

Reflections on a Hypothesis: Lessons for Policy and Corporate Practice

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Agenda

- How the “Porter Hypothesis” emerged
- What has changed
- Implications for continuing environmental progress in 2011
- Applying the principles to other societal issues

Origins of the Porter Hypothesis

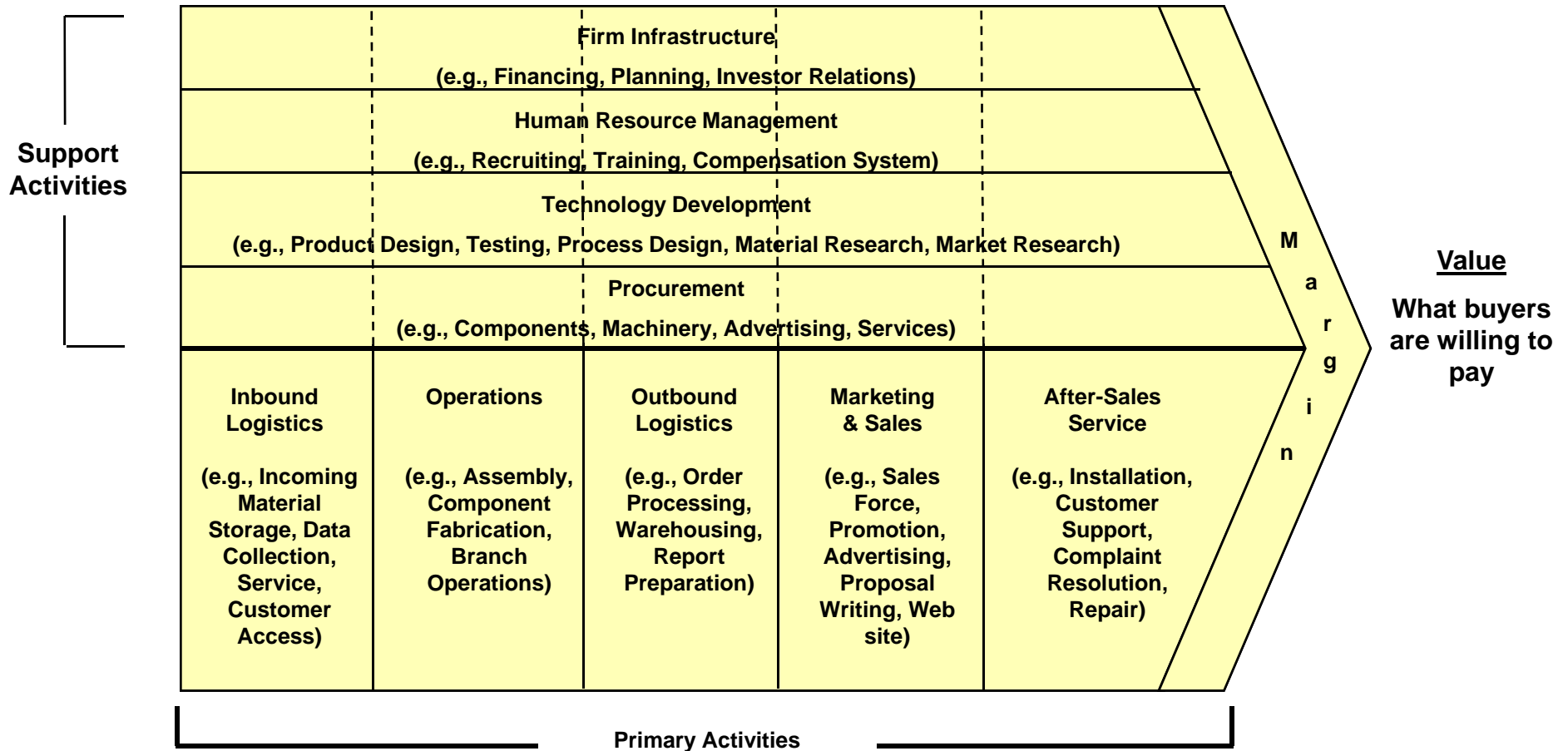
- An empirical observation



- Learning on the firm and competitive advantage
- Redefining the concept of competitiveness
- New thinking about the role of location in competitiveness

