

The New Competitive Advantage: Creating Shared Value

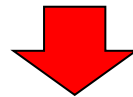
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The ideas drawn from “Creating Shared Value” (*Harvard Business Review*, Jan 2011) and “Competing by Saving Lives” (FSG, 2012). No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means—electronic, 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

- Only business can **create economic prosperity**
- Societies are facing significant **social and environmental** challenges
- Business is facing **growing scrutiny** as the cause or a contributor to many of these challenges
- Corporate social responsibility efforts are greater than ever, but the **legitimacy of business has fallen**
- Government and NGO's **lack sufficient resources and capabilities** to fully meet the challenges alone



We need a **new approach**

The Role of Business in Society

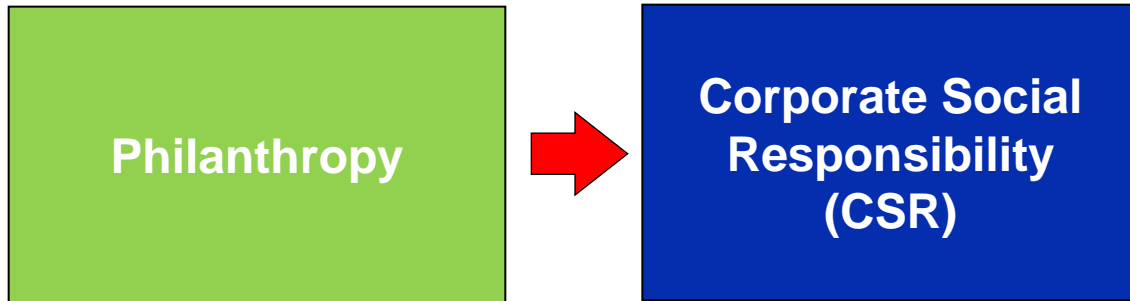
Evolving Approaches

Philanthropy

- Donations to worthy social causes
- Volunteering

The Role of Business in Society

Evolving Approaches



- Donations to worthy social causes
- Volunteering

- Compliance with community standards
- Good corporate citizenship
- “Sustainability”



- Mitigate risk and harm

The Role of Business in Society

Evolving Approaches



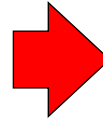
CSR versus Shared Value

Fair Trade



Fair Trade

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



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

Social Needs and Economic Value Creation



- **Social** deficits and **environmental** impact create **economic** costs for companies
- **Community** weaknesses affect company productivity
- Social needs represent the **largest market opportunities**

Levels of Shared Value

I. Reconceiving **needs**, **products**, and **customers**

- Meeting **societal needs** through products
- Serving **unserved or underserved** customers

II. Redefining **productivity in the value chain**

- Utilizing resources, energy, suppliers, logistics, and employees **differently**

III. Improving the **local business environment**

- Improving **workforce skills**, the **supplier base**, the **regulatory environment**, and **supporting institutions** in the communities and regions in which a company operates
- **Strengthening the cluster** in which the company operates while improving company productivity



- Strengthens the link between **company** success and **community** success

Creating Shared Value in Products and Markets

Jain Irrigation Systems

- **Drip irrigation equipment** for small farmers in India and Africa
- 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 is now a **\$820 million** company that is rapidly growing

