metrics with individual performance incentives, and communicating with investors (Exhibit 7). These companies may be more satisfied because they make greater use of metrics that, taken together, assess the whole process of innovation.

Exhibit 7

Less thought, more action

% of respondents[1]



[1]Respondents who answered "somewhat agree," "neutral," or "somewhat disagree" are not shown.
[2]Includes respondents who report higher organic growth than their competitors and say that at least 31 percent of this growth comes from innovation.

Looking ahead

- Companies that use innovation metrics are, on the whole, satisfied with their use. The many companies that don't track their innovations can probably gain a better understanding of their innovation performance just by introducing some of these metrics.
- Many companies would gain a deeper understanding of their innovation performance if they paid more attention to input metrics as well as output metrics, benchmarked themselves against their competitors, and dug into the relationship between innovation spending and shareholder value.
- Although executives are on the whole satisfied with the way their companies use innovation metrics, the findings indicate significant room for improvement in many individual applications—most notably, aligning metrics with individual performance incentives and using them to communicate effectively with investors. ■

The contributors to the development and analysis of this survey include **Vanessa Chan**, an associate principal in McKinsey's Philadelphia office; **Chris Musso**, an associate principal in the Cleveland office; and **Venkatesh Shankar**, the Coleman chair professor at the Mays Business School, at Texas A&M University. They would like to acknowledge the significant contributions of George Day, Boisi professor at the University of Pennsylvania's Wharton School, and of David J. Reibstein, the Woodside professor at Wharton.