

The New Competitive Advantage: Creating Shared Value

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This presentation draws on ideas from Professor Porter's books and articles, in particular, *Competitive Strategy* (The Free Press, 1980); *Competitive Advantage* (The Free Press, 1985); "What is Strategy?" (*Harvard Business Review*, Nov/Dec 1996); and *On Competition* (*Harvard Business Review*, 2008). No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means—electronic, mechanical, photocopying, recording, or otherwise—without the permission of Michael E. Porter. Additional information may be found at the website of the Institute for Strategy and Competitiveness, www.isc.hbs.edu.

The Role of Business in Prosperity

- Only business can **create prosperity**

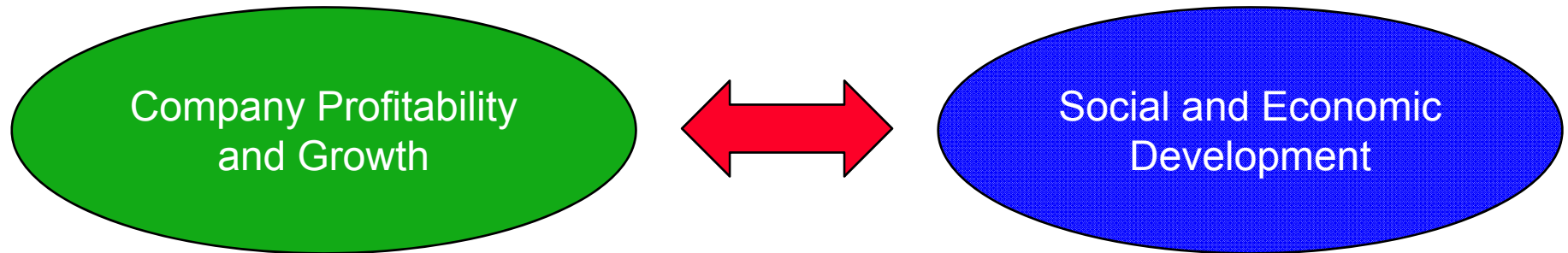
BUT

- Companies are increasingly perceived to be prospering **at the expense of the broader community**
- Business increasingly is seen as **a major cause of social, environmental, and economic problems**
- Government and civil society often attempt to address societal issues **at the expense of business**



- The **legitimacy of business** has fallen

Business and Society: Why the Disconnect?