Creating Shared Value in Products and Markets

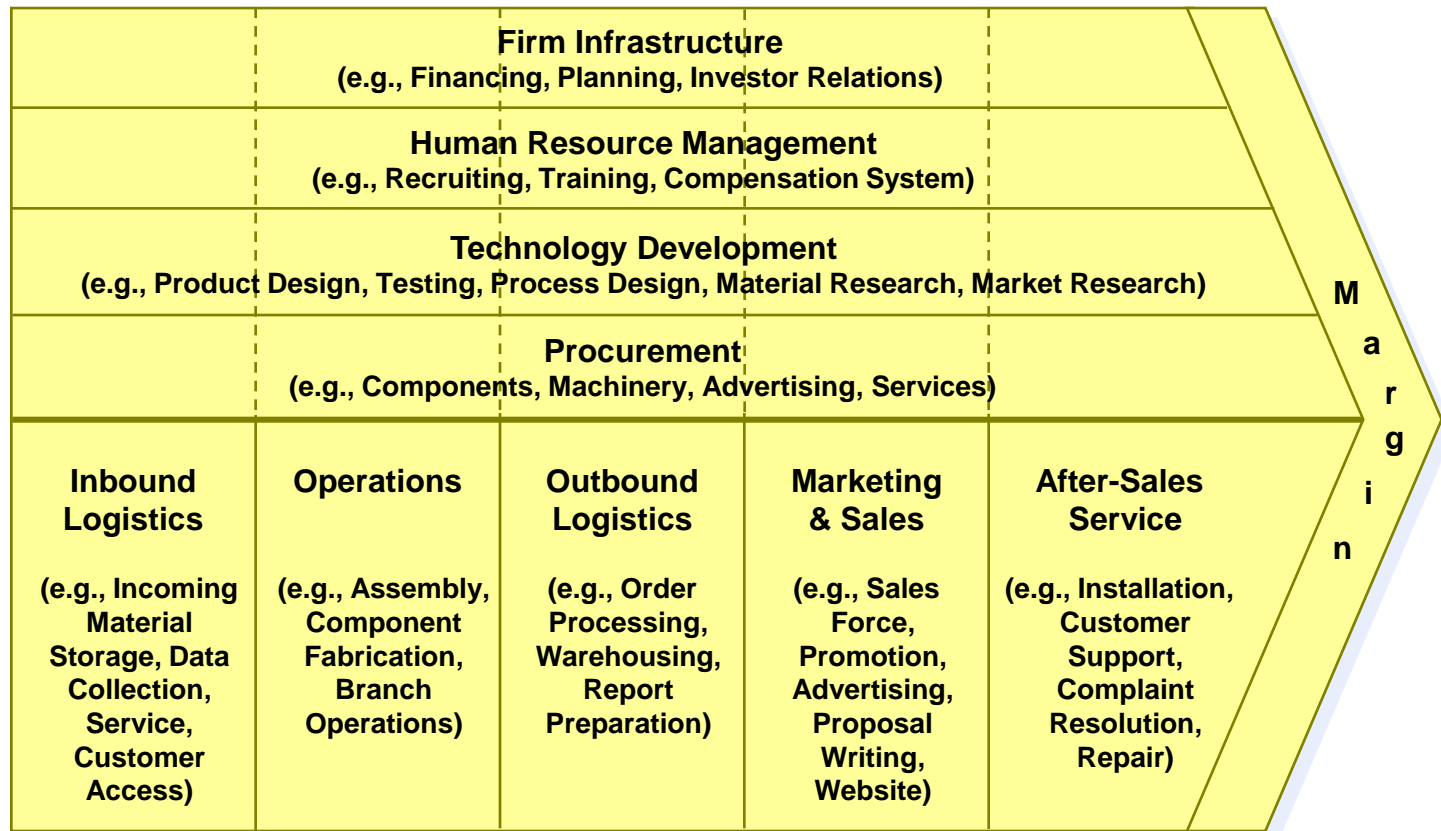
Novo Nordisk in China

- **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 and treatment
 - The program has **trained 55,000 physicians** to date
- 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 has become the company's third largest market with revenues of \$935 million in 2011

Shared Value in the Value Chain



- Procurement that enhances **supplier capabilities** and **efficiency**
- Improving **energy, water** and **resource** efficiency across the value chain
- 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
- Others

Shared Value in the Value Chain

Fibria, Brazil

- Fibria, the world's leading manufacturer of chemical pulp, utilizes **planted eucalyptus trees** rather than harvesting native and old growth forests, and cultivation methods that incorporate partial native habitat on Fibria land
- 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 land and water efficiency versus old growth forest production and traditional plantation methods
- Small scale producers currently contribute 27% of the **raw materials** utilized in Fibria mills, improving efficiency
- **4000 households** have significantly increased their income

Redefining Productivity in the Value Chain

Intercontinental Hotels Group

- **Energy** represents the **second highest cost** in a hotel, with water use and waste also significant
- IHG introduced the **GreenEngage program** in 2009 to address its environmental footprint as an efficiency improvement opportunity
 - The program led to a **wide array of options** for improvement, and tools for franchisees to assess the ROI in each area
- More than 1,900 IHG hotels are using the Green Engage **tools** to enhance environmental and economic performance. IHG is tracking results



- IHG hotels have achieved energy savings of **up to 25%** to date
- **Differentiates** IHG hotels with consumers and corporate clients

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**

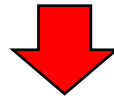


- Participating retailers register **sales increases of 25%** or more, with improved customer satisfaction, leading to similar **increases in the sales of Arca's products**
- Arca Continental **recovers its investment** in 6 months or less
- Beginning in **Mexico**, the program is being extended to **Argentina** and **Ecuador**

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**

Integrating Strategy Across Levels

Novartis in Rural India

Reconceiving Products and Markets

- Portfolio of the **appropriate and affordable medicines** drawn from the company's patented, generics, and over-the-counter (OTC) businesses
- Packaging of OTC medicines to reflect consumers' limited spending power

Redefining Productivity in Value Chain

- Localized sales teams that know the culture and speak the dialect, understand needs and reduce mistrust
- A dense **network of local distributors** to reduce stock-outs

Enabling Local Cluster Development

- **Community health education** programs to address lack of health-seeking behavior
- **Frequent health camps** for physicians in rural areas
- **Microfinance partners** to improve healthcare delivery infrastructure and access to working capital

