

The Competitive Advantage of Nations, States and Regions

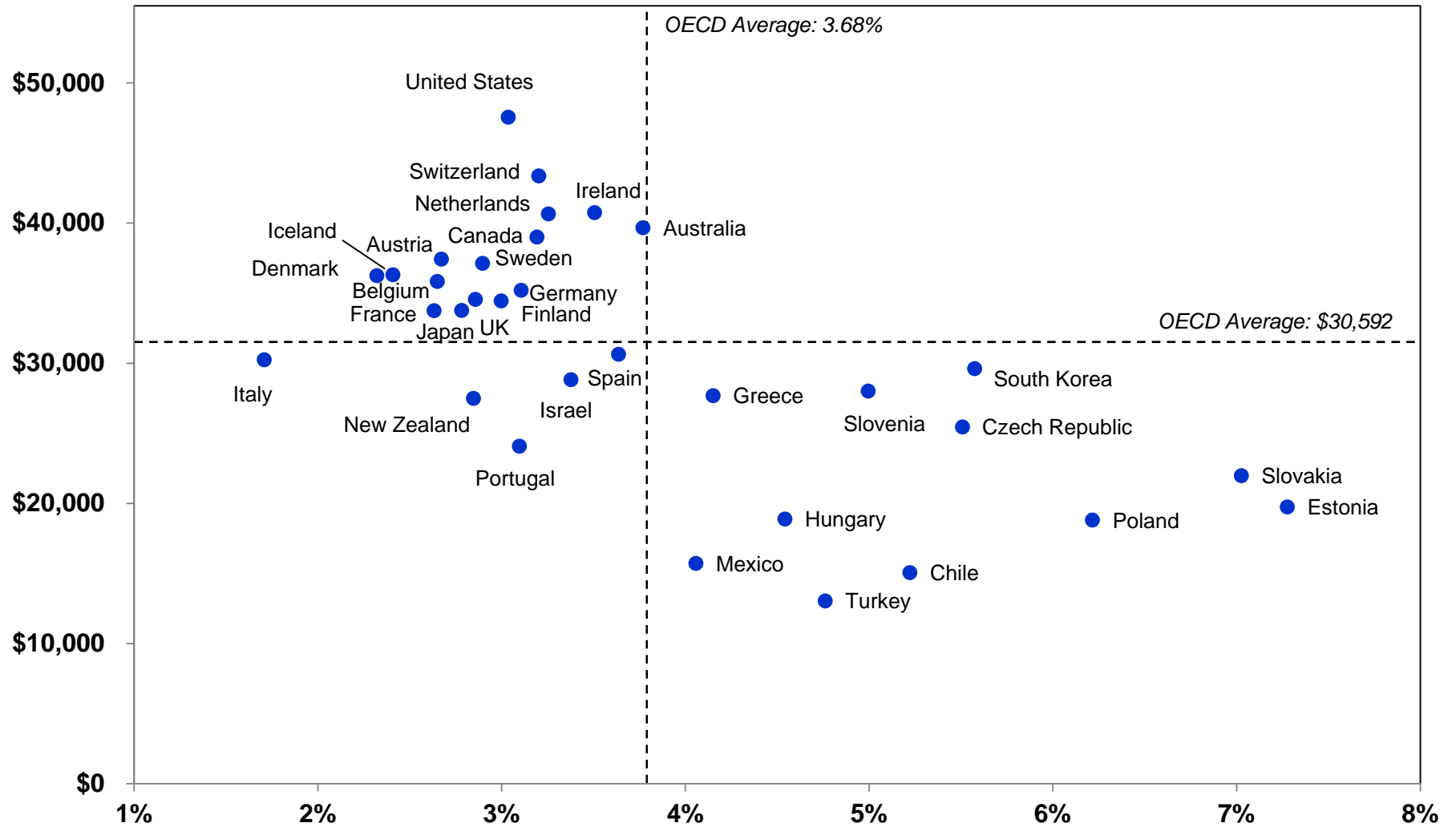
Professor Michael E. Porter
Harvard Business School

*National Council of Professors
Kuala Lumpur, Malaysia
July 7, 2011*

This presentation draws on ideas from Professor Porter's articles and books, in particular, *The Competitive Advantage of Nations* (The Free Press, 1990), "Building the Microeconomic Foundations of Competitiveness," in *The Global Competitiveness Report* (World Economic Forum), "Clusters and the New Competitive Agenda for Companies and Governments" in *On Competition* (Harvard Business School Press, 2008), and ongoing research on clusters and competitiveness. 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. Further information on Professor Porter's work and the Institute for Strategy and Competitiveness is available at www.isc.hbs.edu

Prosperity Performance OECD Countries

PPP-adjusted GDP per
Capita, 2010 (\$USD)



Note: Luxembourg Excluded

Growth of Real GDP per Capita (PPP-adjusted), CAGR, 2000-2010

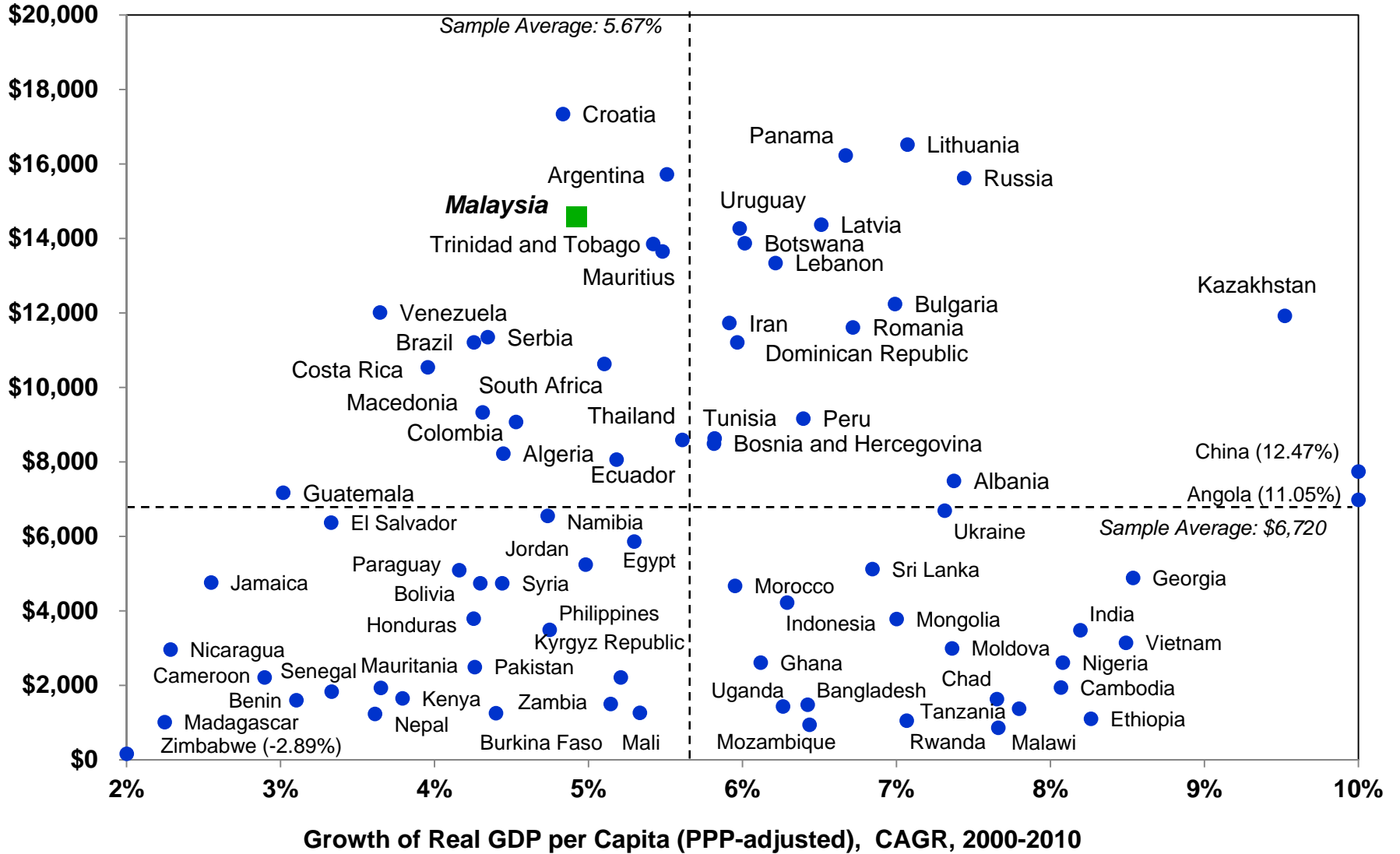
Source: EIU (2011), authors calculations

