

The Business Imperative for Shared Value

Professor Michael E. Porter
Harvard Business School

*Shared Value Executive Education for
Becton Dickinson & Company
Hamilton Park Conference Center
June 24, 2013*

The ideas drawn from “Creating Shared Value” (*Harvard Business Review*, Jan 2011) and “Competing by Saving Lives” (FSG, 2012). 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. For further materials, see the website of the Institute for Strategy and Competitiveness, www.isc.hbs.edu, and FSG website, www.fsg.org.

The Role of Business in Society

- 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



We need a **new model**

The Role of Business in Society

Evolving Approaches

Philanthropy

- Donations to worthy social causes
- Volunteering

The Role of Business in Society

Evolving Approaches



The Role of Business in Society

Evolving Approaches



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

What Shared Value is NOT

- Sharing the economic value **already created** (philanthropy)
- Acting based on strong **personal values** and **ethical standards**
- **Balancing** stakeholder interests
- Avoiding **harm** or **risk**
- Protecting **reputation**

Moving to Shared Value in Pharmaceuticals

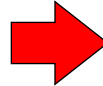
Novartis in Rural India

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



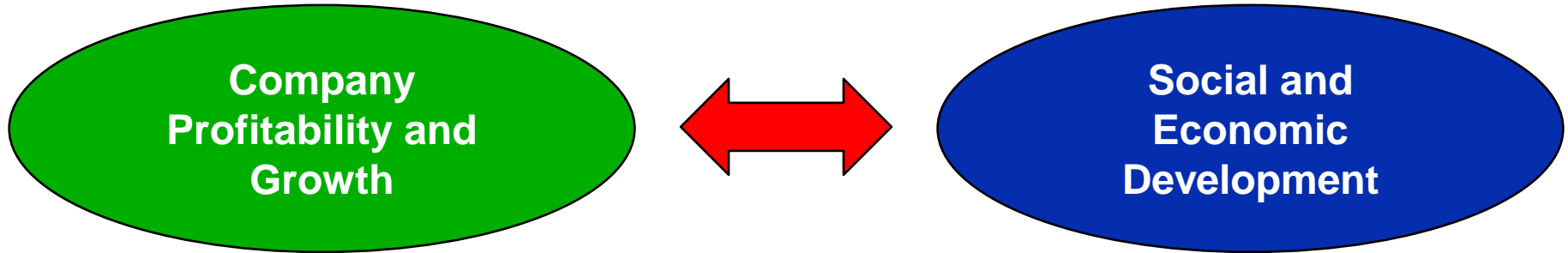
CSV

- 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**



- **Zero sum** competition
- **Growth** and **innovation** suffer

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 business environment**

- Improving the **skills, supplier base, regulatory environment, and supporting institutions** in the communities in which a company operates

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

Dow Chemical Insect Control

The Spinetoram™ Family of insect control products are derived from a **biological organism** that provides control of a broad spectrum of insect pests in a variety of crops

- Natural degradation through UV light and soil microbes
- Low solubility in water
- Favorable toxicological profile
- Carries lowest human hazard label



- Applied in **lower quantities** than conventional insecticides
- **Low impact** on **beneficial insects**
- **Double-digit revenue growth** since launch in 2010

Creating Shared Value in Products and Markets

Jain Irrigation Systems

- **Drip irrigation equipment** for small farmers in Africa and India
- Serves **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

Becton Dickinson Health Worker Safety

- A pressing need to protect health workers from **needle stick injuries** that spread HIV and other infections
- BD engineered syringes to **prevent** accidental sticks