The Firm and Competitive Advantage

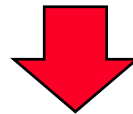
The Value Chain



- All competitive advantage **resides** in the value chain. Strategy is manifested in how activities in the value chain are **configured** and **linked together**

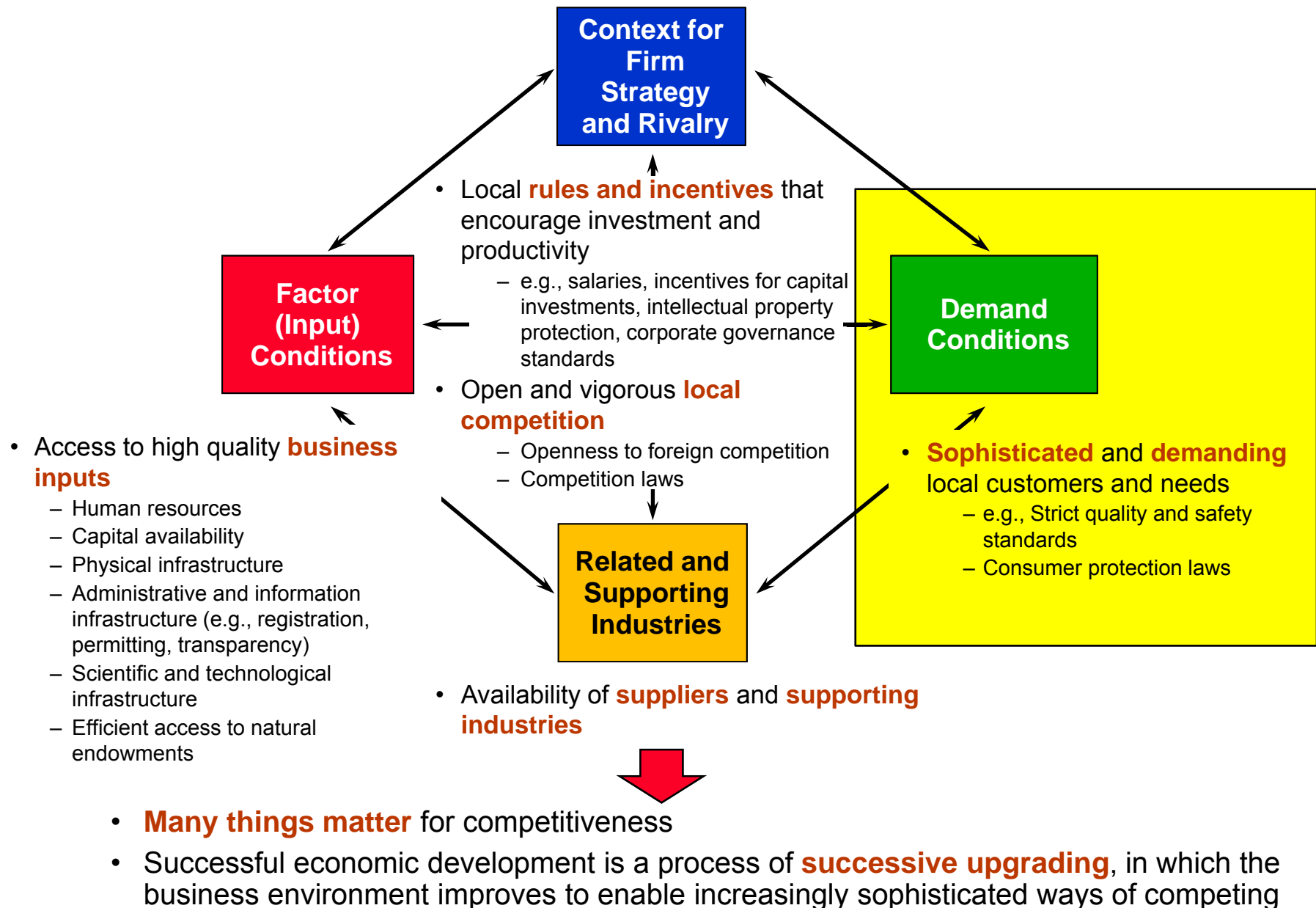
What is Competitiveness?