20110707 – Malaysia VC – v3 07072011 – prepared by RA Stacie Rabinowitz

Prosperity Performance

Lower and Middle Income Countries

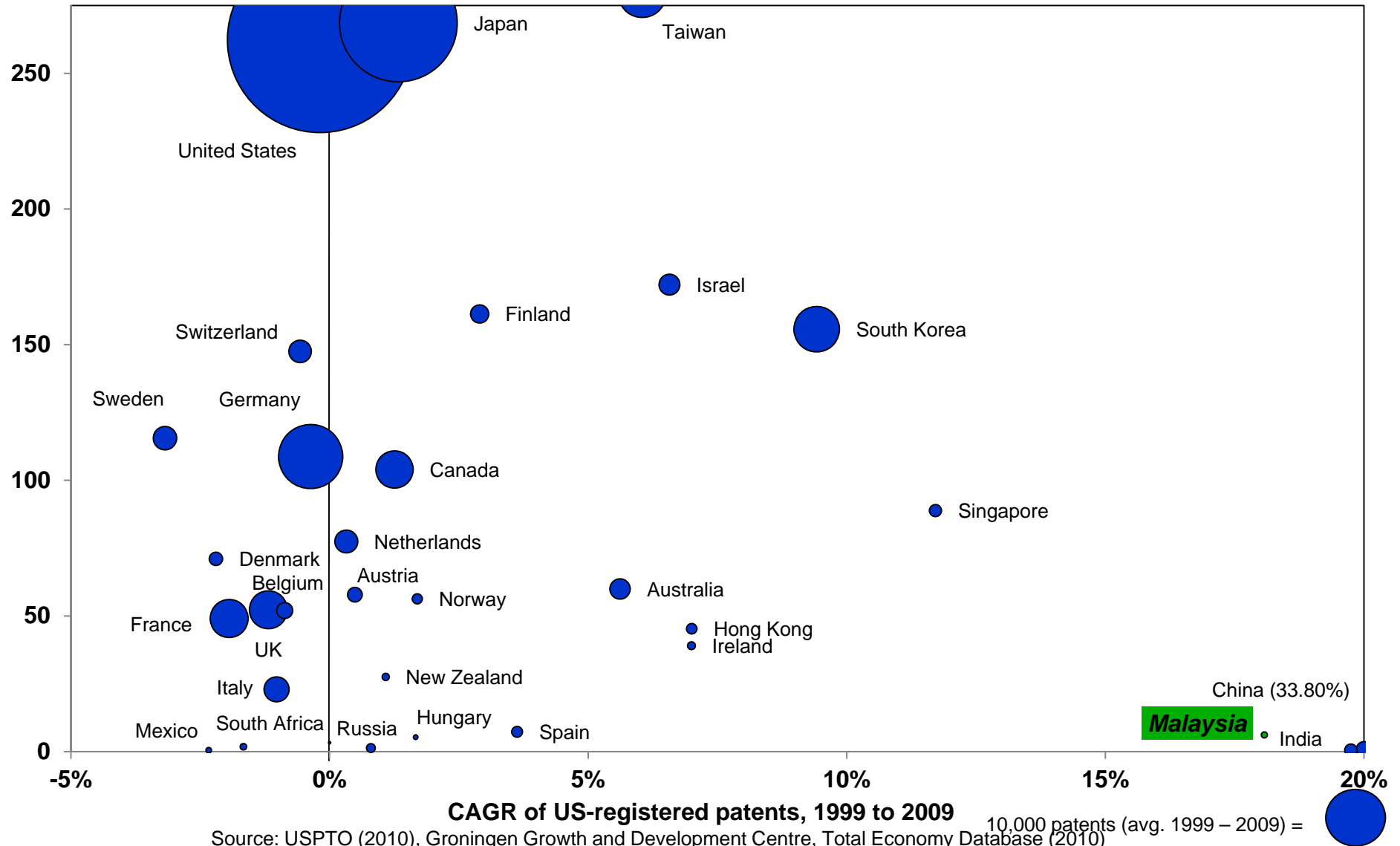
PPP-adjusted GDP per Capita, 2010 (\$USD)



Innovation Output

Selected Countries, 1999 to 2009

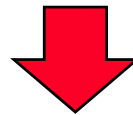
Average U.S. utility patents per 1 million population, 2007-2009



Source: USPTO (2010), Groningen Growth and Development Centre, Total Economy Database (2010)

What is Competitiveness?

- Competitiveness is the **productivity** with which a nation uses its human, capital, and natural resources.
 - Productivity **sets the sustainable standard of living** (wages, returns on capital, returns on natural resources)
 - It is not **what** industries a nation competes in that matters for prosperity, but **how** it competes in those industries
 - Productivity in a national economy arises from a **combination of domestic and foreign firms**



- Only business can create **wealth**
- Nations compete to offer the **most productive environment for business**
- The public and private sectors play **different but interrelated roles** in creating a productive economy

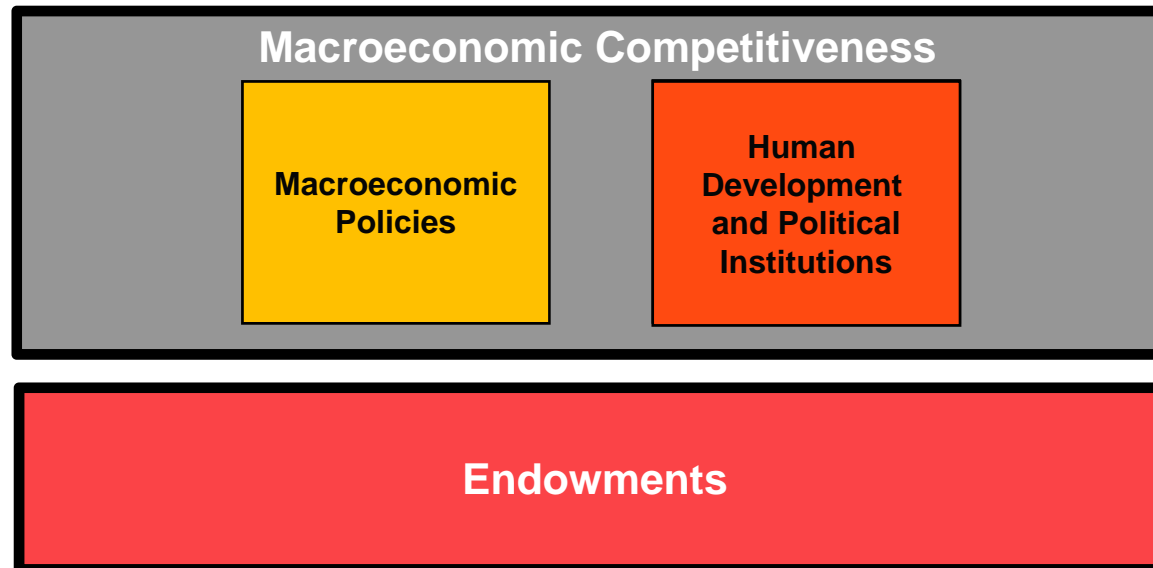
What Determines Competitiveness?



Endowments

- Endowments create a **foundation** for prosperity, but true prosperity is created by **productivity in the use of endowments**

What Determines Competitiveness?



- Macroeconomic competitiveness sets the **potential** for high productivity, but is **not sufficient**
- Endowments create a **foundation** for prosperity, but true prosperity is created by **productivity in the use of endowments**

Macroeconomic Competitiveness

Macroeconomic Policies

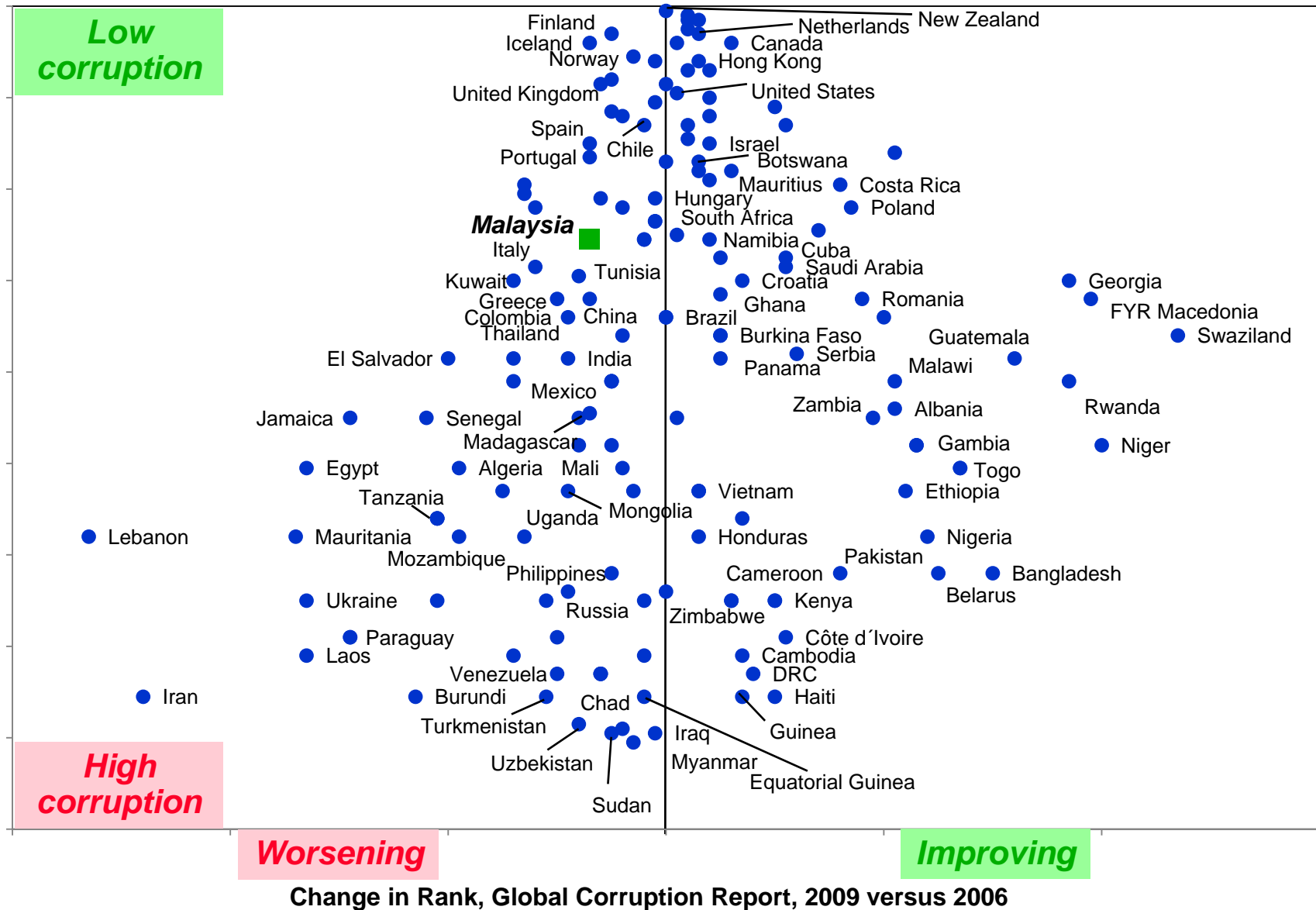
- **Fiscal policy**
 - Government surplus/deficit
 - Government debt
- **Monetary policy**
 - Inflation
 - Business cycle management
 - Savings

Social Infrastructure and Political Institutions

- **Human development**
 - Basic education
 - Health
- **Political institutions**
 - Political freedom
 - Voice and accountability
 - Political stability
 - Government effectiveness
 - Decentralization of economic policymaking
- **Rule of law**
 - Security
 - Civil rights
 - Judicial independence
 - Efficiency of legal framework
 - Freedom from corruption