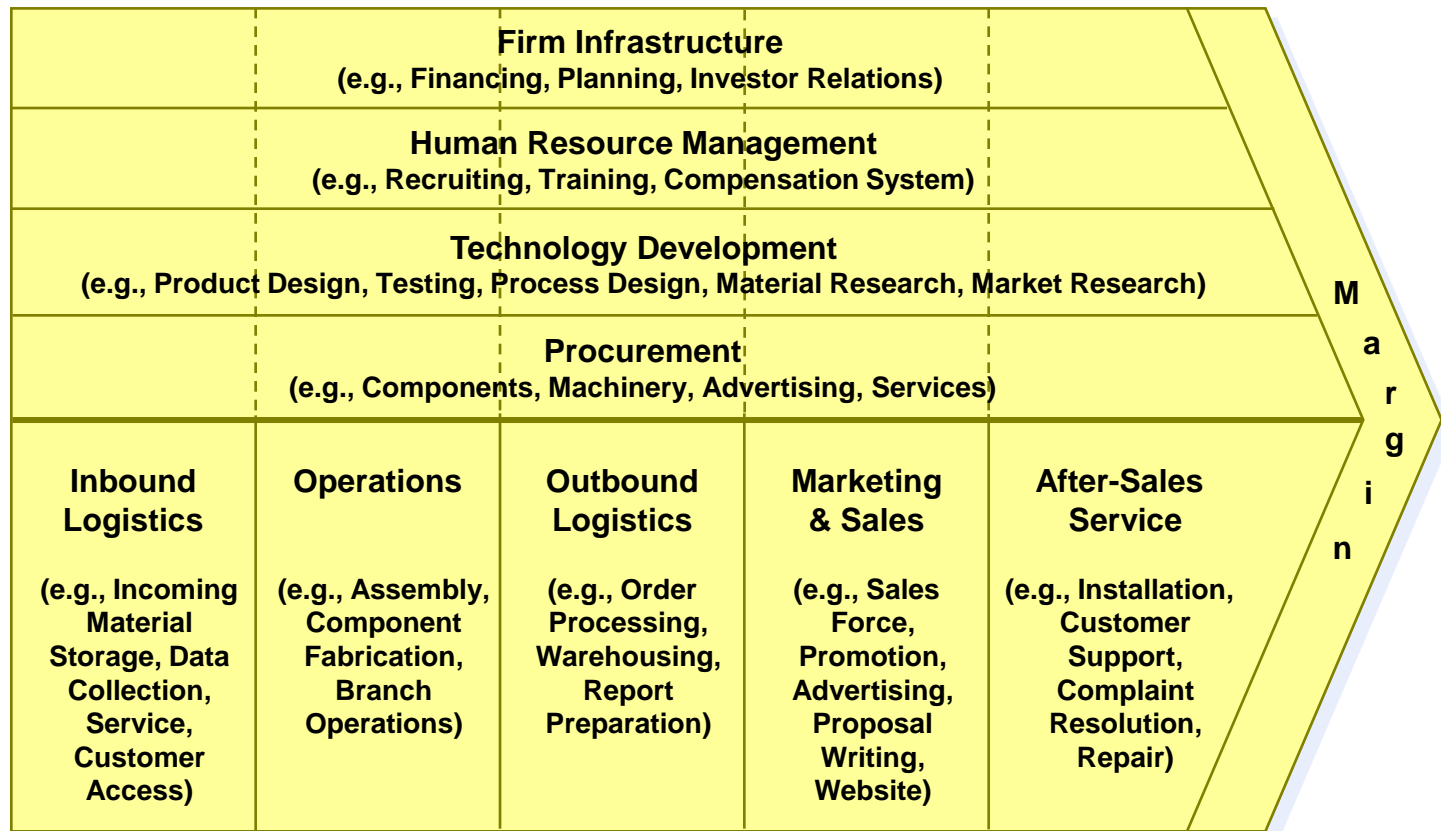


- Achieved substantial **reduction in health worker injuries**
- **\$2 billion** in revenues in 2012, representing 25% of the company's revenues
- Largest source of **company growth** in the past two decades

Unlocking Shared Value in Products and Markets

- Rethink the business around **unsolved customer problems or concerns**, not traditional product definitions
- Identify customer groups that have been **poorly served** or **overlooked** by the industry
- Think in terms of **improving lives**, not just meeting customer “needs”
- Start with **no preconceived constraints** about product attributes, channel configuration, or the economic model of the business (e.g., small loans are unprofitable)

Redefining Productivity in the Value Chain



- Purchasing that **enhances supplier capabilities** and **efficiency**
- Improving **energy** 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

Intercontinental Hotels Group

- **Energy** represents the **second highest cost** in a hotel, with water and waste also significant
- IHG introduced the **GreenEngage program** in 2009 to address its environmental footprint as an efficiency improvement opportunity
 - A **wide array of options** for improvement and tools for franchisees to assess return
- More than 1,900 IHG hotels are using the Green Engage **online tool** to enhance performance



- IHG hotels have achieved energy savings of **up to 25%** so far
- The effort has **improved differentiation** with consumers and corporate clients

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
 - **4000 households** have significantly increased their income