- Competitiveness is the **productivity** with which a nation uses its human, capital, and natural resources
 - Productivity **sets the standard of living**
 - Productivity growth sets **sustainable economic growth**
- Productivity and prosperity depend on **how** a nation competes, not what industries in which it competes
- **Relentless innovation** is necessary to drive **productivity growth** and enable standard of living to rise
 - Technology, products, and organizational methods



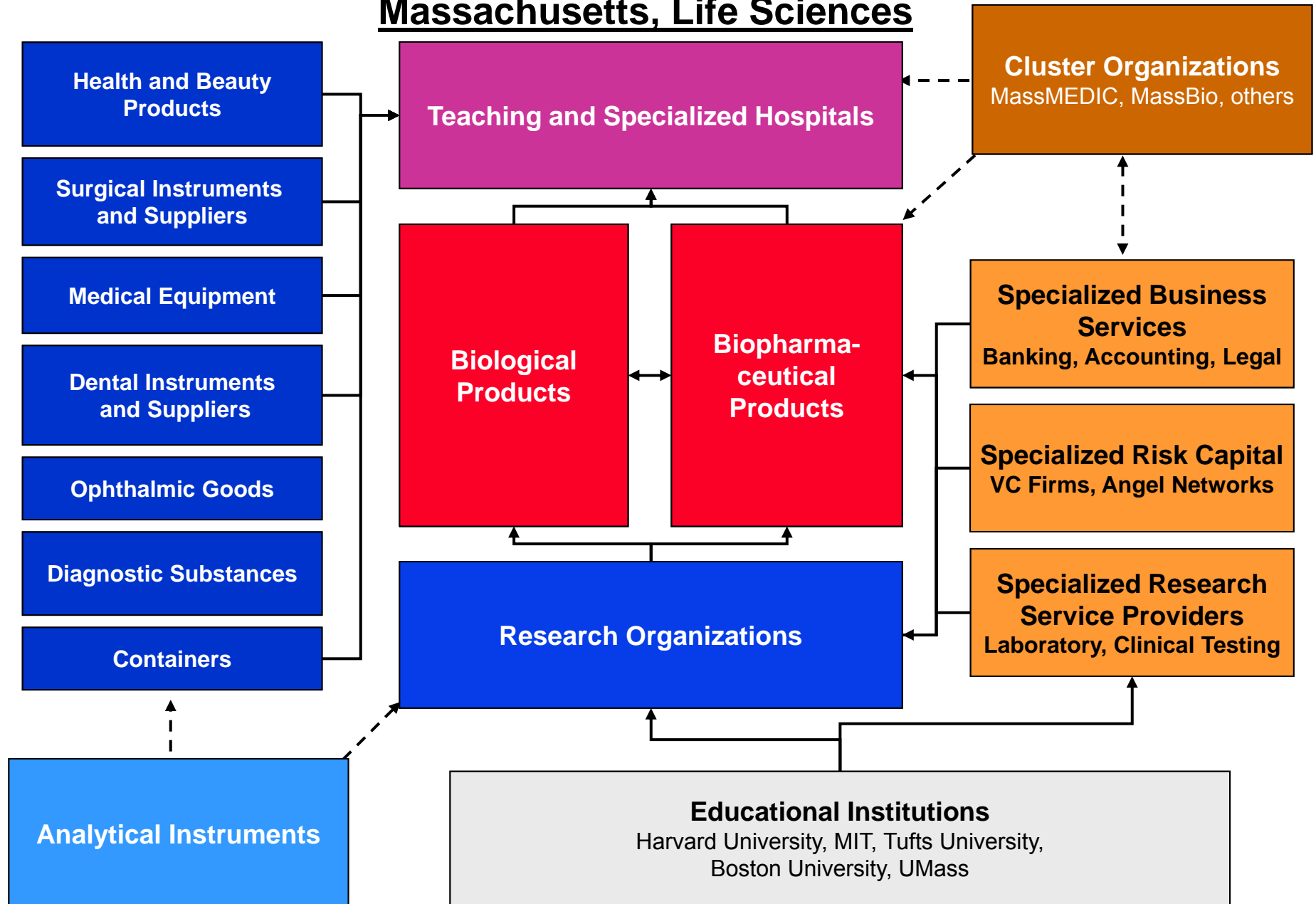
- Nations compete to offer the **most productive environment for business**
- The public and private sectors play **different but interrelated roles** in creating a productive economy

