The New Competitive Advantage: Creating Shared Value

Professor Michael E. Porter
Harvard Business School

Universidad de Monterrey Visit
Nuevo León, México
October 9, 2012
The Role of Business in Society

• Only business can **create prosperity**

• Healthy businesses need a **healthy community**

• There is an ever **growing awareness** of major societal challenges

• Government and NGO’s **lack sufficient resources and capabilities** to fully meet these challenges

• More of the public sees business as prospering **at the expense** of the society

• Despite growing corporate citizenship activities, the **legitimacy of business** has fallen
The Role of Business in Society
Evolving Approaches

Philanthropy

- Donations to worthy social causes
- Volunteering
The Role of Business in Society
Evolving Approaches

Philanthropy
- Donations to worthy social causes
- Volunteering

Corporate Social Responsibility (CSR)
- Compliance with community standards
- Good corporate citizenship
- “Sustainability”
The Role of Business in Society
Evolving Approaches

- Philanthropy
  - Donations to worthy social causes
  - Volunteering

- Corporate Social Responsibility (CSR)
  - Compliance with community standards
  - Good corporate citizenship
  - “Sustainability”

- Creating Shared Value (CSV)
  - Integrating societal improvement into economic value creation itself
    - Driving social improvement with a business model
What Shared Value is **NOT**

- Sharing the value *already created* (philanthropy)
- Acting based on strong *personal values* and *ethical standards*
- **Balancing** stakeholder interests
- The same as *sustainability*
Moving to Shared Value
Fair Trade

CSR

Fair Trade
• Paying a higher price to farmers
• Certification as a fair trade company
• Higher prices for same products

CSV

Transforming Procurement
• Collaborate with farmers to improve quality and yield
• Supporting investments in technology and inputs
• Higher prices for better quality
• Higher yield increases quantity produced

In both cases, compliance with laws and ethical standards and reducing harm for corporate activities are assumed
Moving to Shared Value in Pharma

Novartis

CSR

- **Donate drugs** to lower-income populations
- **Same products**, but free or at a discounted price
- Reach patients through **existing** health systems
- **Lower revenue** at the same cost

CSV

- Implementing a new drug **business model** for low-income populations (Arogya Parivar)
- New quantity, packaging, patient education, and distribution
- Improvement in local healthcare delivery infrastructure
- Learning about non-traditional customer behavior and new business models
- **Higher revenue** and **profitability**
Business and Society: Why the Disconnect?

- Many companies (and investors) adopted a **narrow model** of economic value creation
  - Meeting **conventional** needs of **conventional** customers
  - Optimizing within **narrow company boundaries**
  - Profit improvement through **outsourcing** and **globalizing**
  - Driving revenue through **acquisitions** instead of new business creation
  - Societal issues are treated as **outside the scope of the business**

- Huge **societal needs** go unmet
- **Growth** and **innovation** suffer
Societal Needs and Economic Value Creation

- **Social** deficits create **economic** cost
- "**Externalities**" shape **internal** company productivity
- Social needs represent the **largest market opportunities**
Levels of Shared Value

I: Reconceiving **products**, **needs**, and **customers**
   - Meeting **societal needs** through products, and reaching **unserved** or **underserved customers** with these products

II: **Redefining productivity** in the value chain
   - **Using resources better** across the value chain to improve fundamental productivity

III: Enabling **local cluster development**
   - Improving **available skills**, **suppliers**, and **supporting institutions** in the communities in which a company operates to increase productivity, innovation, and growth
Reconceiving Products and Markets

• Design products and services to **address societal needs**
  – E.g., environmental impact, safety, health, education, nutrition, living with disability, housing, financial security

• Open **new markets** by serving unmet needs in underserved communities
  – Often requires **redesigned products** or different **distribution methods**

• Businesses have the potential to be more effective than governments and NGOs in **creating** and **marketing** solutions to community problems

• New needs and new markets open up opportunities to **differentiate**, **innovate**, and **grow**

• A new generation of **social entrepreneurs** is capturing these opportunities, often faster than mainstream businesses
Creating Shared Value in Products

**Intuit SnapTax**

**SnapTax** provides low-income consumers with access to tax preparation services over the phone and enables rapid refunds:

- **15 minutes for $15**, electronic filing included

- Data extracted from **mobile phone photos** of W-2s via optical character recognition

- **Debit card** option for direct deposit of refunds for unbanked households

- **Simple IRA option** to enable use of refund for retirement savings
Creating Shared Value in Products and Markets

Novo Nordisk in China

• **Product design** that reflects Chinese patient demographics and culture

• **Diabetes training programs for physicians** in partnership with government, NGOs, and opinion leaders to promote the latest thinking on diabetes prevention, screening, treatment, and patient communication
  – The program has trained 55,000 physicians to date, each treating approximately 230 patients

• New types of **diabetes education programs for patients** focusing on prevention, lifestyle changes, and effective use of insulin products

• Novo’s market share in China increased from **0% to 63%**, and China became the company’s third largest market with revenues of $935 million in 2011
Discovering Opportunities to Create Shared Value in Products and Markets

• Redefine the business around **unsolved customer problems or concerns**, not traditional product definitions

• Think in terms of **improving lives**, not just meeting customer needs

• Identify customer groups that have been **poorly served** or **overlooked** by the industry’s products

• Start with **no preconceived constraints** about product attributes, channel configuration, or the economic model of the business (e.g., small loans are unprofitable)

• Opens up **new opportunities** for customer segmentation and marketing
Redefining Productivity in the Value Chain

- Shared value purchasing
- Energy use
- Resource use

- Location of facilities / supply chain
- Logistical efficiency
- Training to enhance the productivity and wages of employees, especially lower income employees
Identifying Opportunities for Shared Value in the Value Chain

**Mining**

- Enhancing skill training and technology partnerships with local colleges and universities
- Value added purchasing practices with suppliers
- Local supplier development

- Energy and water use
- Limiting emissions and waste
- Low ecological and biodiversity impacts
- Minimizing use and effects of hazardous materials
- Recovering additional materials from “exhausted” mines
- Worker safety practices

- Recruiting from disadvantaged surrounding communities
- Diversity in the workforce
- Employee education and job training
- Onsite housing
- Employee health initiatives
- Compensation and benefit models to support a living wage
- Staff retraining and rehabilitation after mine closures

- Minimizing logistical and handling impacts
Improving the Business Environment in the Company’s Major Locations

• A strong local cluster improves company productivity and growth
  – Local suppliers and service providers
  – Supporting institutions and infrastructure
  – Related businesses

• Companies, working collaboratively, can catalyze major improvements in the cluster and the local business environment

• Local cluster development strengthens the link between a company’s success and community success
What is a Cluster?
Tourism Cluster in Cairns, Australia

Public Relations & Market Research Services

Food Suppliers

Property Services

Maintenance Services

Travel Agents

Tour Operators

Hotels

Attractions and Activities
e.g., theme parks, casinos, sports

Restaurants

Airlines, Cruise Ships

Local Retail, Health Care, and Other Services

Local Transportation

Souvenirs, Duty Free

Banks, Foreign Exchange

Government Agencies
e.g., Australian Tourism Commission, Great Barrier Reef Authority

Educational Institutions
e.g., James Cook University, Cairns College of TAFE

Industry Groups
e.g., Queensland Tourism Industry Council

Sources: HBS student team research (2003) - Peter Tynan, Chai McConnell, Alexandra West, Jean Hayden

Copyright 2012 © Professor Michael E. Porter
Local Cluster Development
Anglo-American

• Anglo American has established Anglo Zimele, a South African enterprise investment fund, for mining-related small and medium-sized businesses in South Africa

• As of 2010, the fund had invested in 509 businesses, which collectively employed 9,514 people with annual revenues of $215 million

Economic value
• Anglo-American has created reliable, high-quality local suppliers

• Local suppliers reduce costs and can improve service levels and product tailoring

Community value
• 10,000 new jobs created

• Significant increase in income for SME employees and owners

• Spillover effects of these new businesses on their communities
Creating Shared Value: Deciding Where to Concentrate

Nestlé

- Opportunities to create shared value are **inevitably tied closely** to a company’s particular businesses
Measuring Shared Value

• Measure the **direct link** between social impact and economic impact
  – Line of sight