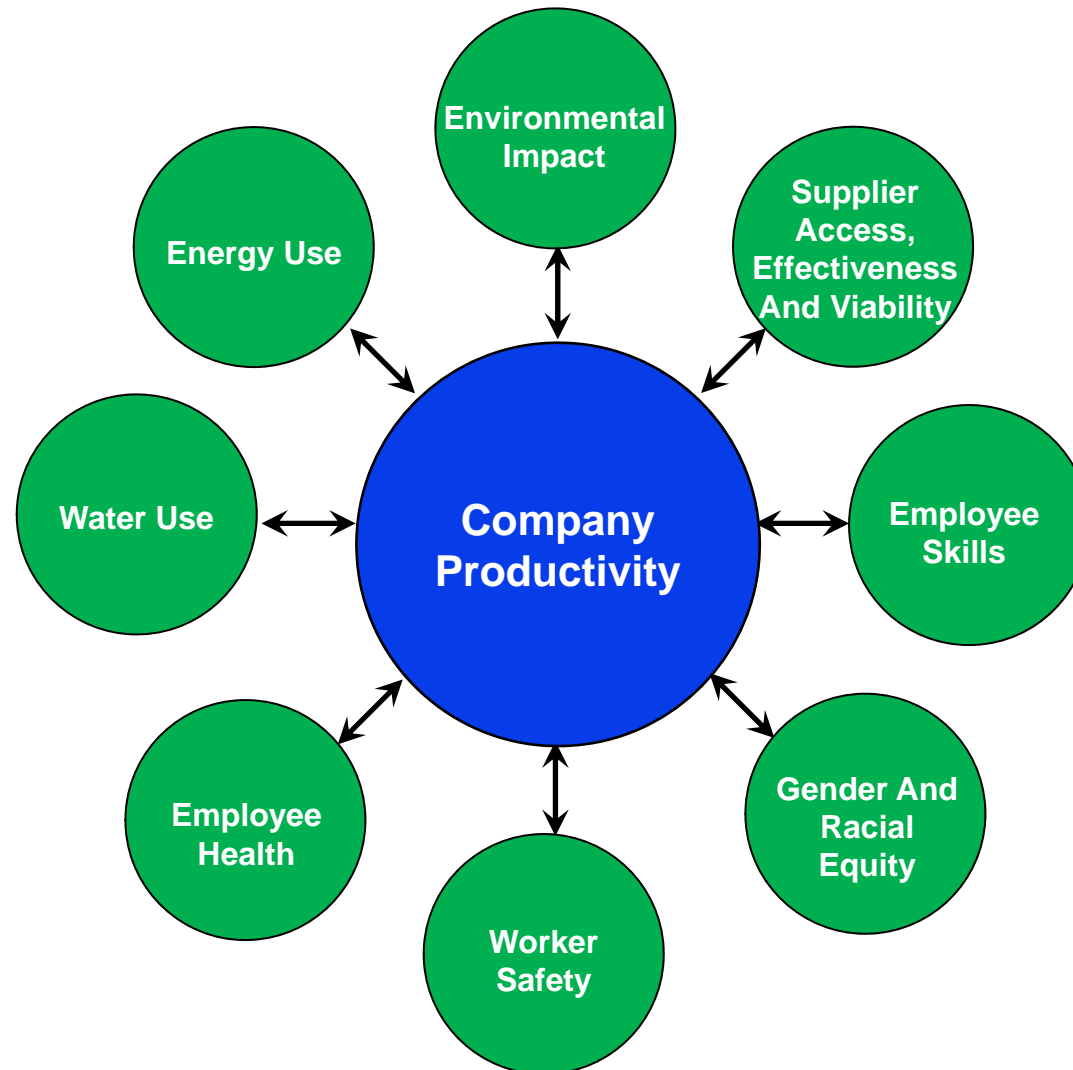


- Companies have adopted a **narrow model** of economic value creation
 - Meeting **conventional** needs of **conventional** customers
 - Driving revenue through **acquisitions** instead of new expansion
 - Profit improvement through **downsizing, outsourcing, relocating**, and **globalizing**
 - Shortening **time horizons**
 - Societal issues are treated as **outside** the scope of business



- Huge **societal needs** go unmet
- **Growth** and **innovation** in business have suffered

Creating Economic Value and Societal Needs



- **Social** deficits create **economic** cost
- **External** conditions shape **internal** company productivity
- There is a growing **congruence** between economic value creation and societal objectives

The Concept of Shared Value

Shared Value: Corporate policies and practices that **enhance competitiveness** of a company while simultaneously **advancing social and economic conditions** in the communities in which it operates

- Create **economic value** by creating **societal value**
 - What is good for the community is good for business
- All profit is **not equal**. Profit involving shared value enables society to advance more rapidly and allows companies to grow faster



- Shared value represents the next evolution of **capitalism**
- Concern with **societal issues** will be a defining characteristic of the post-crisis era
- Incorporating societal issues into strategy and operations is **the next major transformation** in management thinking

Levels of Shared Value

- Reconceiving customer **needs, products, and markets**
- **Redefining productivity** in the value chain
- Enabling **local cluster development**

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**



- Business can be more effective than governments and NGOs in **marketing** solutions to social problems
- New opportunities for **differentiation, innovation, and growth**
- A new generation of **social entrepreneurs** is capturing these opportunities, often faster than mainstream businesses

Creating Shared Value in Products

Intuit

- **Intuit Health Debit Card** allows small employers who cannot afford health insurance to provide pre-tax healthcare support to their employees
 - Card automatically recognizes healthcare expenditures vs. other kinds of spending
 - Unspent funds roll over year to year
- **SnapTax** provides low-income consumers with access to tax preparation services over the phone and 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

Finding Product and Market Opportunities to Create Shared Value

- Redefine the business around **unsolved customer problems**, not traditional product definitions
- Think in terms of **improving lives**, not just meeting consumer needs
- Identify customer groups that have been **poorly served** or **ignored** 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)

Creating Shared Value in Products and Markets

Novo Nordisk in China

Physician Training

- Diabetes training programs with governments, NGOs, and opinion leaders to promote the latest thinking among physicians on diabetes prevention, screening, treatment, and patient communication
- Targeting smaller cities
- 220,000 program sessions to date