The Role of Location in Competitiveness



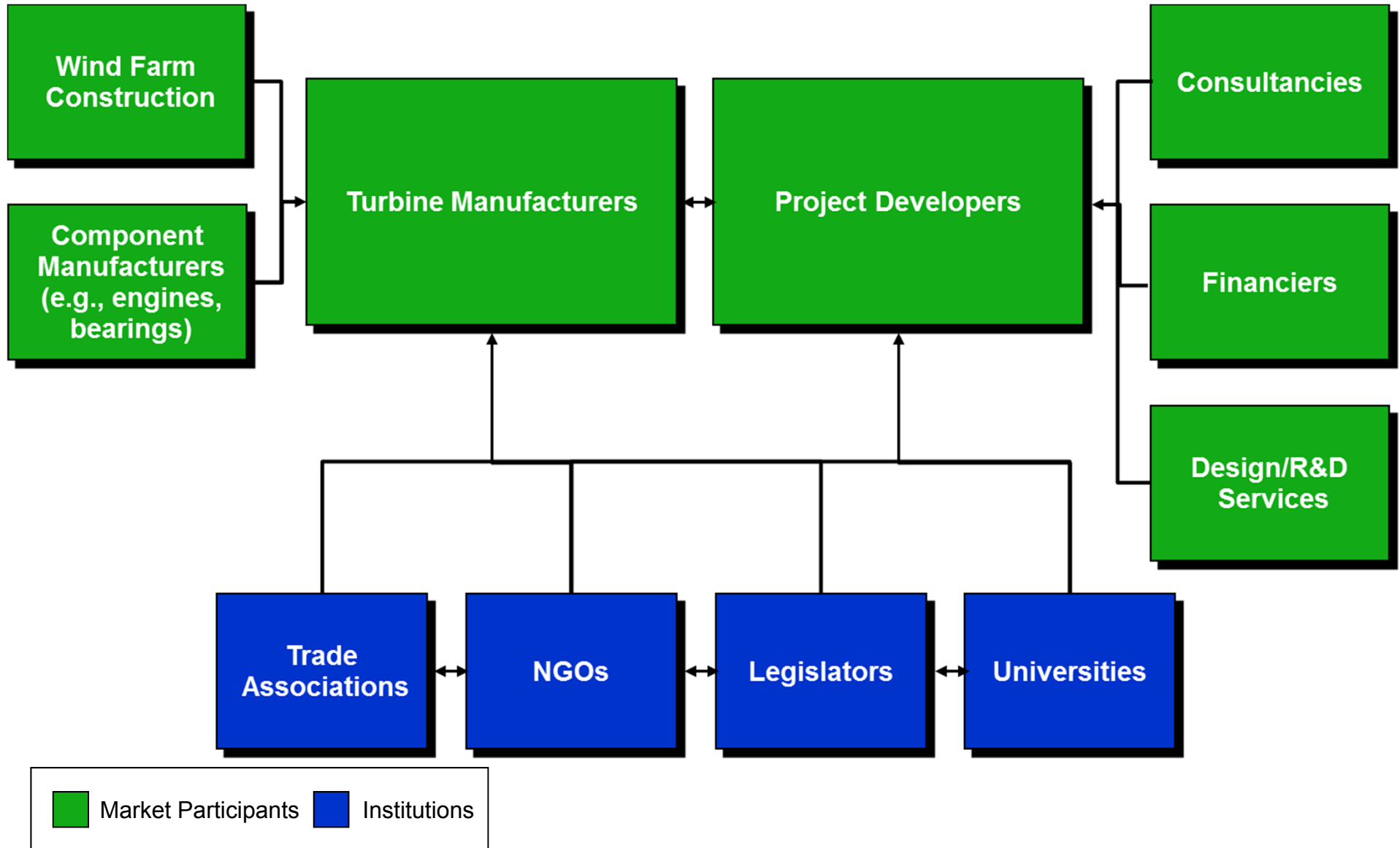
Clusters and Competitiveness

Massachusetts, Life Sciences



Clusters and Competitiveness

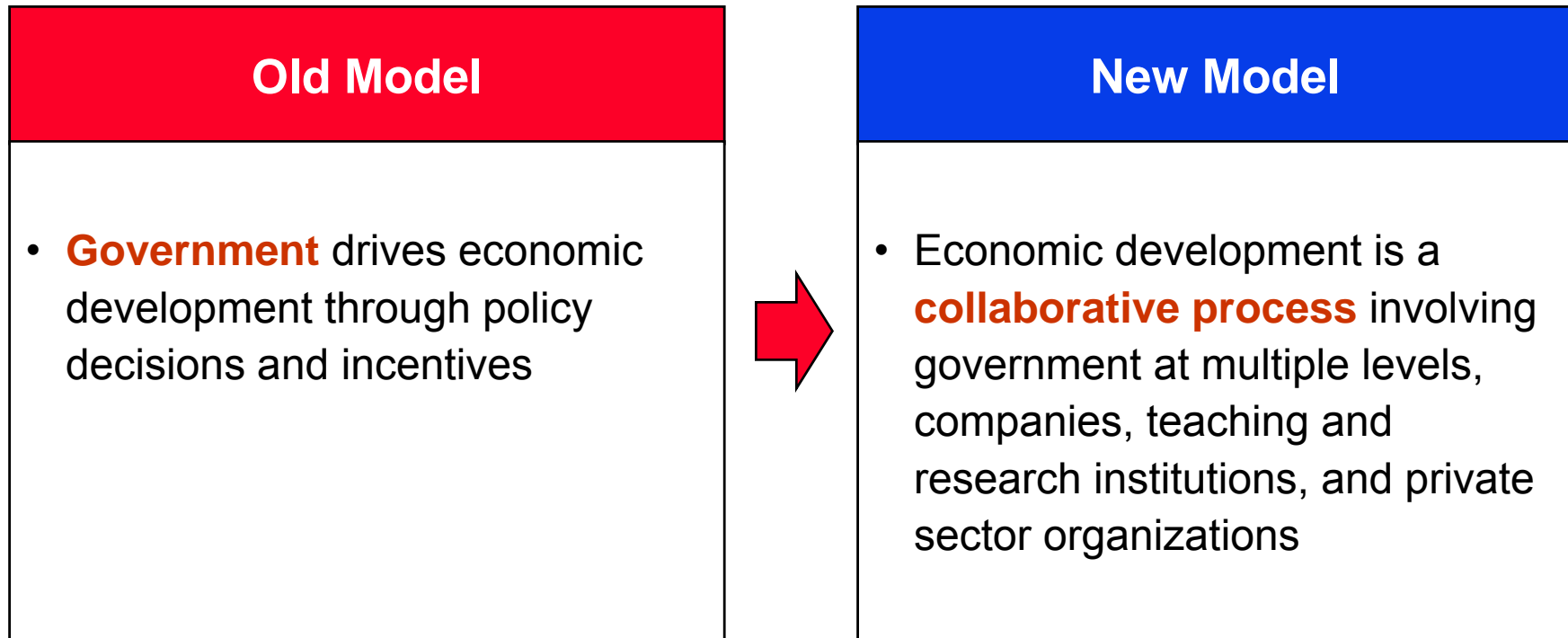
The Spanish Wind Energy Cluster



Source: Harvard student team - Emily Bolon, Matthew Commons, Frank Des Rosiers, Paz Guzman, Nicholas Kukrika (2007)

The Process of Economic Development

Shifting Roles and Responsibilities



- Competitiveness is the result of both **top-down** and **bottom-up processes** in which many individuals, companies, and institutions make relevant decisions

