The Role of Corporations in Society: Creating Shared Value

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The Role of Business in Society

• Only business can **create wealth** and **prosperity**

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

• Business is facing **growing scrutiny** as the cause or a contributor to many of these problems

• Corporate social responsibility efforts are greater than ever, but the **legitimacy of business has fallen**

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

• These challenges are often the **most acute** in developing countries

We need a **new approach**
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”
- Mitigate risk and harm
The Role of Business in Society
Evolving Approaches

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Creating Shared Value (CSV)
- Integrating social needs and challenges into economic value creation itself

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What is Shared Value?

Creating Shared Value:
Addressing a social issue with a business model
What is Shared Value?

Creating Shared Value:

Addressing a social issue with a business model

Social value + Economic value
CSR versus Shared Value

Fair Trade

CSR

- Paying a **higher price** to farmers for the same products
- **Certification** as a fair trade company

Transforming Procurement

CSV

- Collaborate with farmers to **improve quality and yield**
- Supporting investments in **technology** and **inputs**
- Higher prices for **better quality**
- Higher yield increases **quantity** produced
Social Needs and Economic Value Creation

- Social deficits create economic costs
- “Externalities” affect internal company productivity
- Social needs represent the largest market opportunities
Levels of Shared Value

I. Reconceiving needs, products, and customers
   – Meeting societal needs through products
   – Addressing unserved or underserved customers

II. Redefining productivity in the value chain
   – Using resources, energy suppliers, logistics, and employees more productively

III. Improving the local and regional business environment
   – Improving the skills, supplier base, regulatory environment, and supporting institutions in the communities and regions in which a company operates
   – Local cluster development that also improves company productivity
Creating Shared Value in Products and Markets

Jain Irrigation Systems

- **Drip irrigation equipment** for small farmers in Africa and India
- Serves **more than 4 million farmers** worldwide as of 2012
- Reduces **water use** by over 40%
- Enables **higher crop yields** that improve food security while raising farmers’ income
- Jain has built a **$820 million** business that is rapidly growing
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
Redefining Productivity in the Value Chain

- Purchasing that enhances supplier capabilities and efficiency
- Improving energy, water and resource efficiency
- Minimizing logistical intensity
- Improving employee health and safety

- Enhancing the productivity and wages of lower income employees
- Recruiting that represents the diversity of customers and the communities where a company operates
Shared Value in the Value Chain
Fibria, Brazil

• Fibria, a large manufacturer of pulp for paper, utilizes planted eucalyptus trees rather than native and old growth forests

• The company also encourages small-scale producers near its mills to plant eucalyptus in conjunction with other crops, assisting them with technical training and inputs

• Fibria achieves far greater resource efficiency versus old growth forest production, with eucalyptus yielding 30 times higher yield per acre of wood pulp

• Small scale producers contribute 27% of the raw material volume utilized in Fibria mills, improving efficiency

• 4000 households have significantly increased their income
Identifying Opportunities for Shared Value in the Value Chain

Mining

- Enhancing skill training partnerships with local colleges and universities
- Qualifying local suppliers and value added purchasing practices with suppliers
- Recruiting from disadvantaged surrounding communities
- Employee education and job training
- Enabling nearby family housing
- Employee health initiatives

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

- Minimizing logistical and handling impacts
Improving the Local and Regional Business Environment

• Companies, working individually and collaboratively, can catalyze major improvements in the local business environment where they have major operations

• Improving the business environment enhances company productivity while improving economic development in the community and region
Skill and Supplier Development
Rio Tinto, Canada

Rio Tinto’s Diavik Diamond mine has helped create a variety of community based training partnerships with communities, contractors, governments and educational institutions in remote Northern Canada.

- **Education:** Promotes careers in diamond mining. Offers apprenticeships that employ and train students.

- **Worker training:** Partners with communities, colleges and government to train workers in mining related activities.

- **Supplier development:** Sources local inputs and capacity building for local providers of goods and services.

- Rio Tinto hires *62% of its employees locally*.