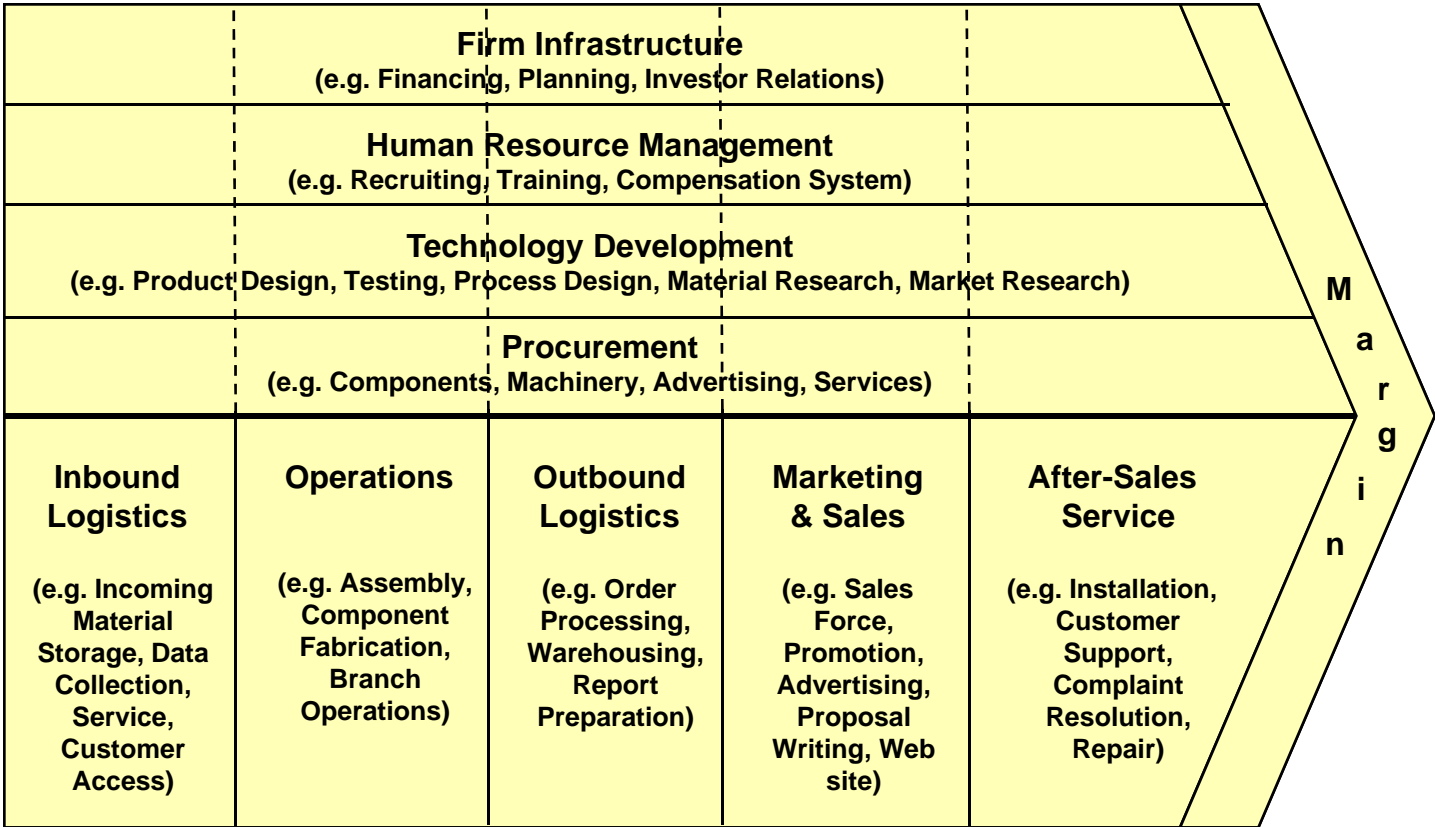
Patient Education

- “Diabetes bus” program to raise awareness and provide on-site advice. NovoCare telephone hotline allows patients to reach specialists with questions. NovoCare Club provides ongoing updates to members.
- Patient education focuses on prevention, lifestyle changes, and effective use of insulin products
- 280,000 patients educated to date



- Since 1997, this new approach to product delivery is estimated to have reduced healthcare costs in China by \$700 million by reducing diabetes related complications, while increasing Novo Nordisk sales by over \$100 million.