Porter Hypothesis: Developments Since 1991

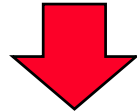
- Wide acceptance in **business**
- Principles embraced by some **regulators**
 - Innovation not abatement
 - e.g., outcomes not methods
- Learning by some **NGOs**
 - Leading NGOs are collaborating with the private sector
- Shift in **societal values**

BUT

- **Zero-sum thinking** persists
- Ongoing **political** obstacles to collaborative, innovation-based approaches

Implications for Policy

- Find and expand win-win opportunities



Regulation

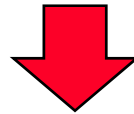
- Set **performance** standards rather than specify methods
- Utilize **phase-in** periods tailored to industry investment and new product cycles
- Ensure **predictable** evolution of standards over time
- Where appropriate, set **prices for resources** that reflect true cost
- Pursue national and international **harmonization** of regulations
- **Simplify** regulatory processes and make them less costly, less time-consuming, and more transparent
 - e.g., timely reporting and selective auditing, versus detailed and expensive compliance processes for everyone

Other steps

- Expand universal performance **measurement, reporting, and benchmarking**
- Harness **cluster/collaborative** improvement models
- Support **research** and diffusion of learning

Implications for Corporate Practice

- Some companies still treat environmental improvement as **CSR**, not as a tool to drive innovation and competitiveness



- Environmental innovation is a tool for **strategic positioning**, not just best practice improvement
- There are numerous opportunities for **cluster-based approaches** to improve environmental performance at lower cost

Economic Value and Societal Needs

Evolving Learning



- **Social** deficits create **economic** cost
- **External** conditions shape **internal** company productivity

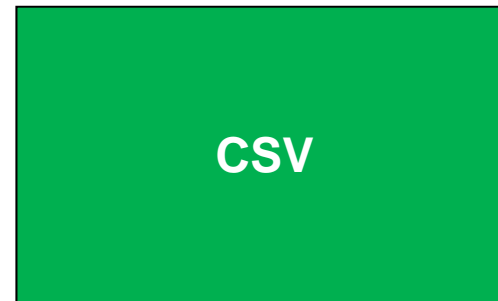
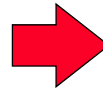
The Concept of Shared Value

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



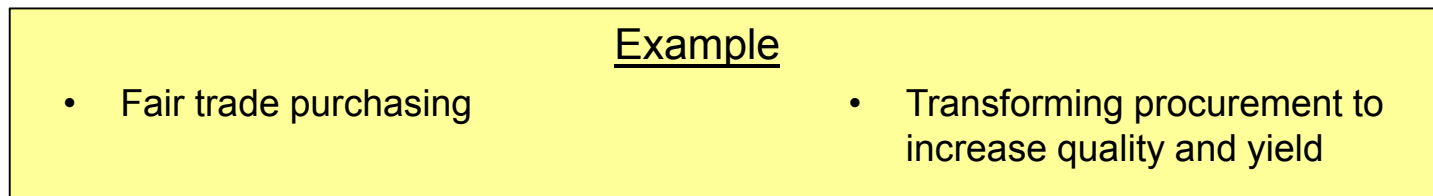
- Create **economic value** by creating **societal value**
 - What is good for the community is good for business

Moving to Shared Value



- Values: doing **good**
- Citizenship, **philanthropy**, sustainability
- Discretionary or in response to external **pressure**
- **Separate** from profit maximization
- Agenda is determined by **external** reporting and personal preferences
- Impact **limited** by corporate footprint and CSR budget

- Value: economic and societal **benefits relative to cost**
- Joint company and community **value creation**
- Integral to **competing**
- Integral to **profit maximization**
- Agenda is **company specific** and internally generated
- Realigns the **entire company budget**



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

Levels of Shared Value

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

Reconceiving Needs, Products and Markets

- Designing products and services to **address societal needs**
 - E.g., environmental impact, safety, health, education, living with disability, housing, financial security
- Opening new markets through serving the **unmet needs** in underserved communities and developing countries
 - Serving these markets often not only benefits customers but spurs social and economic development