• Measures **unique** to the type of shared value being created

• **Intentional** and **focused**

---

**Shared Value Measurement in Action**

• **Intel** measured the impact of its technology on student performance in its **Education Transformation Strategy**

• The company achieved **market leadership** in the growing global market for mobile computing for K-12 education
### New Stakeholder Roles and Relationships

- Shared value thinking is driving **new relationships** between companies, philanthropists, NGOs, and government in addressing social issues

<table>
<thead>
<tr>
<th>Traditional Roles</th>
<th>New Roles</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Philanthropists</strong></td>
<td>• Donate to charitable causes</td>
</tr>
<tr>
<td>• Receive grants to provide social services</td>
<td>• Partner with companies and NGOs to catalyze shared value initiatives</td>
</tr>
<tr>
<td><strong>NGOs</strong></td>
<td>• Enable implementation of new shared value business models</td>
</tr>
<tr>
<td><strong>Governments</strong></td>
<td>• Partner with companies and NGOs to make platform investments and support shared value strategies</td>
</tr>
<tr>
<td>• Tax business and regulate business practices; operate social programs</td>
<td>• Partner with NGOs and government to initiate and scale shared value strategies</td>
</tr>
<tr>
<td><strong>Companies</strong></td>
<td>• Donate to charitable causes or operate ESG programs</td>
</tr>
</tbody>
</table>

*Source: Copyright 2012 © Professor Michael E. Porter*
Adding a Social Dimension to Strategy

• Shared value opens up new **needs**, new **markets**, new **value chain configurations**, and new **ways of thinking** about the business

• This creates new opportunities for **strategic positioning** and new **competitive advantages**

• Companies should incorporate a **social dimension** in their value proposition

• Adding social dimensions makes strategy more **sustainable vs. competitors** than conventional cost and quality advantages
Shared Value and Strategy
Whole Foods Markets

**Value Proposition**

- Natural, fresh, organic, and prepared foods and health items with excellent service at premium prices
- Cater to specialized nutritional requirements (gluten allergies, vegan, etc.)
- Educated, middle class, and affluent customers who are passionate about food and a healthy lifestyle

**Distinctive Activities**

- Well-lit, inviting supermarket store formats with appealing displays and extensive prepared foods sections
- Produce section as “theater”
- Café-style seating areas with wireless internet for meals and meetings
- Each store carries local produce and has the authority to contract with the local farmers. Company provides low-interest loans if needed
- Nutrition information and education provided to shoppers along with products
- High touch in-store customer service via knowledgeable, flexible, and highly motivated personnel
- Flat compensation structure
- Own seafood procurement and processing facilities to control quality, sustainability and price from the boat to the counter
- Heavy emphasis on environmental sustainability in all activities
- Emphasis on supporting community development

- Whole Foods is the most **economically successful** food retailer in North America
- Successful strategies in the future will embody a significant **shared value dimension**
## Purpose Based Strategic Positioning

<table>
<thead>
<tr>
<th>Traditional Positioning</th>
<th>New Positioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nestlé</td>
<td>• Nutrition</td>
</tr>
<tr>
<td>• Food</td>
<td></td>
</tr>
<tr>
<td>Nike</td>
<td>• Health and Wellness</td>
</tr>
<tr>
<td>• Shoes</td>
<td></td>
</tr>
<tr>
<td>Thermo Fisher</td>
<td>• Making the World Healthier, Cleaner, and Safer</td>
</tr>
<tr>
<td>• Leader in Serving</td>
<td></td>
</tr>
<tr>
<td>Science</td>
<td></td>
</tr>
</tbody>
</table>

A **broader sense of purpose** not only opens up **new opportunities** for growth and profitability, but also **motivates** and **attracts** employees, consumers, business partners, shareholders, and the public.
The Purpose of Business

• There is an opportunity to **transform thinking and practice** about the role of the corporation in society

• Shared value gives rise to **far broader opportunities** for economic value creation than conventional management thinking

• Shared value thinking will drive the next wave of **innovation, productivity**, and **economic growth**

• Shared value will give rise to a new generation of **management** thinking

• Businesses **acting as businesses**, not as charitable givers, are arguably the most powerful force for addressing many of the pressing issues facing our society

• A transformation of business practice around shared value will give **purpose** to the corporation and represents our best chance to **legitimize business again**