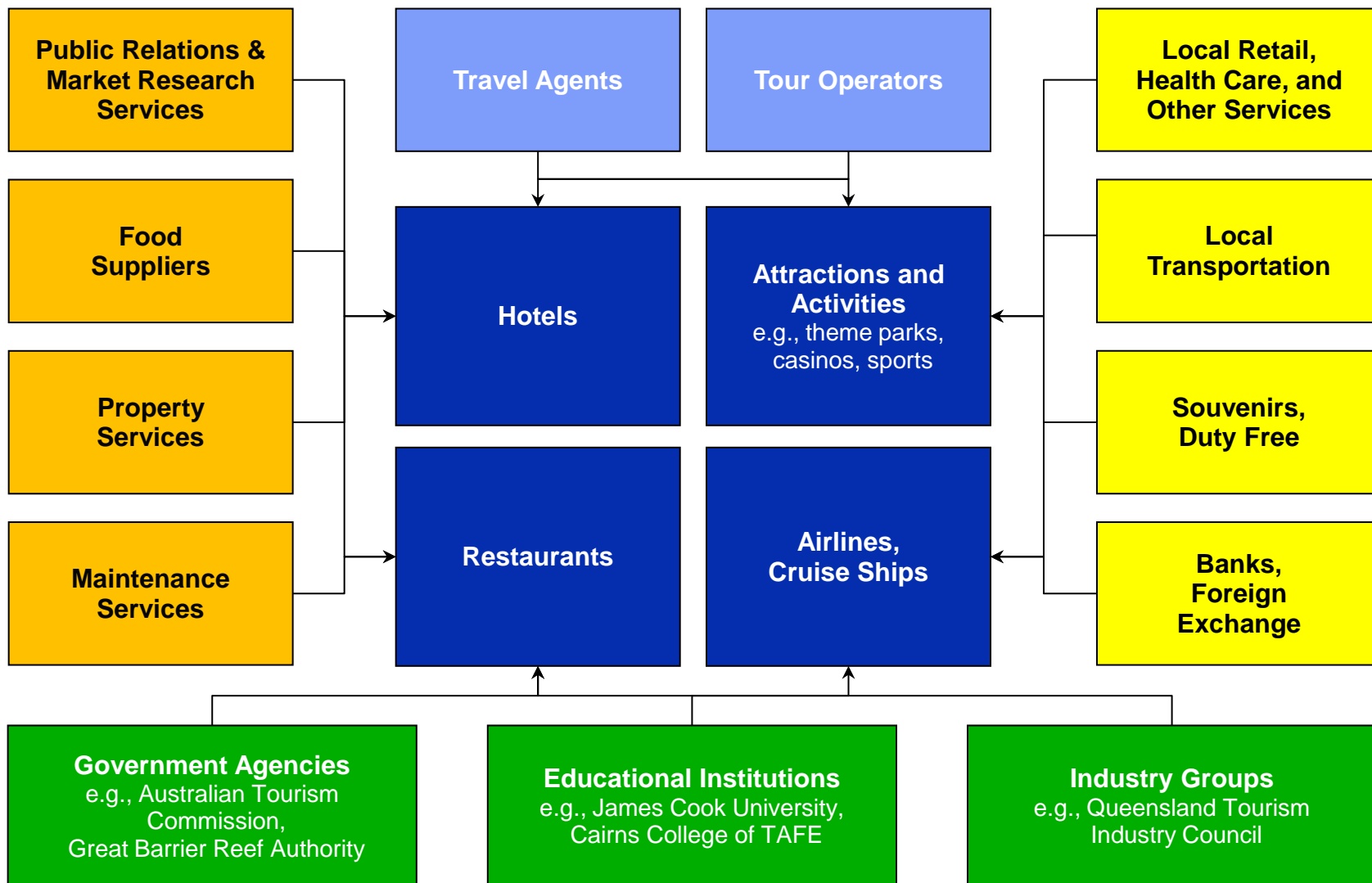
- Fibria achieves far greater efficiency versus old growth forest production, with eucalyptus yielding **30 times higher** yield per acre of wood pulp
- Small scale producers contribute 27% of the **raw material** volume utilized in Fibria mills, improving efficiency

Improving the Business Environment in the Company's Major Locations

- Companies, working individually and collaboratively, can catalyze major improvements in the **local business environment** in the regions in which they have major operations
 - E.g., supplier availability, supporting institutions, infrastructure, and regulating framework
- Building a **strong local cluster** improves company productivity and growth while raising regional competitiveness
 - This **strengthens the link** between a company's success and community success

Improving the Business Environment: Cluster Development

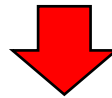
What is a Cluster?