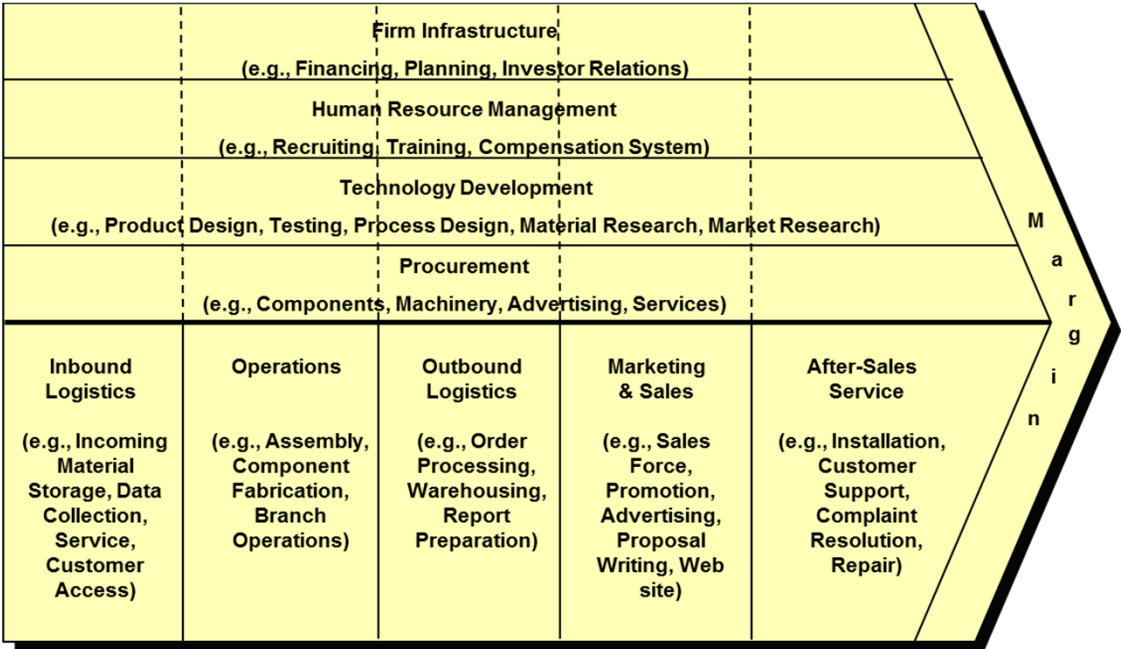


- These new needs and new customers are driving major opportunities for **innovation** and **differentiation**
- A new generation of **social entrepreneurs** is applying these new market principles
 - Corporations have largely sat on the **sidelines**