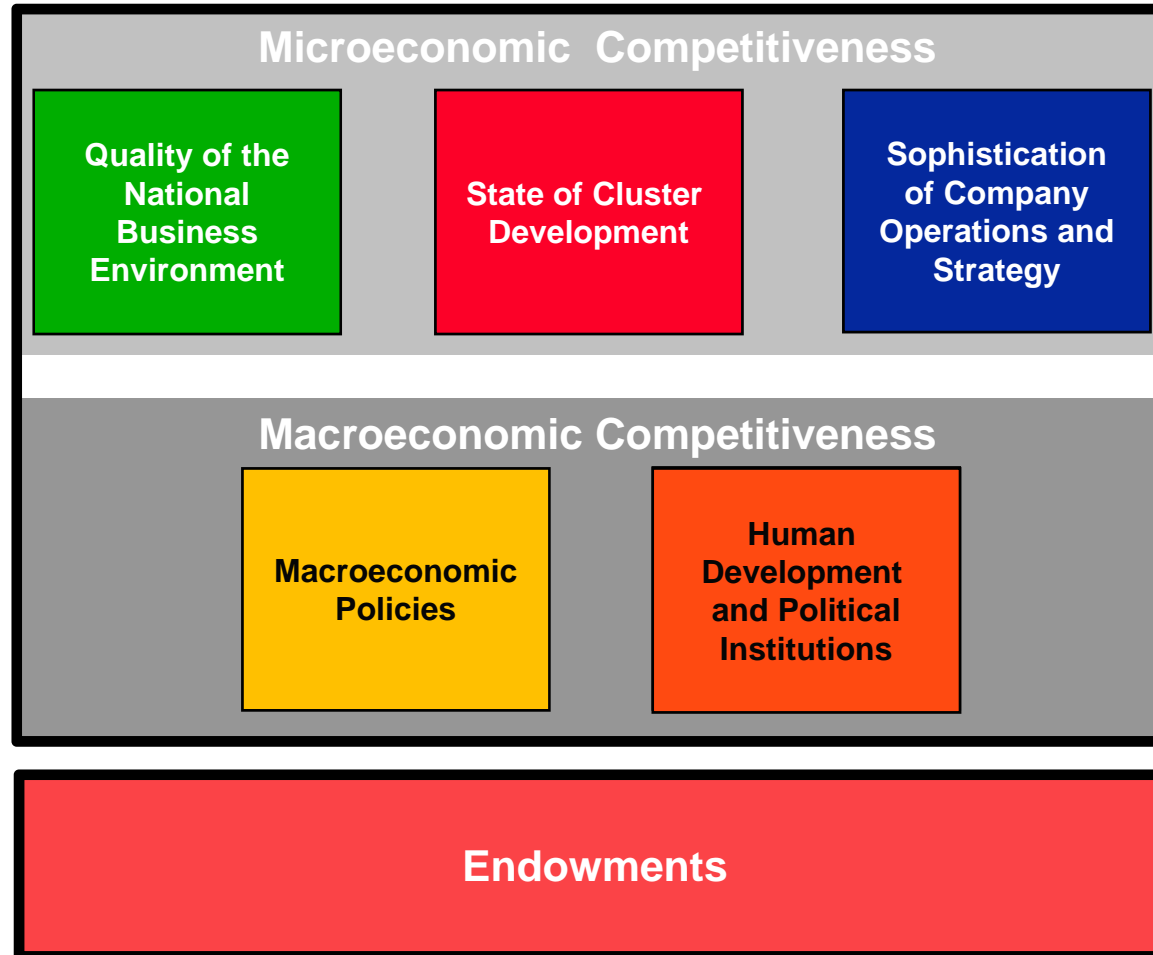
Rank in Global
Corruption Index,
2009

Corruption Perception Index, 2009



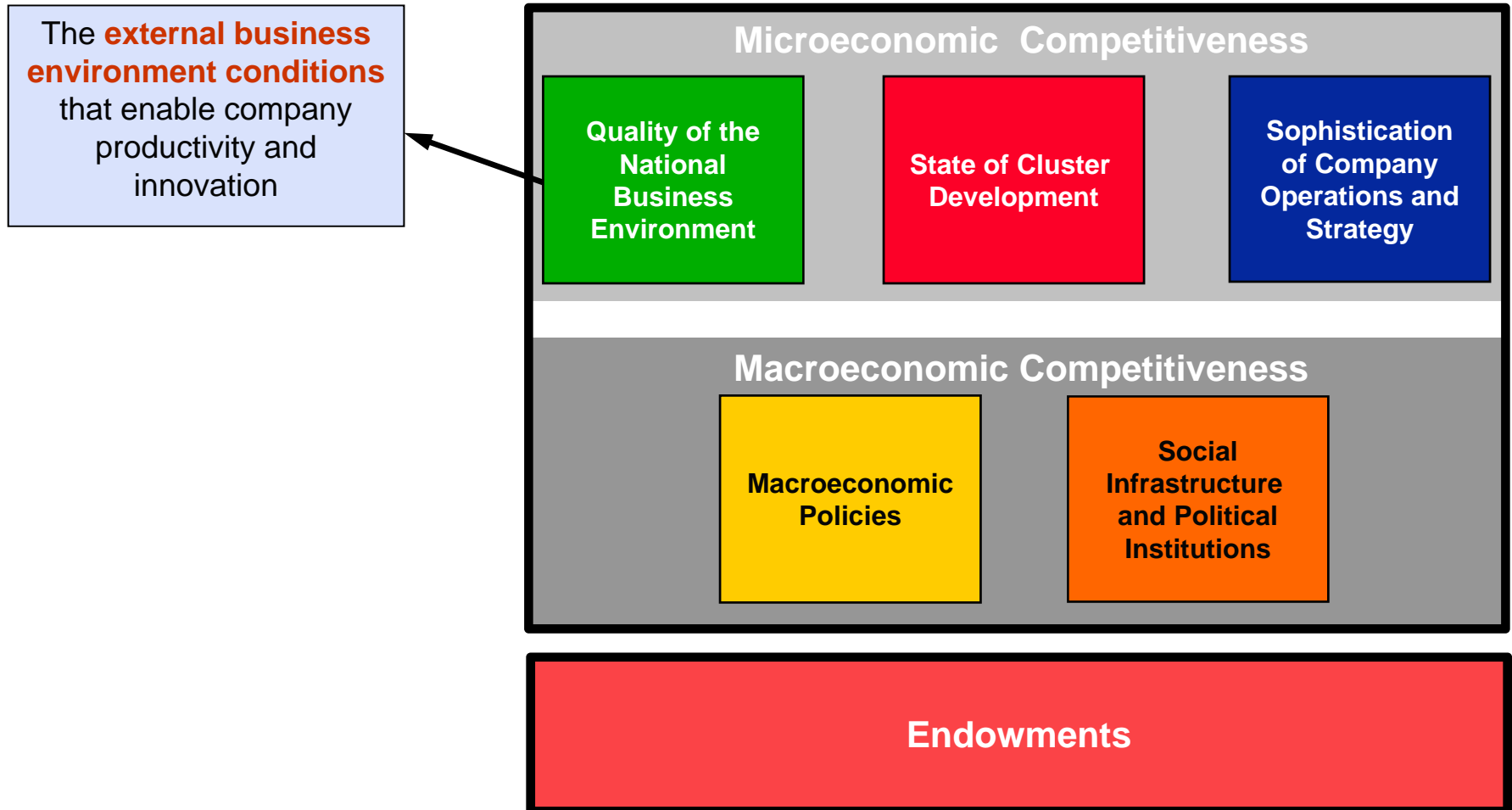
Note: Ranks only countries available in both years (161 countries total)
Source: Global Corruption Report, 2010

What Determines Competitiveness?

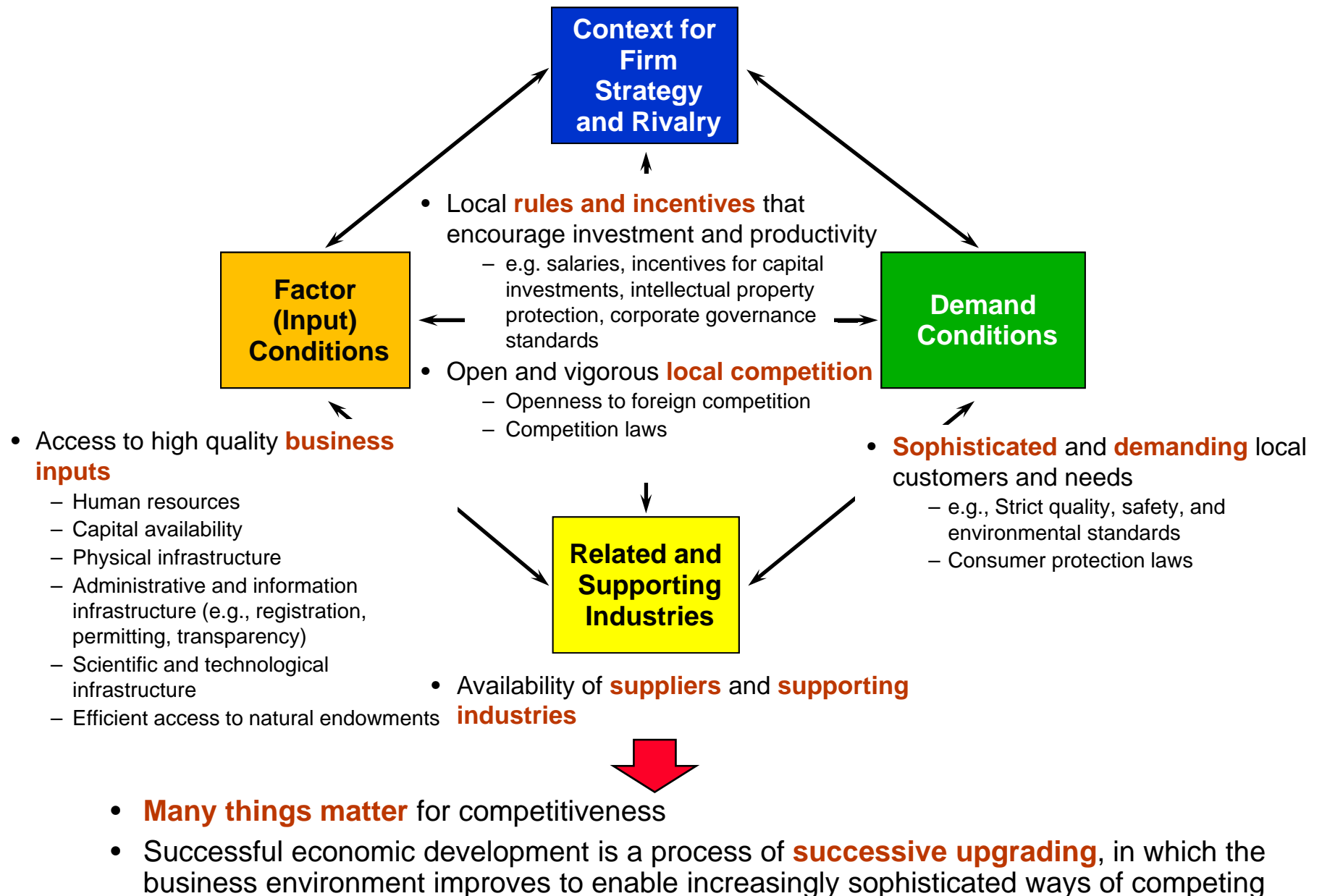


- Productivity ultimately depends on improving the **microeconomic capability** of the economy and the **sophistication of local competition**
- Macroeconomic competitiveness sets the **potential** for high productivity, but is **not sufficient**
- Endowments create a **foundation** for prosperity, but true prosperity is created by **productivity in the use of endowments**

What Determines Competitiveness?

