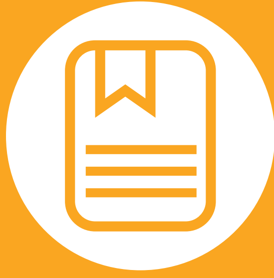

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The Ecosystem of Shared Value

Companies must sometimes team up with governments, NGOs, and even rivals to capture the economic benefits of social progress.

by Mark R. Kramer and Marc W. Pfitzer

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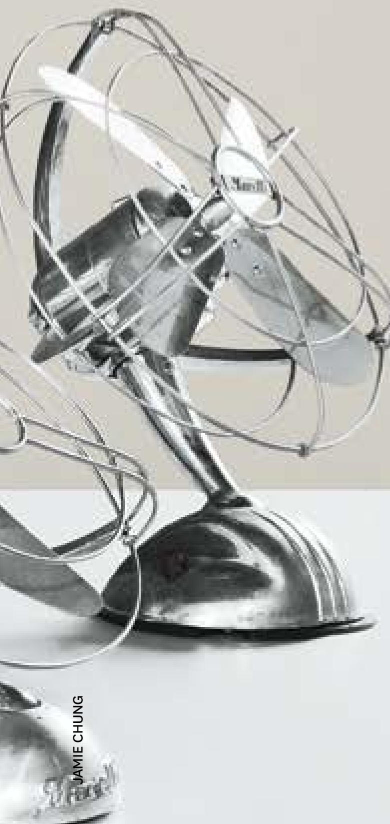
THE ECOSYSTEM OF SHARED VALUE

Companies must sometimes team up with governments, NGOs, and even rivals to capture the economic benefits of social progress.

BY MARK R. KRAMER AND MARC W. PFITZER



JAMIE CHUNG

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In the past, companies rarely perceived themselves as agents of social change. Yet the connection between social progress and business success is increasingly clear. Consider these examples: The first large-scale program to diagnose and treat HIV/AIDS in South Africa was introduced by the global mining company Anglo American to protect its workforce and reduce absenteeism. The €76 billion Italian energy company Enel now generates 45% of its power from renewable and carbon-neutral energy sources, preventing 92 million tons of CO_2 emissions annually.

And MasterCard has brought mobile-banking technology to more than 200 million people in developing countries who previously lacked access to financial services.

If business could stimulate social progress in every region of the globe, poverty, pollution, and disease would decline and corporate profits would rise. Indeed, in recent years *creating shared value*—pursuing financial success in a way that also yields societal benefits—has become an imperative for corporations, for two reasons. The legitimacy of business has been sharply called into question, with companies seen as prospering at the expense of the broader community. At the same time, many of the world's problems, from income inequality to climate change, are so far-reaching that solutions require the expertise and scalable business models of the private sector. Even corporations once known for a hard-nosed approach have embarked on significant shared value initiatives.

But as they pursue shared value strategies, businesses inevitably face barriers at many turns. No company operates in isolation; each exists in an ecosystem where societal conditions may curtail its markets and restrict the productivity of its suppliers and distributors. Government policies present their own limitations, and cultural norms also influence demand.

These conditions are beyond the control of any company—or of any single actor. To advance shared value efforts, therefore, businesses must foster and participate in multisector coalitions—and for that they need a new framework. Governments, NGOs, companies, and community members all have essential roles to play, yet they work more often in opposition than in alignment. A movement known as *collective impact* (introduced in 2011 by John Kania and Mark Kramer in the *Stanford Social Innovation Review*) has facilitated successful collaborations in the social sector, and it can guide companies' efforts to bring together the various actors in their ecosystems to catalyze change.

Companies that turn to collective impact will not only advance social progress but also find economic opportunities that their competitors miss. In this article we'll examine the principles of collective impact and explore its basic elements one by one. But first we'll take a broad look at how two very different companies—the Norway-based manufacturer Yara and the retail giant Walmart—have used collective-impact principles to improve their ecosystems for all concerned.

Reshaping the Ecosystem

Yara, a global leader in fertilizer sales, faced numerous obstacles in its effort to reach African smallholder farmers from its port of entry in Tanzania. Fertilizer had the potential to increase crop yields in the famine-afflicted country. But corruption in the government-controlled port delayed the unloading of shipments for many months. Roads were inadequate for conveying fertilizer to farms and produce back to the port; a third of the harvest was typically left to rot for lack of refrigerated transport. Farmers were poor, often illiterate, and unaccustomed to using fertilizer; they also lacked access to credit. A government ban on the export of key crops, meant to protect local consumption, had the unintended consequence of shrinking the market and curbing capital investment.