Redefining Productivity in the Value Chain

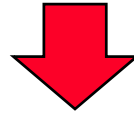
Opportunities

- Energy Use
- Logistics
- Resource Use
- Employee Productivity
- Location



Local Cluster Development

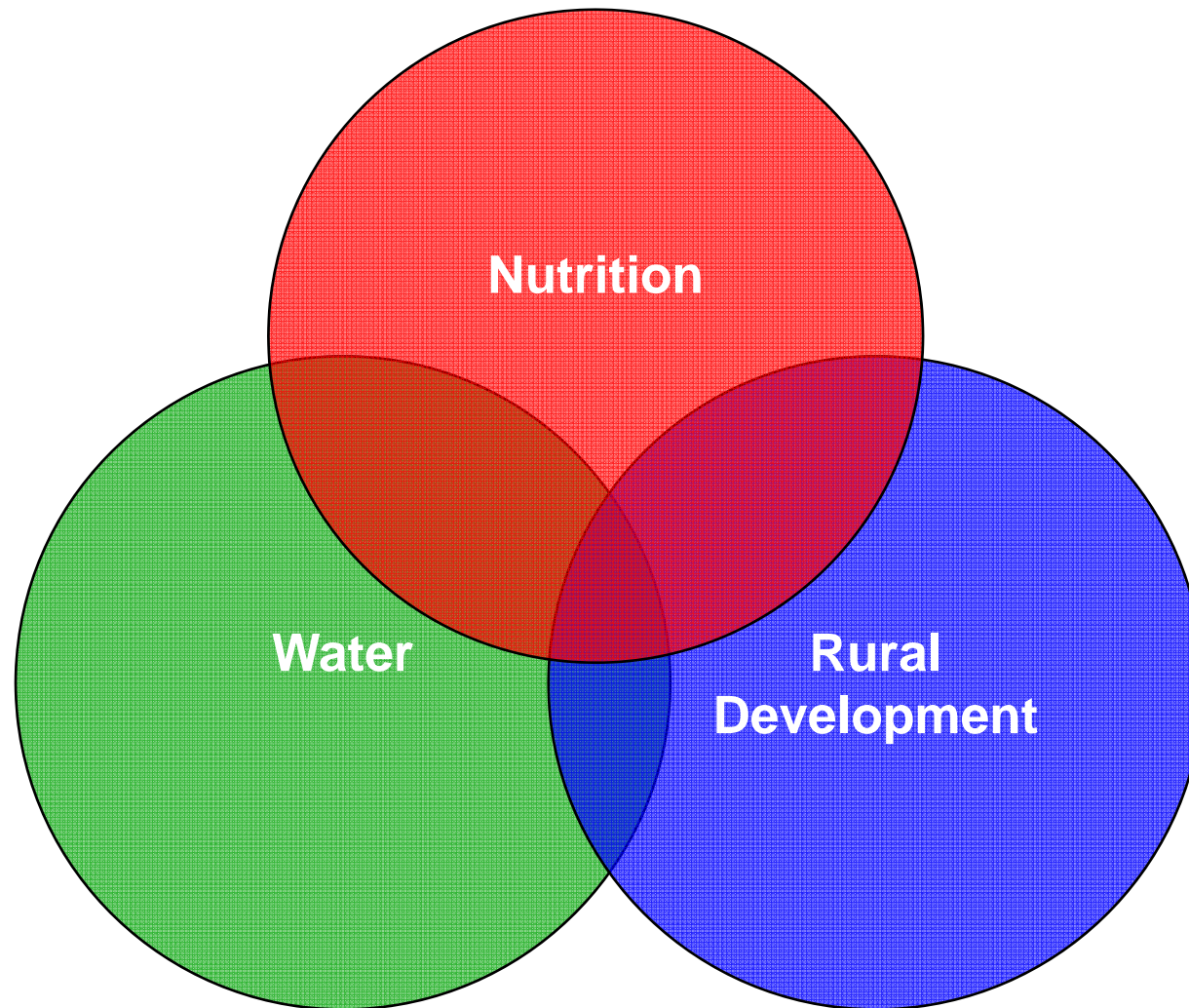
- A strong local cluster **improves company productivity**
- Companies, working with other actors, can have a substantial **positive influence** on local business environment conditions



- Cluster development **amplifies the link** between the company's success and economic development in the local community

Creating Shared Value: Deciding Where to Concentrate

Nestlé



Creating Shared Value

Nespresso

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

- Reconfiguring the value chain
 - Reconceiving procurement
- Upgrading the cluster
 - Supporting cluster development including cluster institutions
- Partnering with stakeholders

Shared Value

Farmers

- **Better yields**
- **Better prices**
- **Better processing**

Community

- **Environmental sustainability**
- **Economic development**

Nespresso

- **Stable supply**
- **Better quality**
- **Reinforces strategic positioning**

Adding a Social Dimension to Strategy

- Shared value opens up new **needs**, new **markets**, and new **approaches to configuring** value chains
- Opportunities for strategic positioning **proliferate**



- Companies should incorporate a **social dimension to their value proposition**
- Shared value can **reinforce** the company's unique strategic positioning
- This social dimension of strategy can be **more sustainable** 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 future strategies will embody a major **shared value dimension**

The Purpose of Business

- There is an opportunity to **transform thinking and practice** about the role of the corporation in society, using the concept of **shared value**
- 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 growth** in the global economy
- 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 to capitalism itself, and represents our best chance to **legitimize business again**