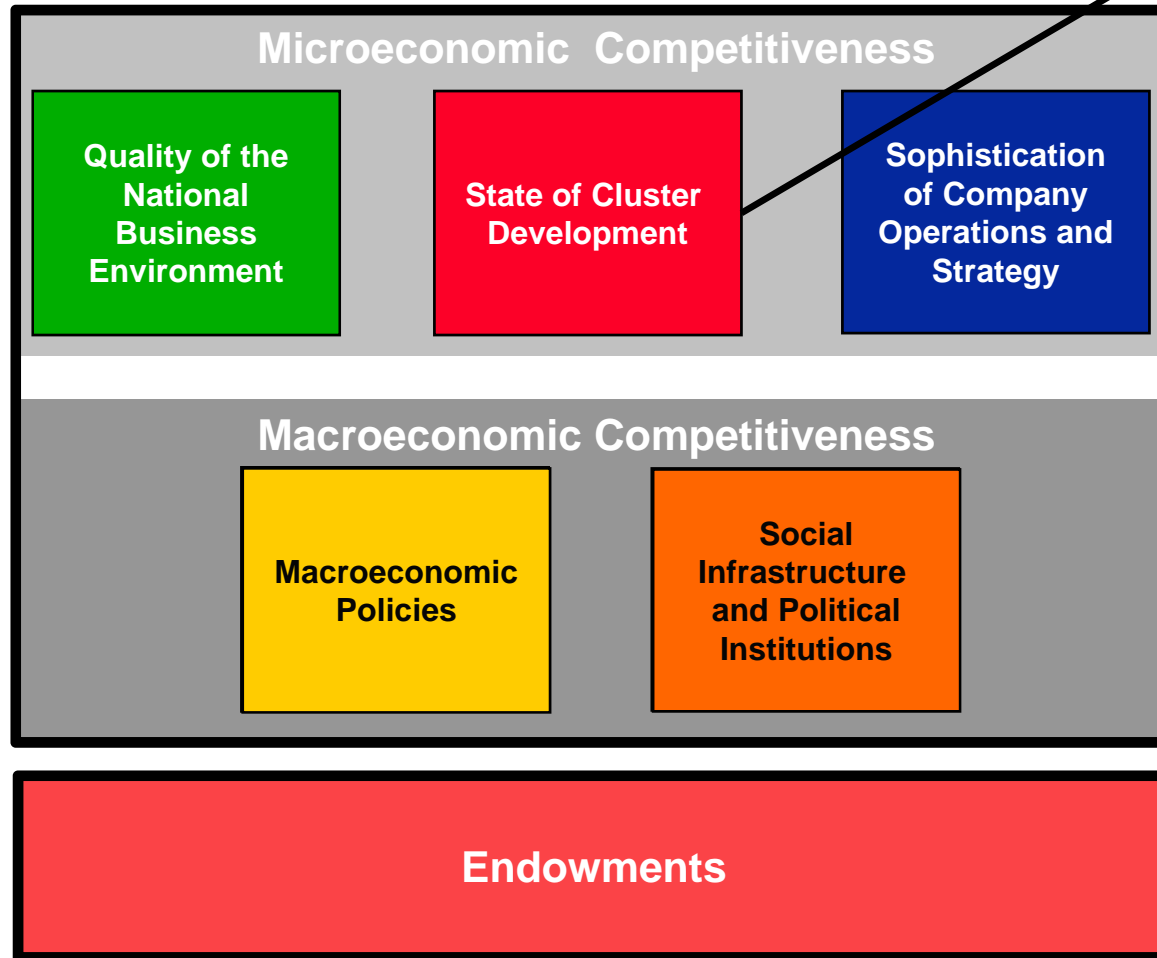


Quality of the National Business Environment



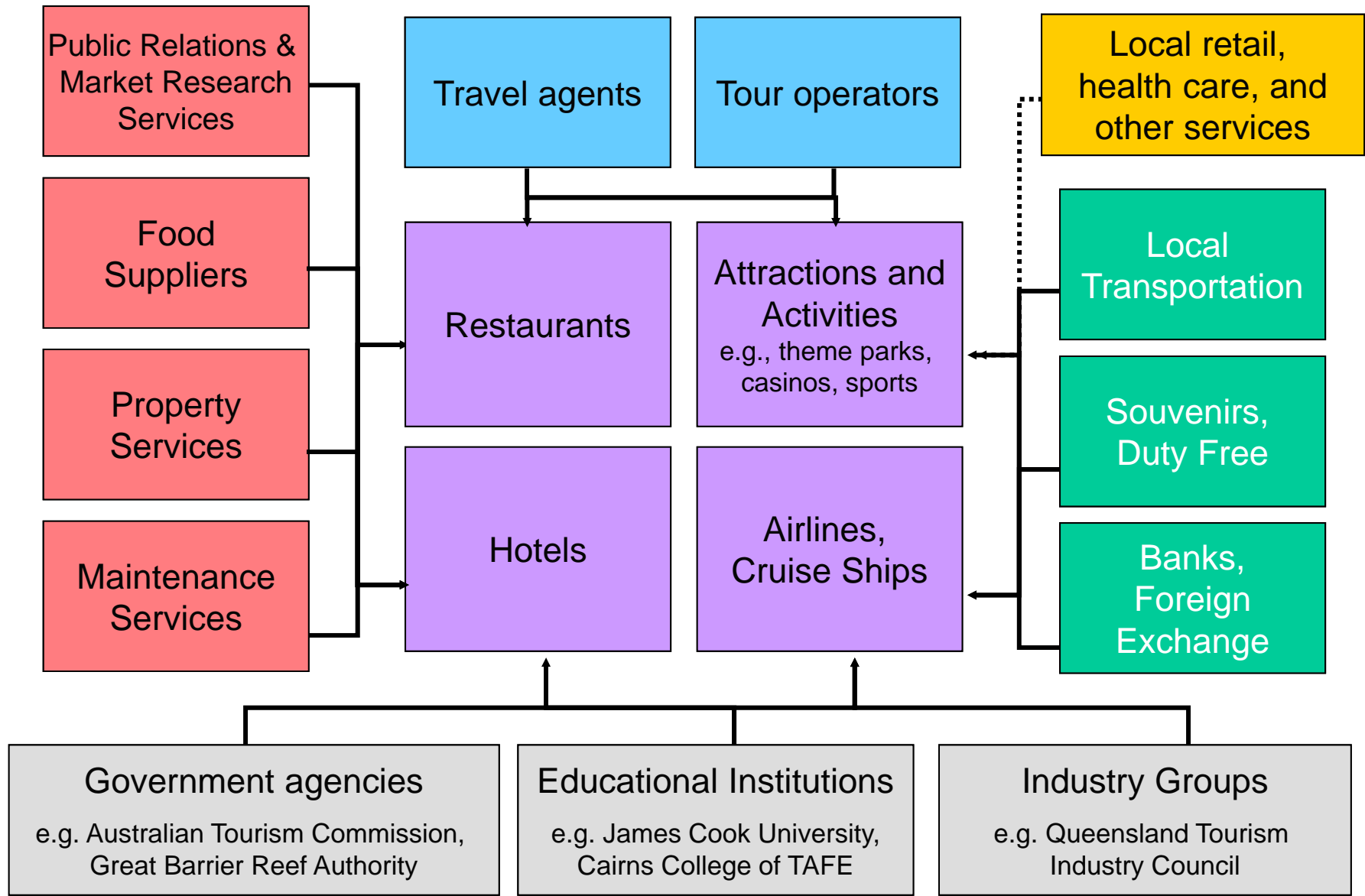
What Determines Competitiveness?

A critical mass of firms and institutions in each field to harness efficiencies and externalities across related entities