- The company sources *71% of goods and services locally*.
Improving the Quality of the Business Environment

Context for Firm Strategy and Rivalry

• Local rules and incentives that encourage investment and productivity
  – e.g. incentives for capital investments, IP protection, corporate governance standards

• Open and vigorous local competition
  – Openness to foreign competition
  – Strict competition laws

Demand Conditions

• Sophisticated and demanding local customers and needs
  – e.g., Strict quality, safety, and environmental standards
  – Consumer protection laws

Factor (Input) Conditions

• Access to high quality business inputs
  – Human resources
  – Capital availability
  – Physical infrastructure
  – Administrative infrastructure (e.g., business registration, permitting, transparency)
  – Scientific and technological infrastructure

Related and Supporting Industries

• Availability and depth of suppliers and supporting industries
  – Quality of collaboration organizations (e.g., trade associations)

Many things matter for competitiveness

Successful economic development is a process of successive upgrading, in which the business environment improves to enable increasingly sophisticated ways of competing.
Building Clusters
Tourism in Cairns, Australia

- Public Relations & Market Research Services
- Food Suppliers
- Property Services
- Maintenance Services
- Travel Agents
- Tour Operators
- Hotels
- Restaurants
- Attractions and Activities e.g., theme parks, casinos, sports
- 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
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.
Cluster Development: Upgrading Channels
Arca Continental

- Arca Continental is the **second largest bottling company** in Latin America, and one of the largest Coca-Cola bottlers in the world

- Arca Continental established a program to train and invest in the **micro-entrepreneur retailers** who sell more than 60% of the Company’s products, including management, sales and marketing and merchandising

- Invests in **low energy use coolers and fixture improvements**

- Participating retailers register **sales increases of 25%** or more, with improved customer satisfaction, leading to similar **increases in the sales of Arca’s products**

- Arca Continental **recovers its investment** in 6 months or less

- Beginning in **Mexico**, the program is being extended to **Argentina** and **Ecuador**
Creating Shared Value: Deciding Where to Concentrate

Nestlé

- Opportunities to create shared value are inevitably tied closely to a company’s particular businesses.
Putting Shared Value Into Practice
Dow Chemical

• Dow has a legacy of innovation to solve problems ("solutionism")
• The company recognized that global social issues represent huge market opportunities
• It created the “Breakthroughs to World Challenges” Program
  – Each business unit is challenged to apply “solutionism” to a range of global problems inspired by the MDGs

Example

• Dow developed Omega-9 canola and sunflower seeds that produce cooking oil with no trans fats and low saturated fats
• The technology yields twice the oil per hectare for farmers than soybeans
• The oils have longer shelf life and usage life for food processors

• One of Dow’s biggest selling product lines with total revenues of approximately $700 million
Partnering for Shared Value

**NGOs**
- Hold business accountable
- Seek donations

**Government**
- Regulate how businesses operate
- Operate social programs
- Tax businesses

**Foundations**
- Donate to charitable causes

**Competitors**
- “Brand” social initiatives

- Partner with business to implement and **scale** shared value solutions
- Regulate to **encourage** market solutions
- **Partner** to deliver shared value solutions to social services
- **Jumpstart market solutions** through minimum purchases or subsidies
- Invest in **infrastructure** to enable shared value approaches (e.g. roads, skills)
- Invest **with** companies, NGOs and government to enable shared value solutions
- **Partner** on business environment improvements
## Shared Value and Company Strategy

### Whole Foods Markets

<table>
<thead>
<tr>
<th>Value Proposition</th>
<th>Distinctive Activities</th>
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</thead>
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| • Natural, fresh, organic, and freshly prepared foods and health items with excellent service at premium prices  
• Cater to specialized nutritional requirements (gluten allergies, vegan, etc.)  
• Serve educated customers who are passionate about food and a healthy lifestyle | • 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**
### From Product to Purpose

<table>
<thead>
<tr>
<th>Traditional Positioning</th>
<th>New Positioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nestlé</td>
<td>• Nutrition Company</td>
</tr>
<tr>
<td>• Food and Beverage Company</td>
<td></td>
</tr>
<tr>
<td>Nike</td>
<td>• Health and Fitness Company</td>
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<tr>
<td>• Footwear Company</td>
<td></td>
</tr>
<tr>
<td>Thermo Fisher</td>
<td>• Making the World Healthier, Cleaner, and Safer</td>
</tr>
<tr>
<td>• Scientific and Laboratory Instruments Company</td>
<td></td>
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</tbody>
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- A **broader sense of social purpose** opens up **new opportunities** for growth and profitability, while **motivating** and **attracting** employees, consumers, business partners, shareholders, and the public.
Redefining Corporate Purpose
Danone

- Danone realized that it had drifted away from its origins as a manufacturer of **healthy foods**
- **Sold off** its beer, meat and cheese units
- Refocused the company on **dairy** and **water**
- Acquired **medical nutrition** and **baby foods** businesses
- Created **Innovation Committees** in business units to provide “healthy food for as many people as possible”

