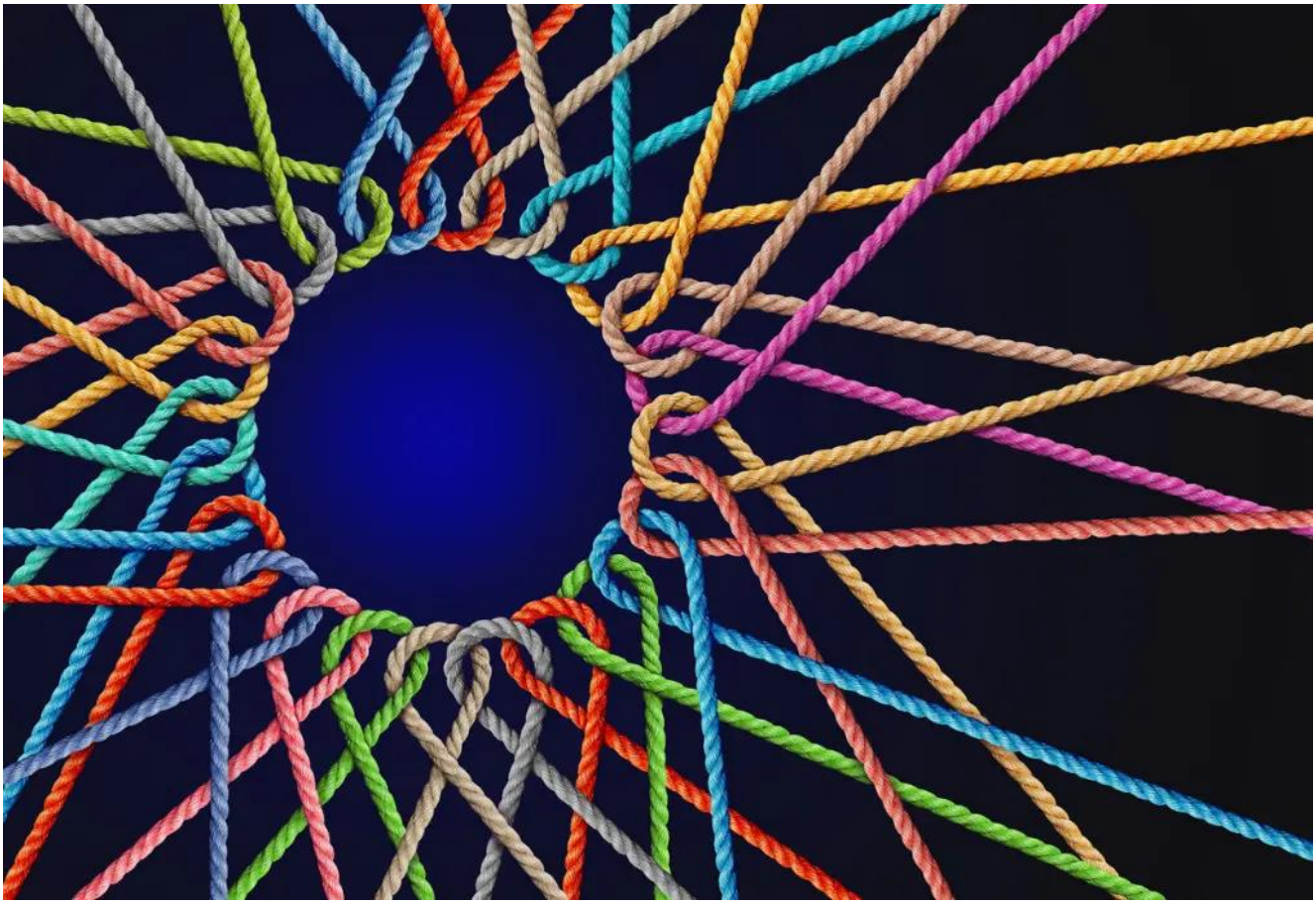
How to align your innovation portfolio with your strategy

Innovation projects that look good on paper can drift away from corporate strategy. Four keys to correcting course.



October 26, 2026

Innovation portfolios can become crowded with projects that seem promising according to standard formal criteria but that are quietly drifting away from what the business actually

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needs. For managers, the solution to this drift is not more metrics or more meetings, but rather a more disciplined conversation about strategy, priorities and investment.