Redefining Productivity in the Value Chain

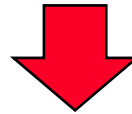


- Resource use
- Energy use
- Logistical efficiency
- Employee productivity
- Location of facilities and the supply chain

Redefining Productivity in the Value Chain

TerraCycle (Trenton, NJ)

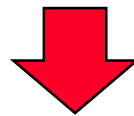
- Manufactures eco-friendly consumer products from otherwise unrecyclable materials. Offers over 1,500 products ranging from recycled park benches to upcycled backpacks at major retailers like Walmart and Whole Foods.
- Produces products in a way that has benefits for the environment and the company through lower energy costs (e.g., TerraCycle pencil case produces 80% less carbon during the manufacturing process than a standard cotton pencil case)
- Business has grown to 75 employees and \$7.6 million in revenue



- Has created a national recycling movement with more than 19 million people collecting waste in 11 countries at over 70,000 locations
- Exposed millions of children to the concept of recycling, promoting awareness at an early age
- Has diverted nearly 2 billion pieces of garbage from landfills and incinerators

Local Cluster Development

- A strong local cluster with capable local suppliers and institutions **improves company productivity**
 - e.g., greater supply chain efficiency, lower environmental impact, and better access to skills
- **Companies**, working collaboratively, can catalyze major improvements in the local cluster and business environment
- Local cluster development **strengthens the link** between a company's success and community success



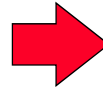
- What suppliers are **inefficient** or **missing locally**?
- What **local deficits** or **institutional weaknesses** create internal costs for the firm?

Local Cluster Development

Consumer's Choice Coffee (Louisville, KY)

- Manufactures and wholesales specialty coffee and other beverages
- Located in an industrial park in the economically disadvantaged Park Hill Corridor of Louisville, with direct access to the freeway and proximity to the airport and UPS shipping facility
- Started the Park Hill Business Association (PHBA) to draw other manufacturers, suppliers, and distribution firms to the area, now with 45 members
- PHBA businesses have pooled their resources to address security concerns; shaped a long-term strategic plan for regional transportation; and leveraged their influence to attract green infrastructural improvements to the area
- The “one stop shop” of multiple food service companies in business park has created an increased customer base
- Consumer's Choice has grown to 30 employees and \$10 million in revenue
- The food cluster has created 104 new jobs in the area with average annual salaries of \$43,710
- 13 active food and beverage processing projects in the pipeline that could create 397 more jobs and a combined capital investment of \$21.3 million

Moving to Shared Value



- **Values:** “doing good”
- Good citizenship, philanthropy, and sustainability
- **Discretionary**
- **Separate** from profit maximization
- Agenda **externally determined**
- Impact is **limited** by the corporate footprint and CSR budget

• Example: Fair trade purchasing

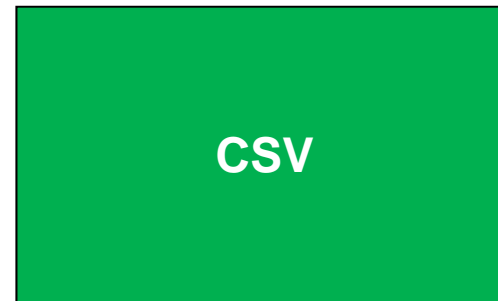
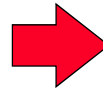
- **Value:** economic and societal benefits relative to cost
- **Joint** company and community value creation
- Part of **competing**
- **Essential** to profit maximization
- Agenda is **business specific**
- Mobilizes the **entire company** budget

• Example: Transforming procurement to increase quality and yield

In both cases, **compliance** with laws and ethical standards and reducing harm for corporate activities are **assumed**

Moving to Shared Value

Novartis



- Donate drugs to lower-income populations
- Same products, but free or at a discounted price
- Provides product access for affected individuals