Improving the Local Business Environment

Cisco Networking Academy

- Cisco established the **Networking Academy** to train network operators
- The company has trained **4 million** young people from all backgrounds in **165 countries** in ICT skills
- 70% of graduates have attained a **new job** or a **better job**



- The program **strengthens relationships** with key suppliers, local businesses and government
- The Networking Academy has alleviated a **key workforce constraint** for Cisco customers and the company, increasing industry growth

Improving the Business Environment: 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**

Leveraging Shared Value Across Levels

Pharmaceuticals and Medical Devices

Reconceiving Products and Markets

- R&D for drugs, vaccines, and devices that **fill unmet health needs**
- Modification of **existing products** to reduce complexity and cost
- **Tailored product offerings** to meet local market conditions

Redefining Productivity in Value Chain

- **Efficient, local supply chains** and **manufacturing** to reduce production costs
- **Locally-adapted sales and distribution** to reduce cost, access new markets, and better meet patient needs

Enabling Local Cluster Development

- **Behavior-change campaigns** to create more sophisticated consumer demand for health care
- **Strengthening local health systems** to enable the delivery of needed products and services
- **Advocacy and capacity building** to improve the regulatory environment



- Leading firms are beginning to design **multi-level approaches** to harness this **multiplier effect**

Novartis Arogya Parivar Initiative

Rural India

Reconceiving Products and Markets

- Portfolio of the **appropriate and affordable medicines** from its originals, generics, and over-the-counter (OTC) businesses
- Adapted packs of some OTC medicines (appeal and size) to address limited consumers' ability to spend out-of-pocket on healthcare

Redefining Productivity in Value Chain

- **Local sales teams** that know the culture and speak the dialect, which provided access to crucial market intelligence and reduced mistrust
- Dense **network of local distributors** to reduce stock-outs

Enabling Local Cluster Development

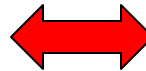
- **Community health education** program to address lack of health-seeking behavior
- **Frequent health camps** with physicians brought into rural areas
- Microfinance partners to improve healthcare infrastructure and access to working capital

Mutual Reinforcement Across Levels

Becton Dickinson Health Worker Safety

Reconceiving Products and Markets

- Redesigned syringes to prevent accidental sharps injuries
- Invested ~\$1 billion in product design and manufacturing capacity