All this added up to a classic market failure that perpetuated famine and poverty and also curtailed Yara's growth. The problem was deeply entrenched:

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Idea in Brief

THE IMPERATIVE
Creating shared value—pursuing financial success in a way that also benefits society—has become increasingly important to companies as they look for new economic opportunities and seek to regain the public's trust.

THE BARRIERS
Companies don't operate in isolation. Each exists within an ecosystem where societal conditions may curtail markets and restrict productivity. Government policies and cultural norms present further limitations.

THE WAY FORWARD
Businesses must initiate "collective impact" efforts that involve all the players in their ecosystems. Five elements are needed: a common agenda, a shared measurement system, mutually reinforcing activities, constant communication, and dedicated "backbone" support from one or more independent organizations.

The farmers had little power to influence government policy, and they were suspicious of any changes to their traditional methods. International aid temporarily alleviated hunger but left the underlying issues untouched. No single intervention could prevail; success required that all the interrelated obstacles be addressed at once.

Starting in October 2009, Yara worked to bring together 68 organizations, including multinational companies, civil society groups, international aid agencies, and the Tanzanian government, in a partnership known as the Southern Agricultural Growth Corridor of Tanzania (SAGCOT), which was initiated at the World Economic Forum Africa summit in 2010. The mission was to build a $3.4 billion fully developed agricultural corridor from the Indian Ocean to the country's western border, covering an area the size of Italy. It has involved, among other things, investing in infrastructure, including the port, a fertilizer terminal, roads, rail, and electricity; fostering better-managed farmer cooperatives; bringing in agro dealers and financial services providers; and supporting agro-processing facilities and transport services. Public sources have provided one-third of SAGCOT's funding; the rest comes from the participating private enterprises. Although originally envisioned as a 20-year project, the corridor was well established within three years and has already bolstered the incomes of hundreds of thousands of farmers. Yara was decisive in launching the effort but did not lead or control it. Nor was the company's investment—$60 million—a major part of the funding. Yet the project has boosted Yara's sales in the region by 50% and increased the company's EBITDA by 42%.

Societal constraints are not limited to emerging markets, of course. In 2012, as Walmart was working to eliminate 20 million tons of greenhouse gas emissions from its supply chain and reduce its packaging costs, it encountered an unexpected roadblock: Its suppliers could not source enough recycled plastic to use in their packaging. It turned out that 45% of the U.S. population lived in cities that were still dumping trash in landfills. Even though recycling would have yielded significant new revenues and savings, cash-strapped municipalities could not afford the up-front investment required for collection and sorting equipment and for campaigns to change consumer behavior. So in April 2013 Walmart, like Yara, convened a cross-sector coalition of NGOs, city managers, recyclers, major consumer brand companies (including direct competitors such as Unilever and P&G), and financing experts from Goldman Sachs. Many of the participants had spent years trying to launch their own recycling programs; by the time they met, all recognized that the problem could be solved only by collectively addressing the challenge of financing municipal curbside recycling.

Together, 10 companies invested in the $100 million Closed Loop Fund, whose purpose is to catalyze investments in recycling infrastructure across the United States. It is governed by an independent committee of experts in finance, the environment, recycling, supply chain, and municipal management. Although it lends to municipalities and private companies at below-market interest rates, it insists that every proposal demonstrate the potential for commercially viable returns so that the model can eventually be scaled up through conventional capital markets.

To date the fund has financed 10 projects with a total of $80 million: $20 million of its own capital and $60 million from co-investors. As the result of one project, every household in Memphis, Tennessee—a city that had no curbside recycling whatsoever—now has access to convenient recycling carts. These 10 projects alone are expected to reduce annual waste

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to landfill by more than 800,000 tons and cut greenhouse gas emissions by more than 250,000 tons while creating hundreds of jobs. And the benefits to Walmart are considerable: The increased availability of recycled materials strengthens its supply chain and reduces the cost of packaging. Again like Yara, Walmart neither led nor controlled its cross-sector effort—but it provided the necessary impetus.

What Is Collective Impact?

Collective impact is based on the idea that social problems arise from and persist because of a complex combination of actions and omissions by players in all sectors—and therefore can be solved only by the coordinated efforts of those players, from businesses to government agencies, charitable organizations, and members of affected populations. What's needed is nothing less than changing how the system functions. Collective-impact efforts have made significant progress on issues as diverse as education, homelessness, juvenile justice, substance abuse, childhood obesity, job creation, and pollution.