- Reduced revenue at the same cost

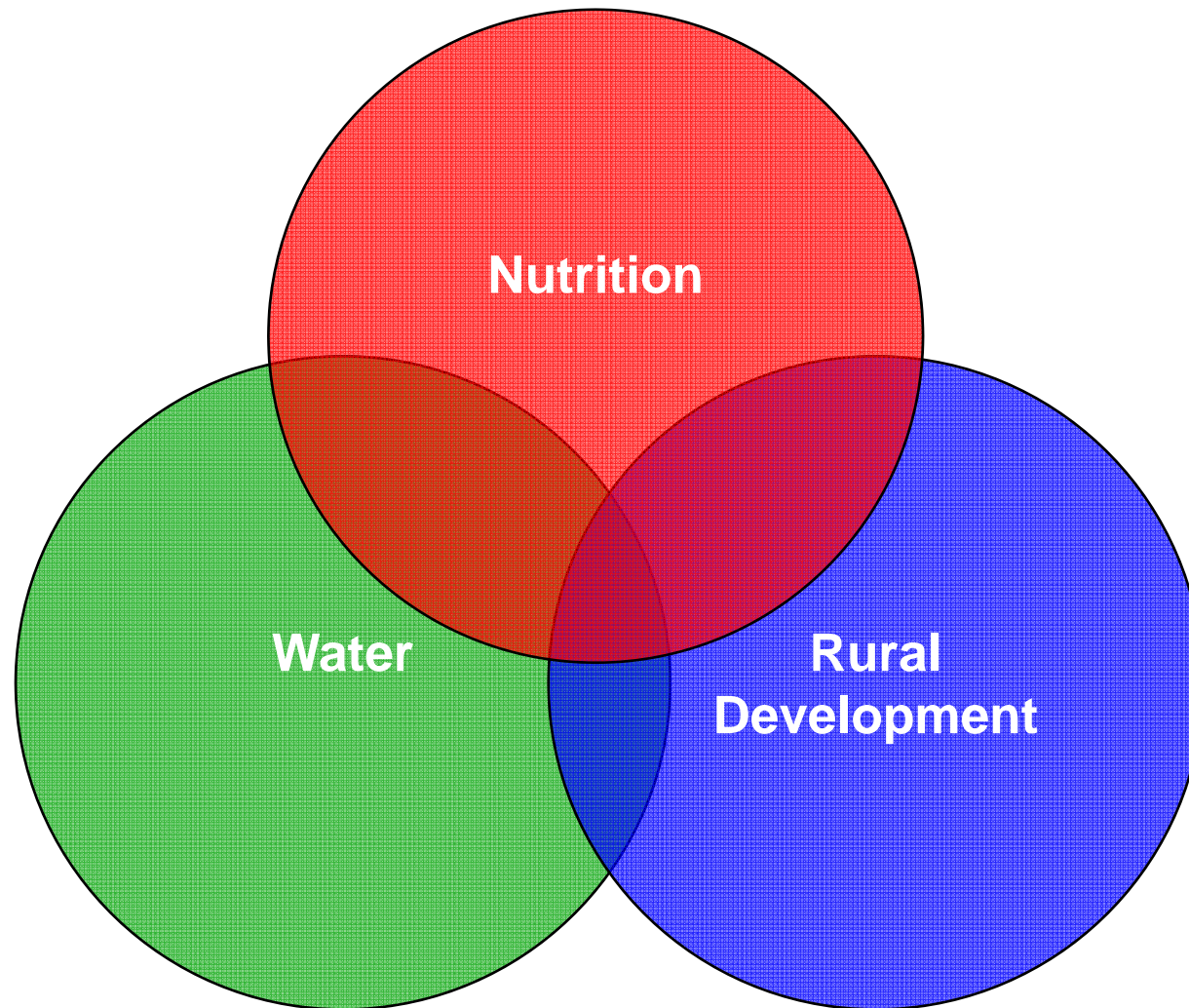
- Arogya Parivar: Implementing a new drug distribution channel for low-income populations
- New quantity, packaging, patient education, and distribution
- Improvement in local healthcare delivery infrastructure
- Learning about customer behavior and new business models



- Expanded revenue and profitable business model

Creating Shared Value: Deciding Where to Concentrate

Nestlé



- Opportunities to create shared value are inevitably **tied closely** to a company's particular businesses

Creating Shared Value

Nestle Nespresso

Implementing shared value in sourcing premium coffees from farmers in Costa Rica, Guatemala, Colombia, and Ghana

- Reconfiguring the value chain
 - Reconceiving **procurement**
- Upgrading the cluster
 - Supporting local **cluster development** in coffee growing regions, including establishment of cluster institutions
 - **Partnering** with stakeholders

Shared Value		
<u>Farmers</u>	<u>Community</u>	<u>Nespresso</u>
→ Better yields	→ Environmental sustainability	→ Stable supply
→ Better prices	→ Economic development	→ Better quality
→ Better processing		→ Reinforces strategic positioning

Adding a Social Dimension to Strategy

- Shared value opens up new **needs**, new **markets**, and new **value chain configurations**
- This creates **new strategic positions**, and new opportunities for **extending existing positioning**



- Companies should incorporate a **social dimension** to their value proposition
- Shared value can **reinforce** and even **anchor** a company's strategy
- The social dimension of strategy can be **more sustainable vs. competitors** than conventional cost and quality advantages

Shared Value and Strategic Positioning

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 and microcredit if needed
- 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 (and price) from the boat to the counter
- Heavy emphasis on environmental sustainability in all activities.
- Emphasis on supporting community development



- Successful strategies in the future will embody a significant **shared value dimension**

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 approaches** to economic value creation
- Shared value thinking will drive the next wave of **innovation, productivity enhancement, and economic growth**
- 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**