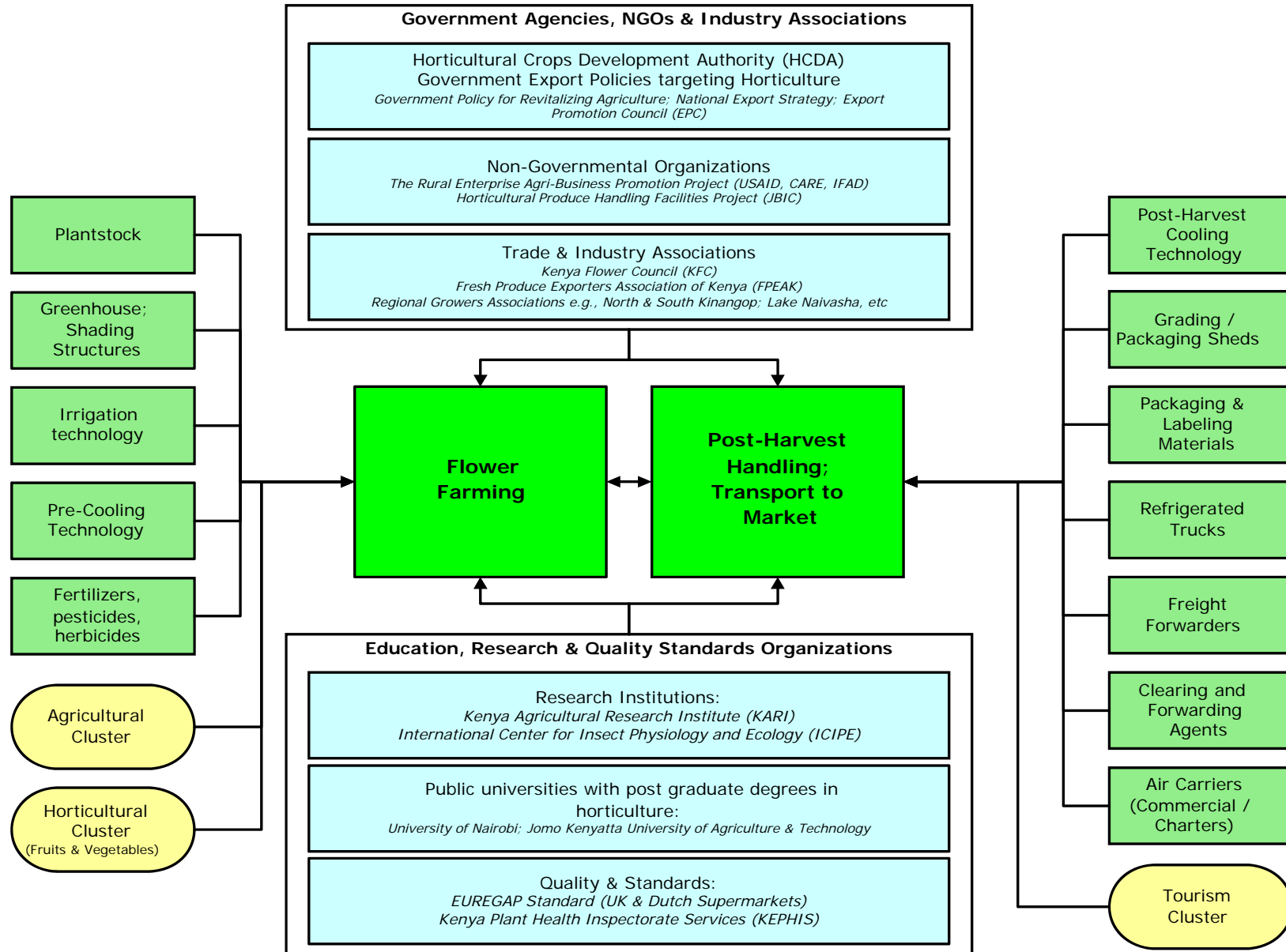


State of Cluster Development

Tourism Cluster in Cairns, Australia

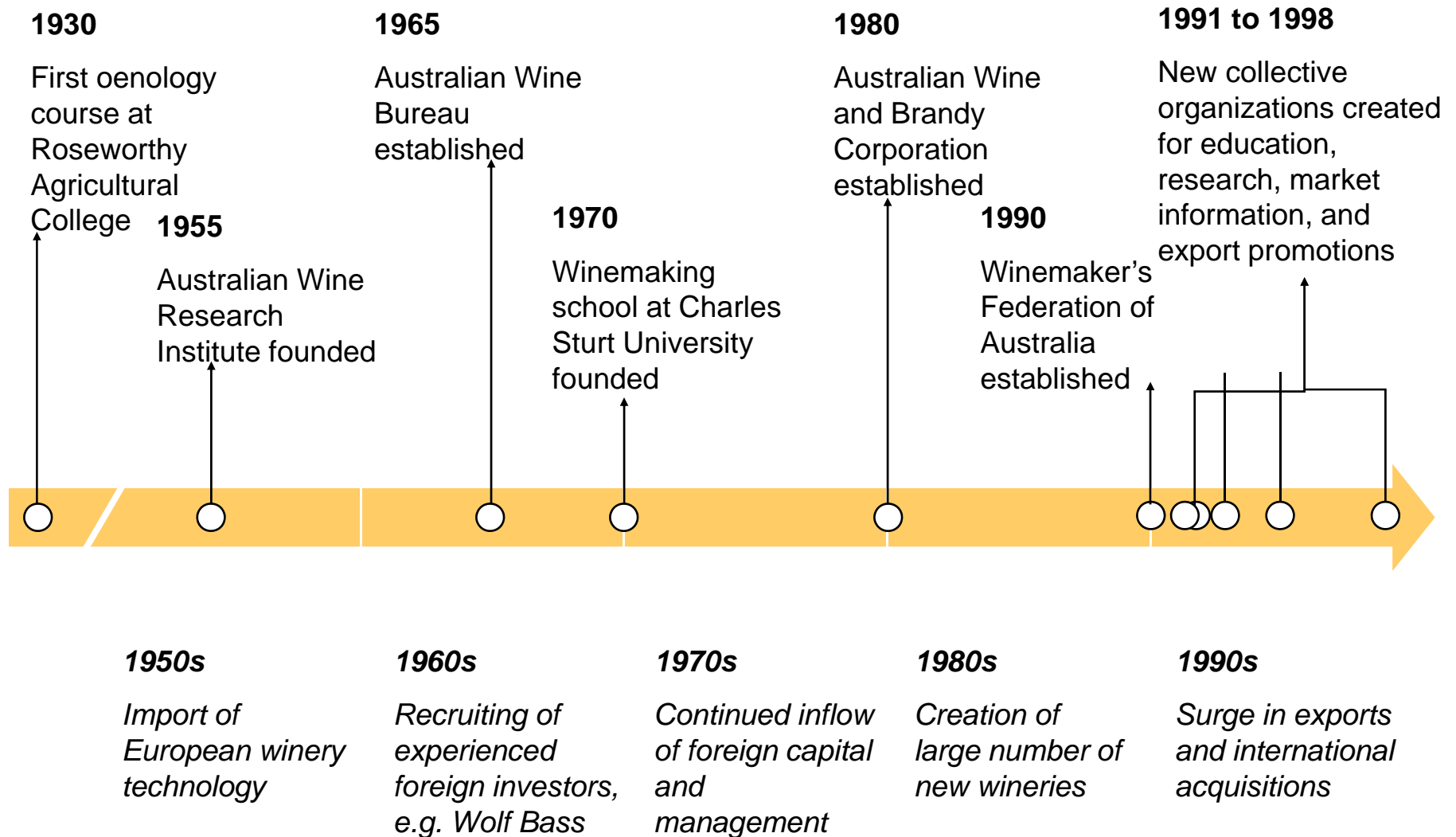


Kenya's Cut Flower Cluster



Sources: MOC student team research by Kusi Hornberger, Nick Ndiritu, Lalo Ponce-Brito, Melesse Tashu, Tijan Watt, Harvard Business School, 2007

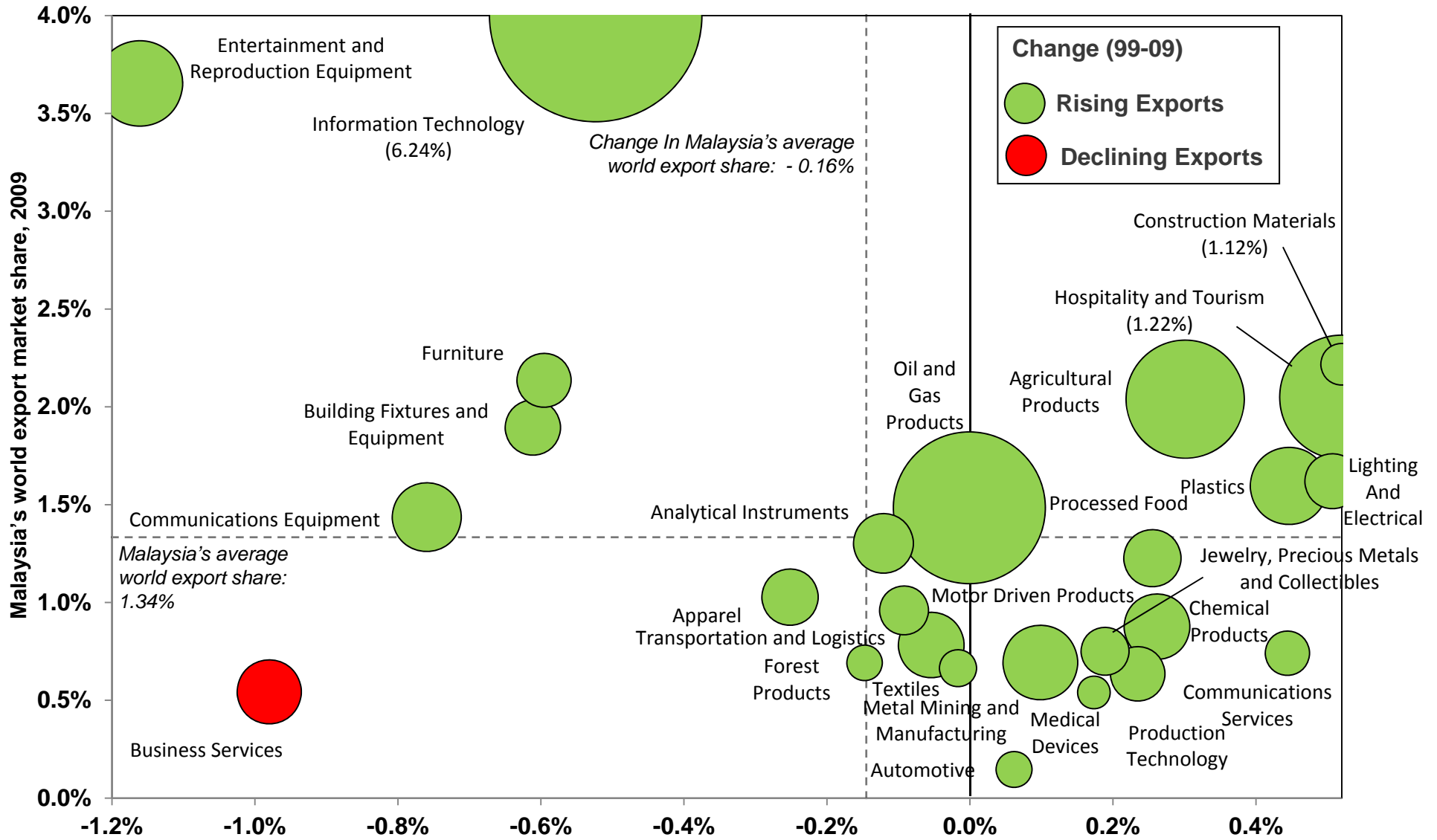
Development of the Australian Wine Cluster



Source: Michael E. Porter and Örjan Sölvell, The Australian Wine Cluster – Supplement, Harvard Business School Case Study, 2002