Innovation is often treated as a pipeline problem: generate enough ideas, select the most promising ones and allocate resources to them. Research by IESE's Christoph Loch, with coauthors Haijian Si and Stylianos Kavadias, shows how that approach can miss a deeper question of *how* to select: Are the projects being funded still connected to the strategy the company is trying to pursue?

For senior leaders, keeping that connection requires regular attention. It starts with making innovation meetings less about reviewing projects and more about challenging the assumptions behind them.

1. Start with the strategy, not the projects

A regular innovation meeting can provide a useful forum for senior leaders to step back and ask whether the company's strategy is still fit for purpose.

- Is the strategy still working?
- Are leaders confident it can deliver the company's business goals?
- Where are the areas where the strategy may need to be updated or changed? This is where innovation comes in.

These questions may sound basic, but they can expose differences in how leaders understand the company's direction. Senior executives may believe they agree on a strategy while holding different views about its priorities and weaknesses.

That makes the discussion itself important. The objective is to leave the discussion with a shared view of the strategic situation and a clear understanding of where change may be needed.

2. Turn strategic needs into innovation goals

Once the senior management team agrees where strategic vulnerabilities lie, the next step is to translate them into specific innovation goals: change needs or opportunities that improve the organization's position. It is important to note that innovation, in this broad sense, means "changes that are of strategic importance," which includes not just new technology, but also new markets, new processes, new services, new organizational structures or new promotion

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methods. Indeed, in many highly innovative small companies, technologies are bought from the outside but new ways of serving the customer are developed continuously.

A vulnerability might require an innovation response, but so might an opportunity. A promising technology developed by an R&D team, for example, could open up a new market or change how the company operates. Likewise, an opportunity could be addressing a new, yet so far overlooked, group of customers.

Importantly, innovation does not have to start at the top. An idea emerging from somewhere else in the organization can gain enough evidence and support to become a significant management-backed project. In some cases, it may even prompt a change in the broader strategy. This requires the organization to continuously look for new ideas that might eventually improve the strategic position, providing channels where bottom-up ideas can be articulated and brought in front of senior managers.

Innovation goals can also look further into the future. A company might decide that it needs to explore a new business model, identify opportunities outside its current customer segments, introduce AI into important business processes or pursue specific sustainability improvements.

The common requirement is leadership agreement on where opportunities that improve or modify the strategy are welcome. How many innovation goals should there be? Maybe about five, certainly no more than 10 per business unit. If you chase too many changes at once, you will get distracted. Each innovation goal is best supported by a maximum of a handful of innovation projects.

3. Put the innovation portfolio under the microscope

With strategic innovation goals established, managers can turn to the existing innovation portfolio.

The key question is: How well do our current projects support the strategic goals we have identified?

Answering this requires looking across the portfolio rather than evaluating projects one at a time. A project may have an attractive business case but contribute little to the company’s innovation goals (for example, because another project already addresses this). Other

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projects may appear uncertain financially while addressing a critical future need.

The comparison can reveal gaps. Important strategic change goals may have no projects supporting them, while other areas may be duplicating investments.

Decisions to reduce investment in some projects are always difficult, and moreover, the financial indicators supporting these decisions, for example ROI, are often manipulated. The decisions become easier if backed up by an agreement about what strategic changes need to be accomplished.

The important point is that the strategy should shape the portfolio, not the other way round.

4. Don’t let financial numbers run the show

Financial measures still play an important role. Expected revenue, costs, returns and other quantitative indicators can help managers identify projects that are financially unacceptable and provide a useful due-diligence check.

But those numbers are risky to use as the primary way to select innovation projects, as they can be gamed and gradually pull the portfolio away from strategy. Every CFO knows that business cases have many parameters — discount rates, revenue projections or the timing of payments — which can be subtly manipulated in ways that significantly change the overall story.

Projects with the most attractive short-term financial projections may not be the projects that address the company’s most important strategic challenges. Conversely, an initiative aimed at a new market, technology or business model may have limited financial evidence in its early stages.

Treating financial indicators as a supporting check, rather than the final decision-maker, can make the portfolio more robust and effective, as well as reducing the pressure to manipulate assumptions or forecasts.

Toward strategic alignment

These four points provide the keys to a relatively simple framework, even if the decisions remain challenging.

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The result is a different way of thinking about innovation management. Instead of asking only whether individual projects look attractive, leaders ask whether the collection of projects is helping the organization prepare for the future it is trying to create.

That shift, from managing an innovation pipeline to managing a strategically aligned portfolio, may be one of the most important conversations a leadership team can have.

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