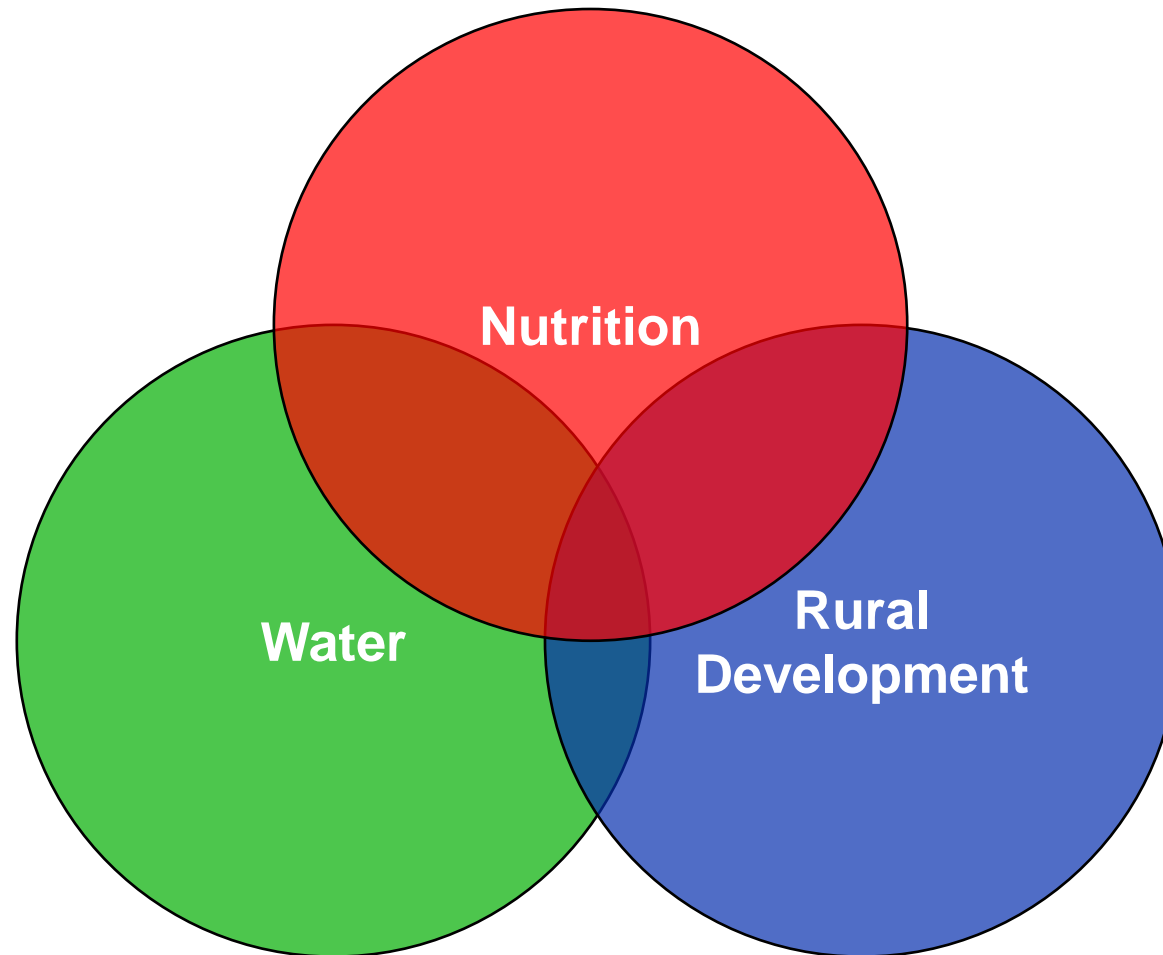


Enabling Local Cluster Development

- Engaged with leading experts and advocates
- Funded training of health workers in hospitals and clinics
- Developed a surveillance system to monitor accidents of needle pricks in the U.S.
- Advocated to policy changes to require safe devices

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

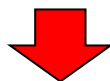
Dow Chemical

- 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**

Measuring Shared Value

- Measure the **direct link** between social impact and economic impact
 - Line of sight
- Measures are **unique** to the type of shared value being created
- The shared value being created is **intentional** and **focused**

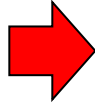


- Some stakeholders still believe economic success is **inconsistent** with social benefit

Partnering for Shared Value

NGOs

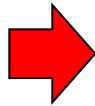
- Hold business accountable
- Seek donations



- Partner with business to **implement** and **scale** shared value solutions

Government

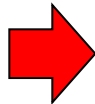
- Regulate how businesses operate
- Operate social programs
- Tax businesses



- Regulate to **encourage** market solutions
- **Partner** to deliver shared value solutions to social services
- **Jumpstart market solutions** through purchase commitments or subsidies
- Invest in **infrastructure** to enable shared value approaches (e.g. roads, skills)

Foundations

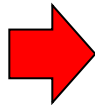
- Donate to charitable causes



- Invest **with** companies, NGOs and government to enable shared value solutions

Competitors

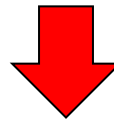
- Donate to charitable causes
- “Brand” social initiatives



- **Partner** on business environment improvements

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 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

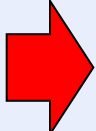
Distinctive Activities

- 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**

From Product to Purpose

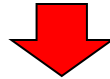
	<u>Traditional Positioning</u>		<u>New Positioning</u>
Nestlé	<ul style="list-style-type: none">• Food and Beverage Company		<ul style="list-style-type: none">• Nutrition Company
Nike	<ul style="list-style-type: none">• Footwear Company		<ul style="list-style-type: none">• Health and Fitness Company
Thermo Fisher	<ul style="list-style-type: none">• Scientific and Laboratory Instruments Company		<ul style="list-style-type: none">• Making the World Healthier, Cleaner, and Safer

- 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

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**

Additional Slides

Some Roles of Government in Creating Shared Value

- **Spur innovation** through regulatory design and co-investment in research and development
- **Jumpstart markets** by committing to purchase or subsidize a minimum volume of products
- Create **supporting infrastructure** (e.g., roads, training, property rights)
- **Provide bridge capital** by financing the private sector and NGOs to develop shared value solutions