National Cluster Export Portfolio

Malaysia, 1999-2009

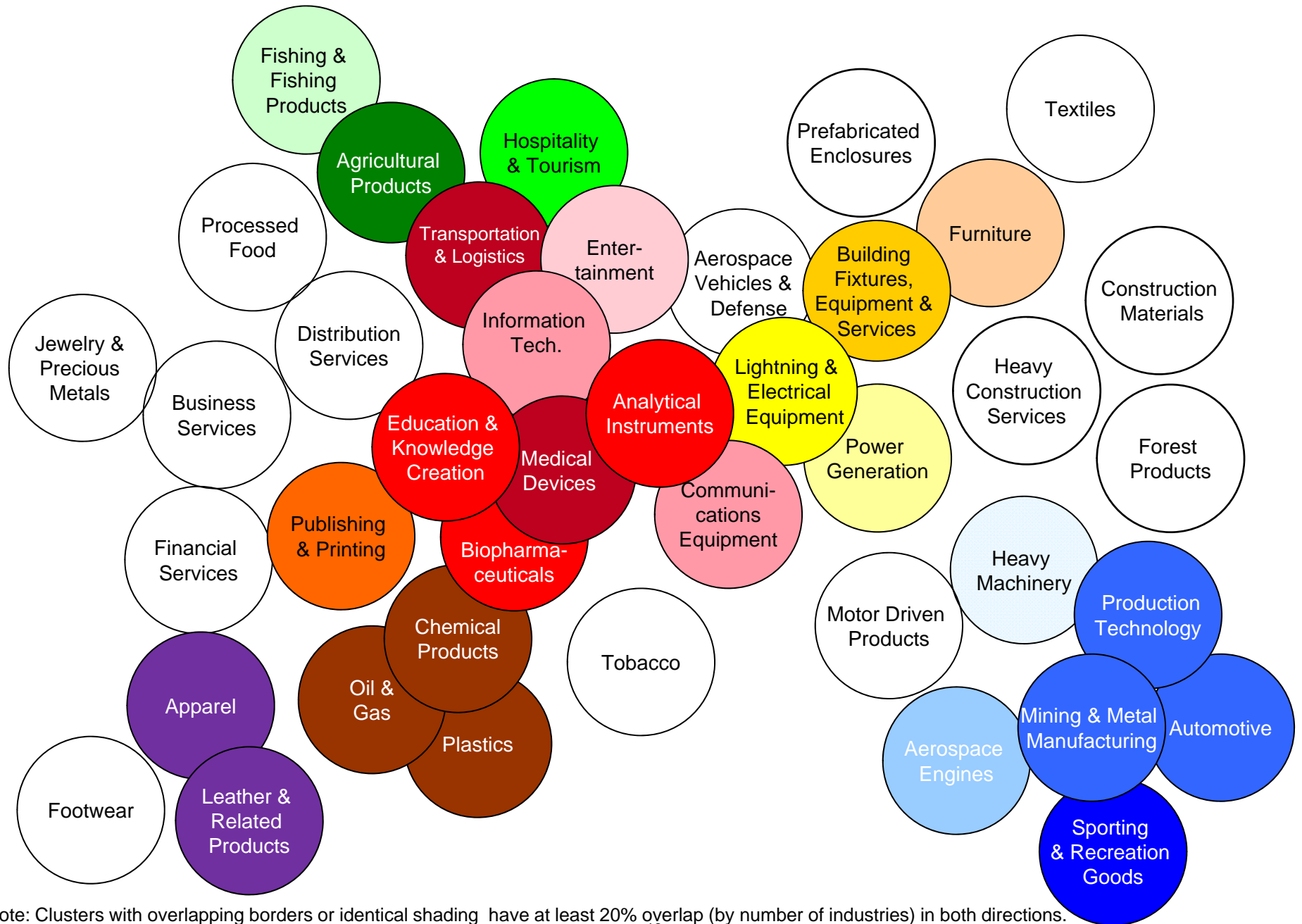


Change in Malaysia's world export market share, 1999 – 2009

Source: Prof. Michael E. Porter, International Cluster Competitiveness Project, Institute for Strategy and Competitiveness, Harvard Business School; Richard Bryden, Project Director. Underlying data drawn from the UN Commodity Trade Statistics Database and the IMF BOP statistics. 20110707 – Malaysia VC – v3 07072011 – prepared by RA Stacie Rabinowitz

Exports of US\$2.3 Billion =

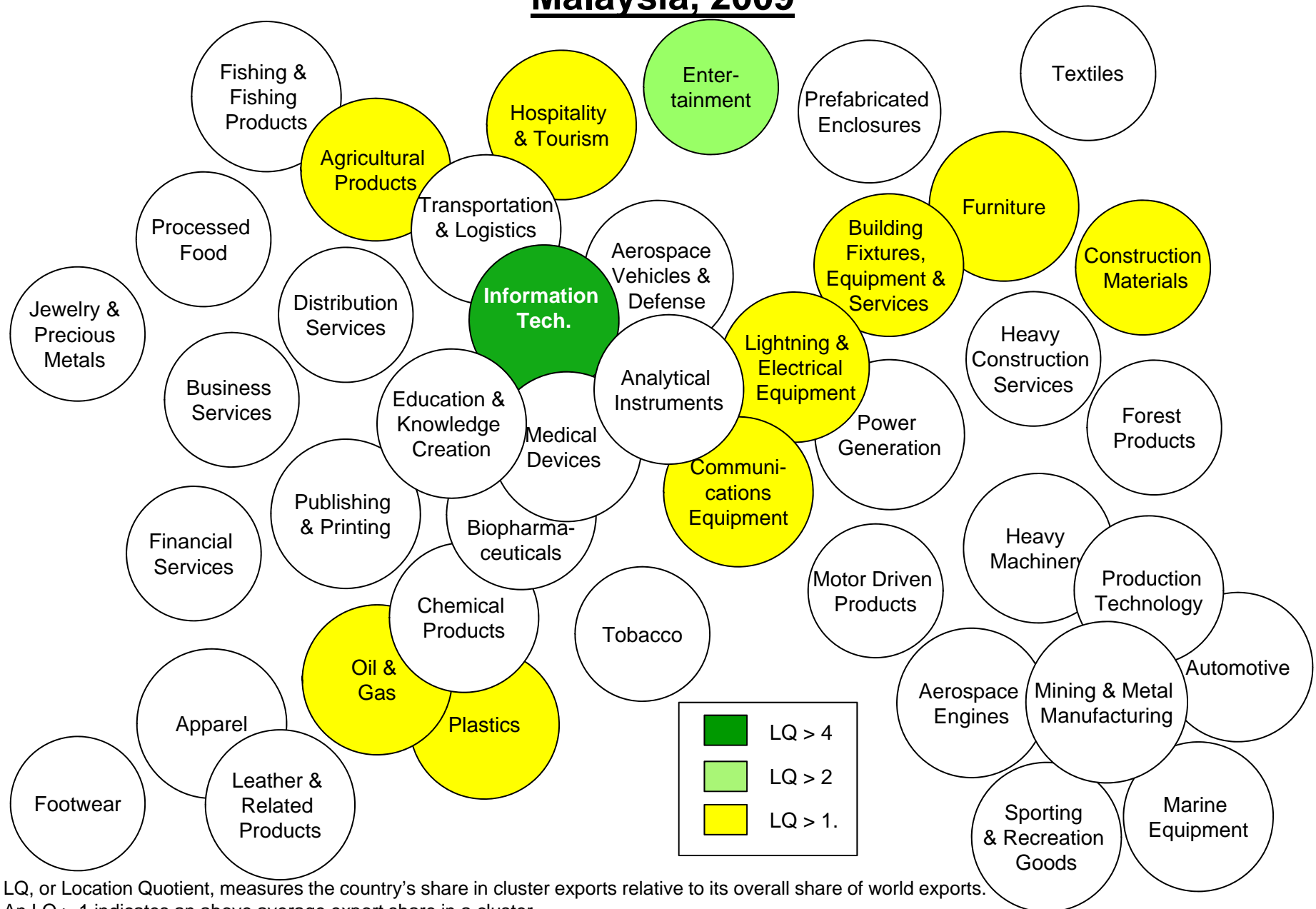
Cluster Linkages and Economic Diversification



Note: Clusters with overlapping borders or identical shading have at least 20% overlap (by number of industries) in both directions.

Share of World Exports by Cluster

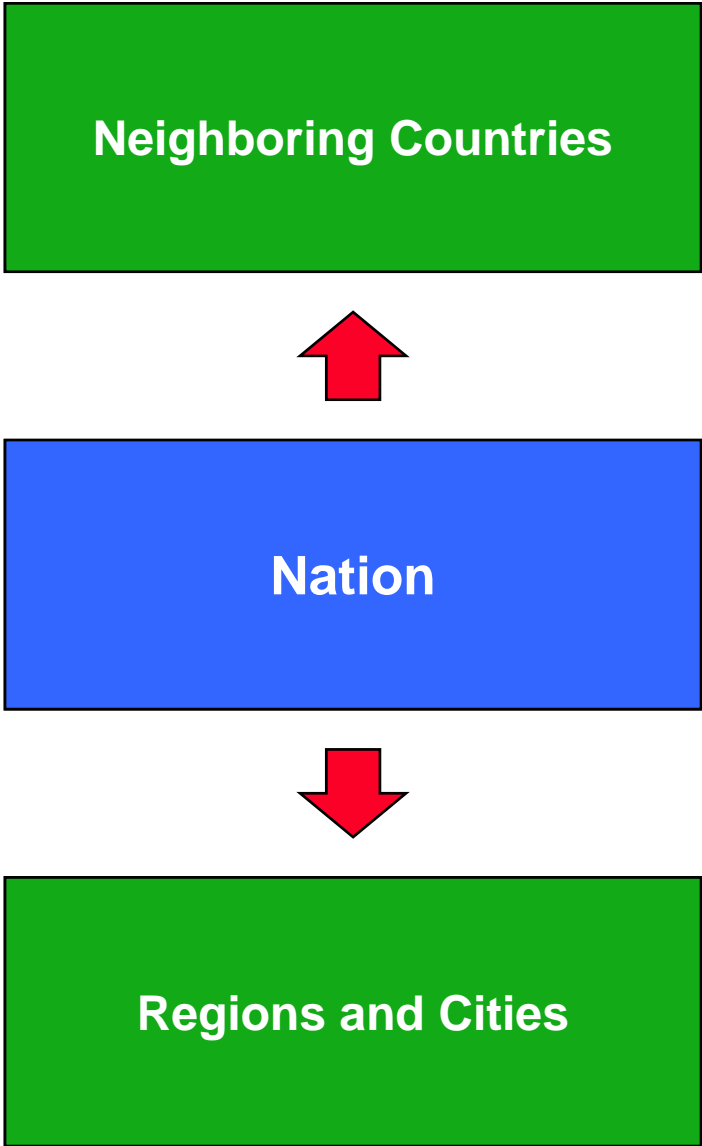
Malaysia, 2009



LQ, or Location Quotient, measures the country's share in cluster exports relative to its overall share of world exports.