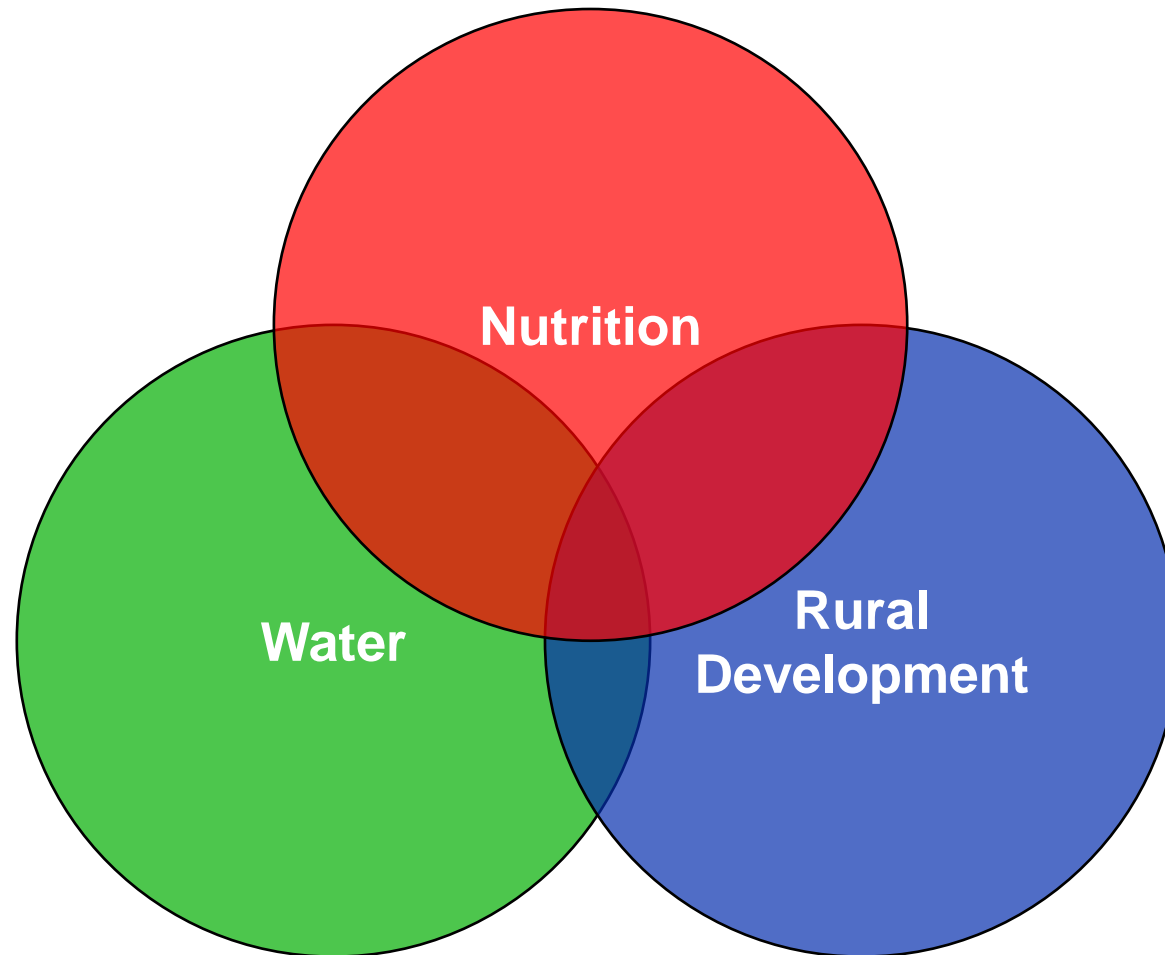
Connecting the Dots



- **Platform investments** to enable shared value approaches:
 - Educate
 - Research
 - Invest in enabling assets and infrastructure
 - Incubate
- **Engaging stakeholders** to collaborate on societal problems
- Address societal needs and challenges with a **business model**

Creating Shared Value: Deciding Where to Concentrate

Nestlé

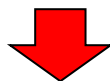


- Opportunities to create shared value are **inevitably tied closely** to a company's particular businesses

Putting Shared Value Into Practice

Dow Chemical

- Dow has a legacy of **innovation to solve problems** (“solutionism”)
- It recognized that global social issues represent **huge market opportunities**
- 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

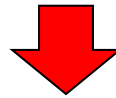
- Dow developed **Omega-9 canola and sunflower seeds** that produce cooking oil with no trans fats and low saturated fats
- The technology yields **twice the oil per hectare** for farmers than soybeans
- The oils have **longer** shelf life and usage life for food processors



- One of Dow’s biggest selling product lines with total revenues of approximately **\$700 million**

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 Company 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

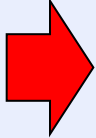
Distinctive Activities

- 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**

Purpose Based Strategic Positioning

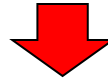
| | <u>Traditional Positioning</u> | | <u>New Positioning</u> |
|----------------------|---|--|--|
| Nestlé | <ul style="list-style-type: none">• Food and Beverage Company |  | <ul style="list-style-type: none">• Nutrition Company |
| Nike | <ul style="list-style-type: none">• Footwear and Apparel Company | | <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 **clear social purpose** opens up new opportunities for growth and profitability, while motivating and attracting consumers, business partners, employees, shareholders, and the public

Redefining Corporate Purpose

Danone

- In the late 1990's, 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**