Before engaging in a collective-impact effort, each participant has typically viewed the problem at hand solely from its own perspective. By bringing together all the relevant parties and ensuring rigorous data collection and careful facilitation, collective-impact initiatives foster a shared understanding of the problem—the first step toward solving it. If an initiative is to succeed, each entity must be represented by senior leaders with the authority to execute change within their organizations. Local communities affected by the problem must be included and empowered, and any data analysis or proposed actions must account for their perspectives.

Businesses bring essential assets to collective-impact efforts. They know how to define and achieve objectives within a limited time and budget. They understand change management and the art of negotiation. And corporate pragmatism, accountability, and data-driven decision making can cut through the red tape and ideological disagreements that often stymie governments and NGOs.

In addition to these considerable assets, businesses whose growth and resilience are constrained by societal problems have a powerful motive to kick-start social change. Conventional wisdom holds that governments and NGOs are the strongest catalysts of social progress, but that is not always true. Governments typically respond only to the most influential interests and may be paralyzed by partisan divides. Few NGOs have the resources and the clout to command attention from governments and global corporations, whose involvement is essential. But that doesn't mean that companies should try to lead or control an effort; it does mean they can be instrumental in getting it off the ground. Because collective impact mobilizes resources from many entities, businesses do not have to shoulder the massive costs of social transformation alone. And they can win big when new economic opportunities arise from social progress.

The Elements of Collective Impact

Five elements must be in place for a collective-impact effort to achieve its aim of large-scale social change: a common agenda, a shared measurement system, mutually reinforcing activities, constant communication, and dedicated "backbone" support from one or more independent organizations. Let's examine them in turn.

A common agenda. Participants must reach a shared vision for change and a joint approach to a solution. This not only helps align their efforts but also defines each organization's commitment and determines how data will be shared within and outside the group. The agenda must take each participant's perspective and interests into consideration. Not surprisingly, reaching agreement among numerous diverse stakeholders can be extremely challenging and may require six to 12 months or more of intensive work.

Just as companies should not lead or control a collective-impact effort, they should not try to impose an agenda. But they can initiate the process of reaching one, using their relationships to assemble key participants. The Closed Loop Fund, for example, emerged from a lengthy campaign—including an

COMPANIES THAT TURN TO COLLECTIVE IMPACT WILL BOTH ADVANCE SOCIAL PROGRESS AND FIND ECONOMIC OPPORTUNITIES THAT THEIR COMPETITORS MISS.

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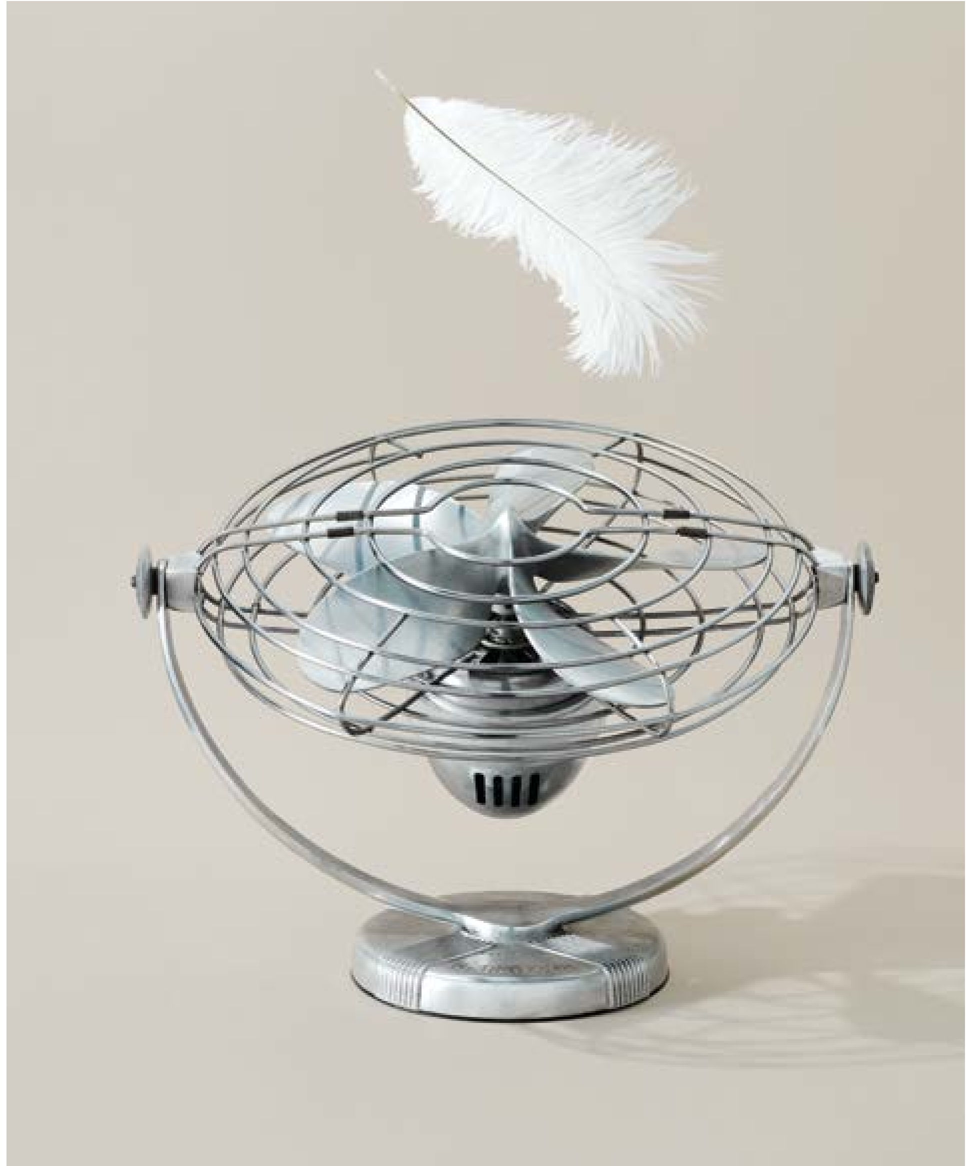