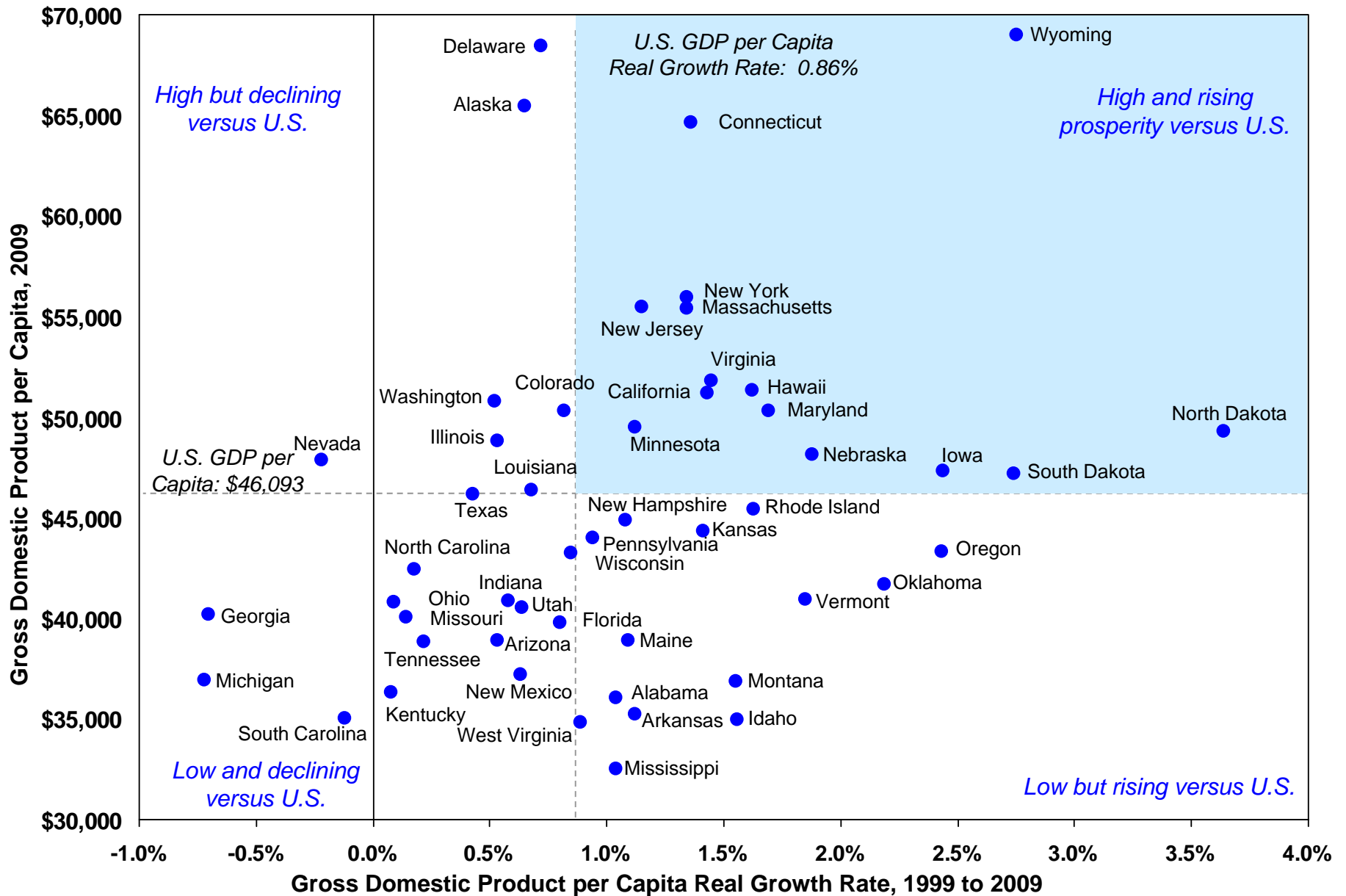
An LQ > 1 indicates an above average export share in a cluster.

Geographic Influences on Competitiveness



Prosperity Performance

U.S. States, 1999 to 2009



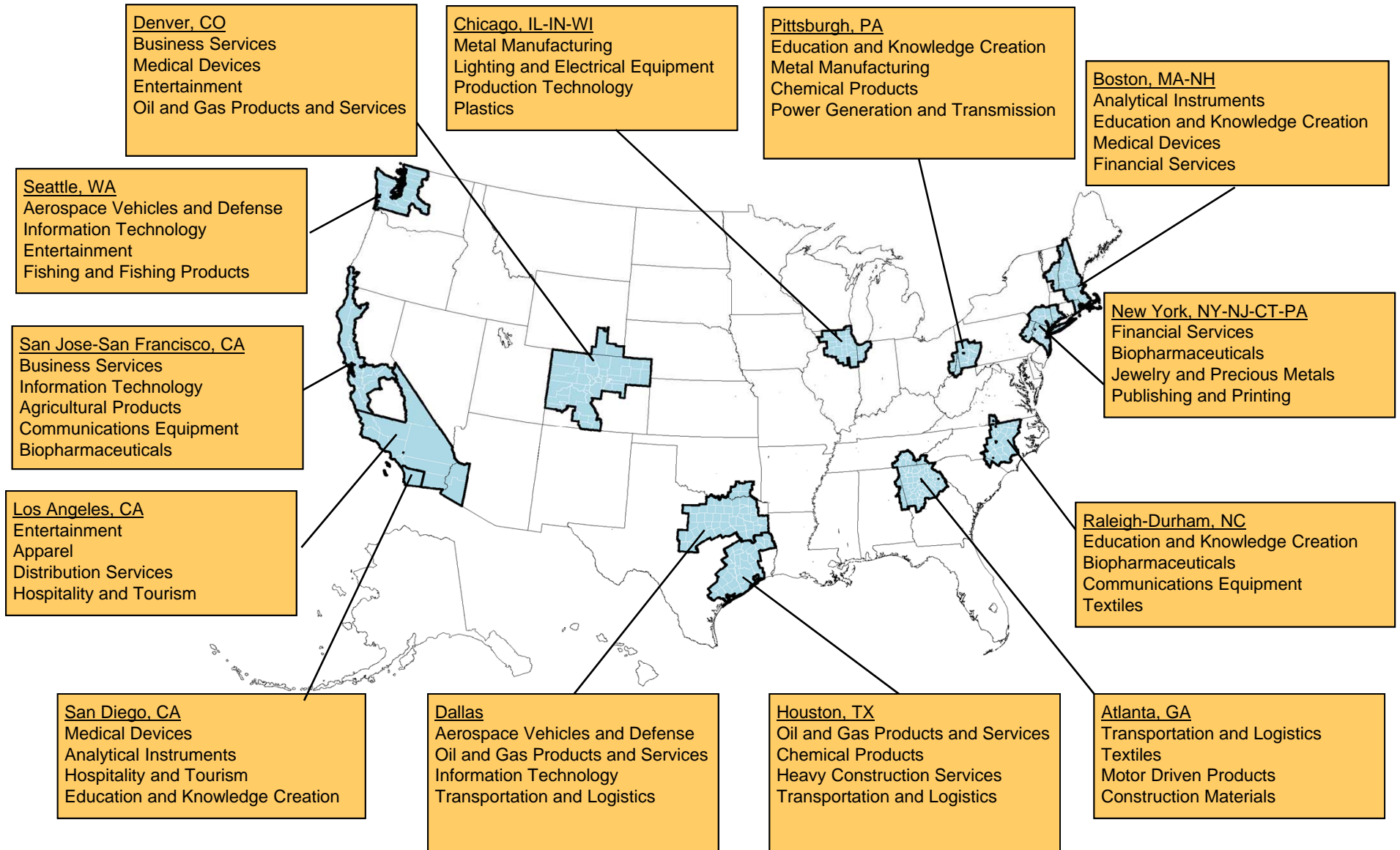
Notes: Real GDP figures in 2005 chained US dollars from the Bureau of Economic Analysis. Growth rate is calculated as compound annual growth rate. D.C. excluded
 20110707 - Malaysia VC - v3 07072011 - prepared by RA Stacie Rabinowitz
 Copyright © 2011 Professor Michael E. Porter

Regions and Competitiveness

- 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
- **Cluster strength** directly impacts regional performance

Specialization of Regional Economies

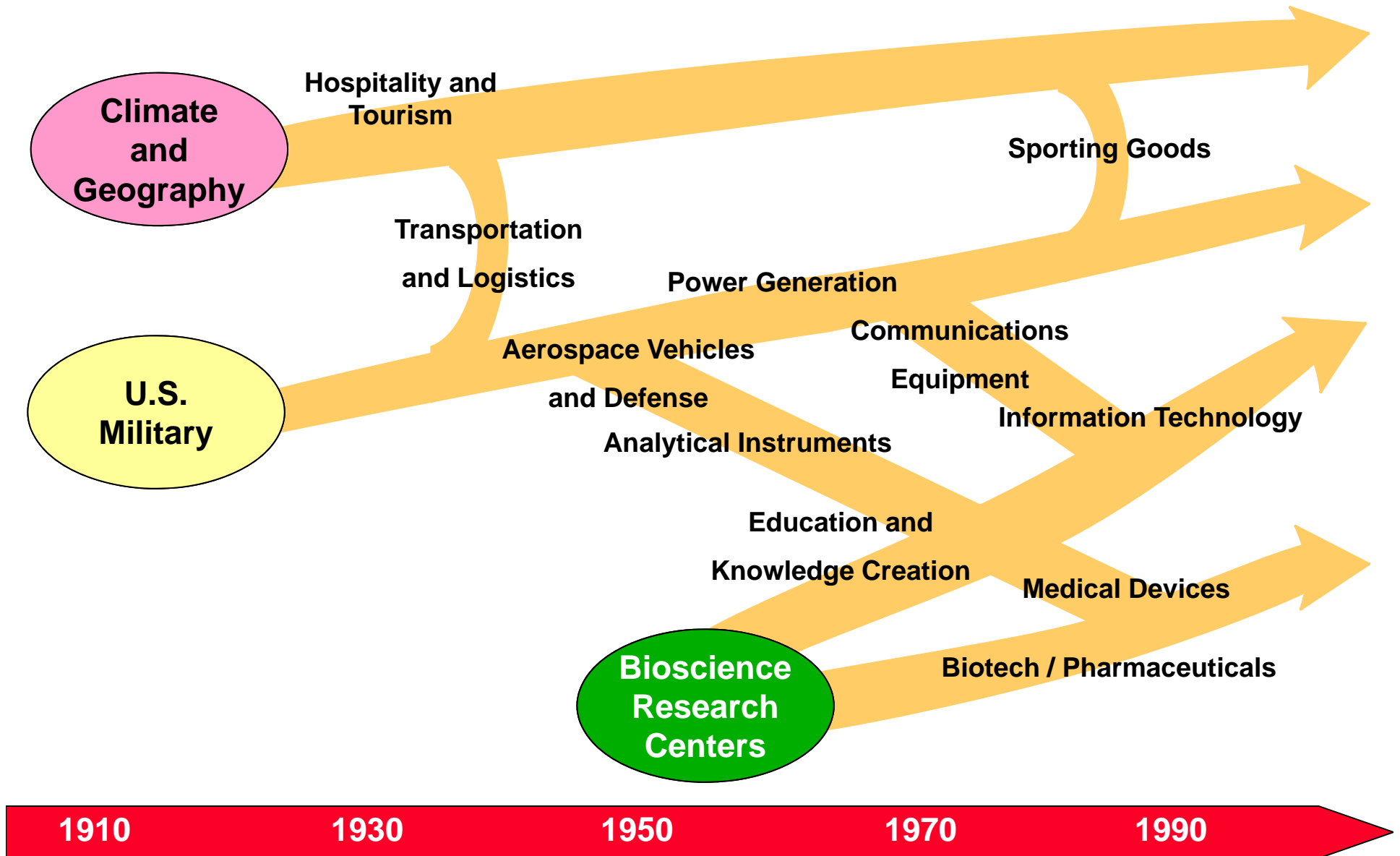
Leading Clusters by U.S. Economic Area, 2008



Source: Prof. Michael E. Porter, Cluster Mapping Project, Institute for Strategy and Competitiveness, Harvard Business School; Richard Bryden, Project Director.