**Vision**

*The ‘dual economic and social’ project, creating economic value by creating social value*

**Mission**

*Bringing health through food to as many people as possible by refocusing on four complementary business lines and expanding into fast-growing new regions*
Creating Shared Value: Opportunities for Pacific Rubiales

- **Redefining productivity** in the value chain
  - Recruiting and workforce development
  - Energy efficiency and waste reduction
  - Water optimization for irrigation

- Enabling **local cluster development** and participating in national and regional **competitiveness initiatives**
  - Create a local supplier base
  - Spur community infrastructure development
  - Build the oil and gas cluster in the region
  - Spur development of other clusters in the region
  - Provide training to government officials on infrastructure investment and regulatory
  - Reactivate the Regional Competitiveness Commission by increasing private sector participation
What is Competitiveness?

A nation or region is competitive to the extent that firms operating there are able to compete successfully in the global economy while supporting rising wages and living standards for the average citizen.

- Competitiveness depends on the long term productivity with which a nation or region uses its human, capital, and natural resources.
  - Productivity sets sustainable wages, job growth, and standard of living.
  - It is not what industries a nation or region competes in that matters for prosperity, but how productively it competes in those industries.
  - Productivity in a national or regional economy benefits from a combination of domestic and foreign firms.

- Nations and regions compete to offer a more productive environment for business.
- Competitiveness is not a zero sum game.
Regional Competitiveness and Economic Prosperity

• Economic performance *varies significantly* across sub-national regions (e.g., provinces, states, metropolitan areas)
Prosperity of Mexican States

Mexico Real Growth Rate of GDP per Capita: 1.36%

Mexico GDP per Capita: $77,212

Gross Domestic Product per Capita, 2010 (in constant 2003 Mexican Pesos)

Source: INEGI. Sistema de Cuentas Nacionales de México.
Regional Competitiveness and Economic Prosperity

• Economic performance *varies significantly across* sub-national regions (e.g., provinces, states, metropolitan areas)

• Many essential levers of competitiveness reside at the *regional level*

• Regions *specialize* in different sets of clusters
Traded Cluster Composition of the Puebla Economy

Overall change in the Puebla Share of Mexican Traded Employment: +0.09%

Puebla Overall Share of Mexican Traded Employment: 4.20%

Education and Knowledge Creation
Distribution Services
Heavy Machinery
Chemical Products
Furniture
Processed Food
Forest Products
Building Fixtures, Equipment and Services
Automotive
Leather and Related Products
Information Technology
Construction Materials

Employees 5,000 =


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Regional Competitiveness and Economic Prosperity

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- Regions are ultimately the **most important unit** in competitiveness
- Each region needs its own distinctive **strategy and action agenda**
  - Business environment improvement
  - Cluster upgrading
Clusters as a Tool for Competitiveness Policy

• A forum for collaboration between the private sector, trade associations, government, educational, and research institutions

• Brings together firms of all sizes, including SME’s

• Creates a mechanism for constructive business-government dialog

• A tool to identify problems and action recommendations

• A vehicle for investments that strengthen multiple firms/institutions simultaneously

• Fosters greater competition rather than distorting the market

• Enhances the efficiency and effectiveness of traditional economic policy areas, such as training, R&D, export promotion, FDI attraction, etc.
Creating a Regional Economic Strategy

Regional Value Proposition

- What is the **distinctive competitive position** of a geographic area given its location, legacy, existing strengths, and potential strengths?
  - What unique advantage as a business location?
  - For what types of activities and clusters?
  - And what roles with the surrounding regions, nation, and the broader world?

Developing Unique Strengths

- What **elements of the business environment** can be unique strengths relative to peers/neighbors?
- What **existing and emerging clusters** can be built upon?

Achieving and Maintaining Parity with Peers

- What **weaknesses** must be addressed to remove key constraints and achieve parity with peer locations?

- **Priorities and sequencing** are necessity in economic development
Transforming The New Process of Economic Development

Competitiveness is the result of both **top-down** and **bottom-up processes** in which many companies and institutions take responsibility.

**Old Model**
- **Government** drives economic development through policy decisions and incentives

**New Model**
- Economic development is a **collaborative process** involving government at multiple levels, companies, teaching and research institutions, and private sector organizations.
The Purpose of Business

• Our purpose in business is to **create shared value for society**, not economic value for its own sake

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

• Shared value will give rise to **far broader opportunities** for economic value creation

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

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