initial gathering of 30 consumer goods companies—to align numerous parties around a shared understanding of the problem and its solution. The idea of a social-impact fund using capital from participating companies arose in the very first meeting; however, developing the business case took eight months of work. Walmart CEO Doug McMillon played an instrumental role in the fund's launch: He asked his counterparts in major companies, including Procter & Gamble, PepsiCo, Unilever, Johnson & Johnson, Keurig Green Mountain, and Coca-Cola, to publicly commit to involvement. Another eight months of legal work ironed out the model—a limited-partnership structure with a fund management team in charge of reviewing and advising on city applications and an independent investment committee responsible for funding decisions. In October 2014, 18 months after the initial impetus, the fund closed its first round of financing and began issuing requests for proposals.

A shared measurement system. Participants must agree on a single short list of indicators that

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determine how success will be measured and reported. This helps formalize the common agenda, establishes a basis for understanding as a group what is or isn't working as each organization implements its activities, and sets the stage for ongoing course adjustments.

CocoaAction, a coalition similar to SAGCOT, brings together nine chocolate companies and numerous partner organizations to increase agricultural productivity and support communities in Côte d'Ivoire and Ghana. It spent two years establishing its agenda, goals, and measurements. The first step, as for SAGCOT, was recognizing the systemic challenges faced by farmers who operate at subsistence levels and were unable to invest in yield-enhancing innovations or in the community health and education practices needed for successful farming. Once the coalition had agreed on the imperative to address both farm productivity and community gaps, it could build consensus on performance measures. In May 2016 it released its guide to measurement and evaluation, which includes metrics for capturing farmers' adoption of recommended agricultural practices, soil fertility practices, and planting material; assessing the number of boys and girls in school; and gauging the number of women participating in income-generating activities.

Mutually reinforcing activities. Collective impact does not, of course, require that all participants do the same things. Instead, diverse stakeholders engage in mutually reinforcing activities. Each organization focuses on what it can do best. Typically, initiatives form multiple working groups, each addressing a different aspect of the problem.

Through their supply and distribution chains, businesses are deeply practiced in coordinating hundreds of organizations with different specialties. They can clearly evaluate participants' strengths and weaknesses while offering their own functional expertise.

IN COLLECTIVE-IMPACT EFFORTS, DIVERSE STAKEHOLDERS ENGAGE IN MUTUALLY REINFORCING ACTIVITIES, AND EACH ONE FOCUSES ON WHAT IT CAN DO BEST.