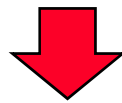
The Evolution of Regional Economies

San Diego



Regions and Competitiveness

- 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
- **Cluster strength** directly impacts regional performance
- Each region needs its own distinctive **competitiveness strategy and action agenda**
- Improving competitiveness requires **effective policy collaboration** between regions and the national government



- **Decentralization** is important to foster regional specialization, internal competition, and greater government accountability
- Effective decentralization requires clarity on roles and responsibilities, and sufficient administrative **capacity at local and regional level**

Competitiveness and Integration with Neighboring Countries

Turkey's Neighborhood



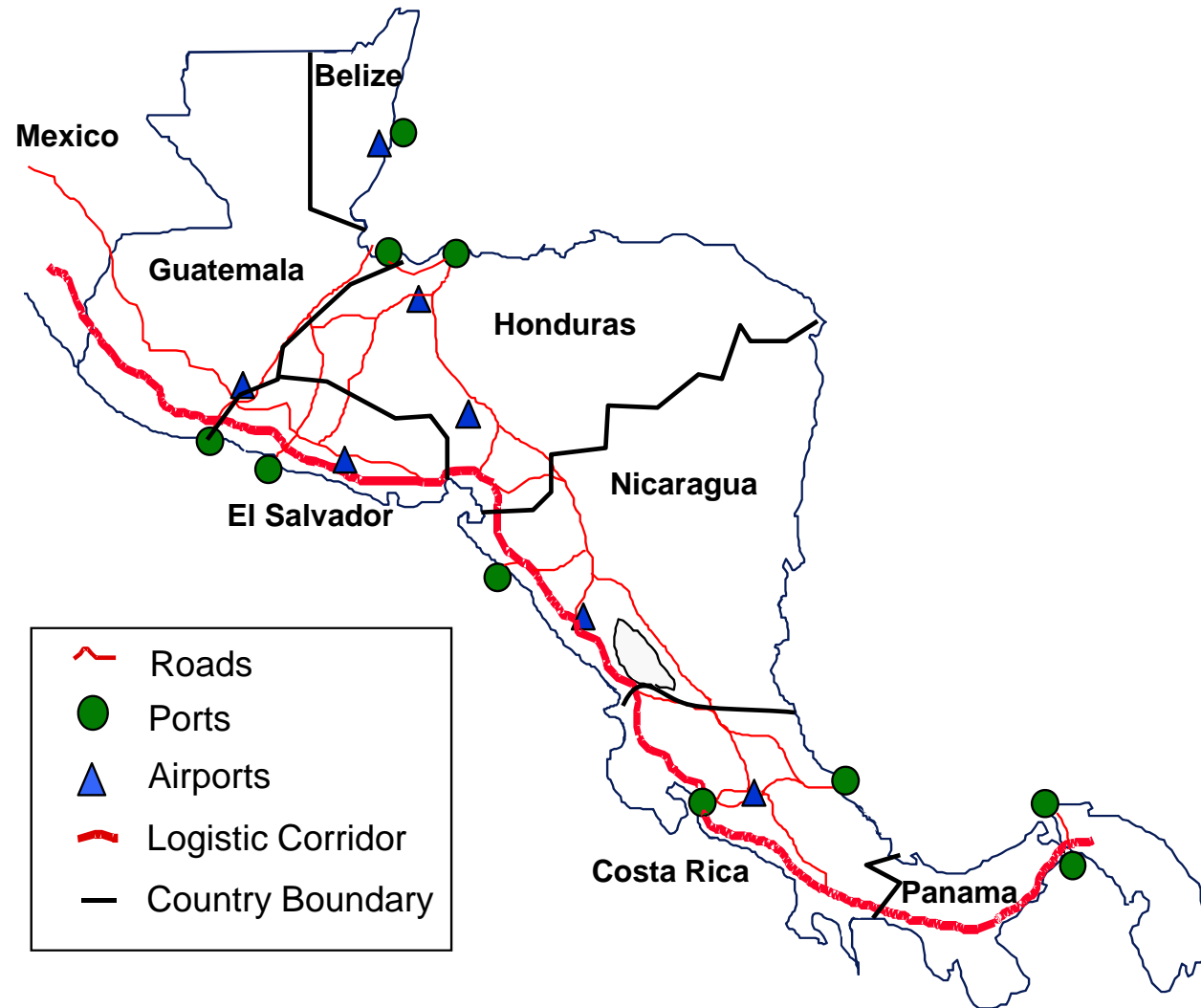
- Turkey sits at the crossroad between Europe and the Middle East
- Economic coordination among neighboring countries can significantly enhance competitiveness
- Integration offers greater opportunities than participation in broader economic forums (e.g., EU)

Competitiveness and the Neighborhood

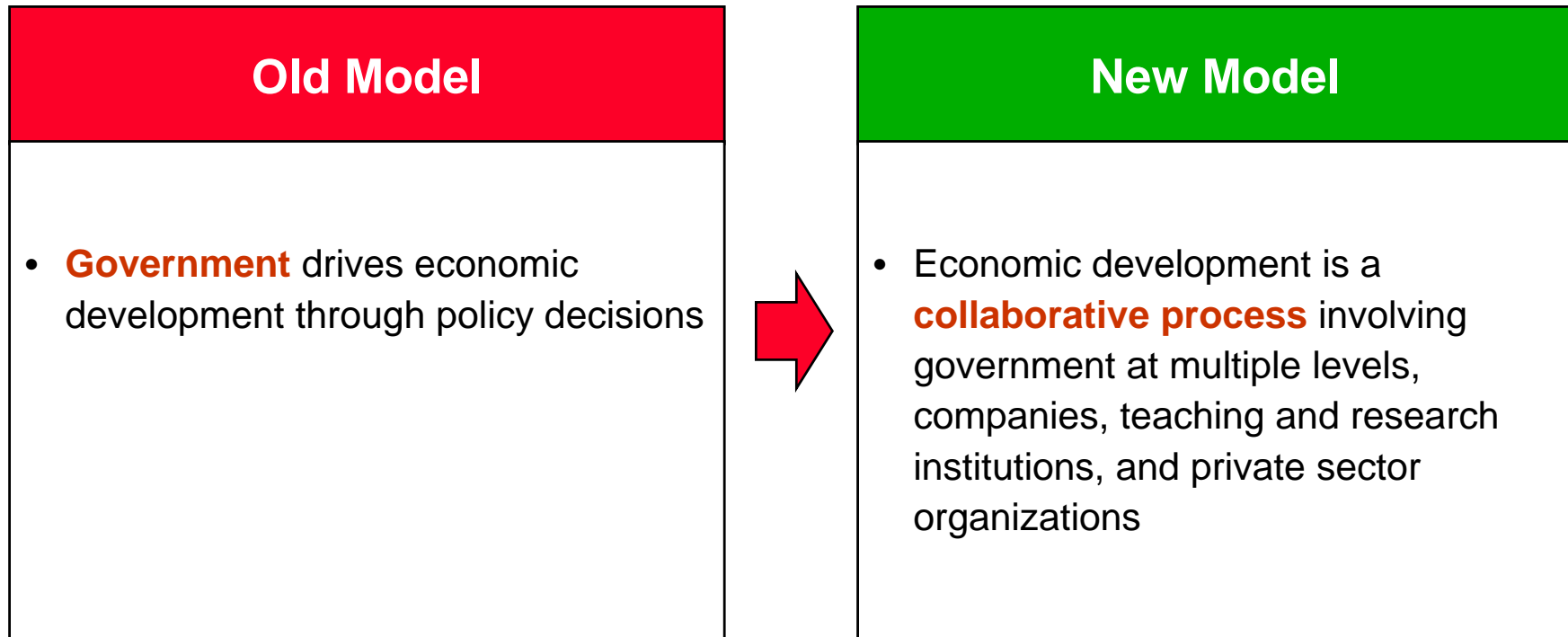
- Opening **trade and investment** among neighbors
 - Expands the **available** market
 - A nation's **neighbors** are its most natural trading and investment partners
 - The natural **path of internationalization** for local firms is the neighborhood
 - Open trade and investment make each **country** a more attractive location for investment
- Economic coordination to drive **improvements in the business environment**
 - Capture **synergies** in policy and infrastructure
 - Gain greater clout in **international negotiations**
- External agreements to help **overcome domestic political and economic barriers** to reform

Competitiveness and Integration with Neighboring Countries

Central American Logistical Corridor



The Shifting Process of Economic Development



Creating a National Economic Strategy

National Value Proposition

- What is the **distinctive competitive position** of a nation given its location, legacy, existing strengths, and potential strengths?
 - What unique value as a business location?
 - For what types of activities and clusters?
 - And what roles with neighbors, the region, 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** represent local strengths?

Achieving and Maintaining Parity with Peers

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

- **Priorities** and **sequencing** are necessity in economic development

Universities' Role in Competitiveness

Business Environment Quality

- **Educate** future managers, researchers, and employees
- **Transfer of technology** and knowledge
- **Adapt** global knowledge to local circumstances
- Act as a **launching pad** for new companies and clusters
- Create **networks** of alumni and other partners to enable collaboration
- Collect and provide **data** on all aspects of the economy
- Create **new knowledge**
- Raise **visibility** and provide profile to the region and its economy



Competitiveness Efforts

- Generate specific data and **analysis on competitiveness**
- **Educate** public and private leaders about competitiveness
- Provide a **platform** for public-private action
- **Initiate and lead** competitiveness efforts

- Competition in the global economy is increasingly **knowledge-driven**, putting universities at the very heart of the competitiveness agenda

Universities and Cluster Development

- Universities should **identify** and **reach out** to local clusters
- Universities should focus on clusters where they have a material **impact** on cluster performance
- Universities should consider **specializing** in areas in which the local economy has an established position
- Universities should, alone or with others, get involved in upgrading the cluster-specific cluster environment
 - Conduct **joint R&D** programs with companies
 - Develop **training programs** with the cluster
 - Participate in the **attraction of companies and research centers** important for the development of the cluster