At SAGCOT, the long-term vision determined the sequence of investments and activities, starting with broad infrastructure improvements. Better roads and a more efficient port had to precede investments in refrigerated transport and increased yields. The Tanzanian government ended its export ban, waived taxes on irrigation equipment, eliminated a crop tax, generated new land-use plans, and spent $211 million modernizing the port. Aid agencies financed roadwork and facilitated farmer co-ops. Yara focused its direct investment on port infrastructure and agro-dealer networks—areas in which it had extensive knowledge from its activities in other parts of the world. To help coordinate the initiative, it drew on its experience with global agricultural markets and its work in Tanzania and other African countries in conjunction with the UN Millennium Project's Hunger Task Force and the Tanzanian Agricultural Partnership.

For the Closed Loop Fund, gaps in the recycling value chain of cities have determined the projects undertaken. These range from curbside collection supervised by municipalities to materials processing and manufacturing by private operators. And for CocoaAction, the national governments approve and help finance specific interventions; Mars, Nestlé, and other chocolate manufacturers are leveraging decades' worth of research on plant science and dissemination; Cargill, Olam, Barry Callebaut, and other cocoa processors and exporters are building the capacity of cooperatives; and the International Cocoa Initiative, CARE, and other NGOs are tackling child-labor monitoring systems.

Constant communication. All players must engage in frequent and structured communication to build trust and coordinate mutual objectives. Building trust among NGOs, governments, and competing businesses is not easy; however, constant communication and consistent follow-through on commitments can overcome even long-standing suspicions. Communication also fosters legitimacy, momentum, and learning.

Companies bring expertise in effective messaging for diverse audiences and have sophisticated in-house communication teams. SAGCOT, the Closed Loop Fund, and CocoaAction have all benefited from high-profile events set up by champion companies.

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CREATING SHARED VALUE

In the 2011 HBR article "Creating Shared Value," Michael Porter and Mark Kramer argued that companies can move beyond corporate social responsibility and gain competitive advantage by including social and environmental considerations in their strategies. Treating societal challenges as business opportunities, they suggested, is the most important new dimension of corporate strategy and the most powerful path to social progress.

Shared value results from policies and practices that contribute to competitive advantage while strengthening the communities in which a company operates. Companies can create shared value in three ways: by reconceiving products and markets, redefining productivity in the value chain, and strengthening local clusters. All three require a sufficiently robust market ecosystem. A collective-impact approach may not always be needed for the first two activities, but it is always necessary at the cluster level.

SAGCOT, a member of the World Economic Forum, gains exposure and commitment at the forum's yearly conference in Davos, Switzerland. Walmart used the CEO's bully pulpit at its 2014 Sustainable Product Expo in Bentonville, Arkansas, to enlist its suppliers in the Closed Loop Fund. And CocoaAction has used Barry Callebaut's annual Chocovision conference to mobilize partners and heighten the urgency for change.

At the operational level, each coalition issues regular updates and schedules meetings for its working groups and investors. SAGCOT holds an annual partnership forum and more-frequent regional-cluster meetings, while the Closed Loop Fund and CocoaAction convene each quarter. The fund's communications often draw on the technical expertise of businesses. For example, as investments make possible the processing of new streams of recycled packaging material, the participating companies discuss how to foster markets that can get the material into packaging supply chains—which requires a sophisticated understanding of quality and quantity specifications and of geographic and transportation constraints.

Dedicated "backbone" support. A separate, independently funded staff dedicated to the initiative—the "backbone" of the project—is needed to guide vision and strategy, support activities, establish shared measurement practices, build public will, advance policy, and mobilize resources. These activities can be managed by a single organization or divided among several with differing competencies. The backbone function ensures that all the working groups remain aligned and informed. Companies cannot be the backbone—they are not neutral players. They can, however, provide funding to launch it, technology support for online communication, and mentoring or coaching, in some cases introducing Six Sigma and other continuous improvement processes.

Although Yara initiated Tanzania's agricultural corridor, it was careful to avoid taking ownership or branding the effort as its own. The backbone is an independent secretariat—the SAGCOT Centre—whose initial CEO was a former head of the Tanzania National Business Council and whose deputy CEO was an associate director of the World Economic Forum. The Closed Loop Fund was likewise independently incorporated and staffed; its recycling experts have a deep understanding of the relevant technologies and economics. CocoaAction has entrusted its backbone to the World Cocoa Foundation, whose staff members are widely experienced in agricultural development and policy; the lead companies maintain strategic oversight through membership on the foundation's board.

Together these five elements—simple to describe, immensely challenging to implement—can ensure that the hundreds of organizations spanning the populations affected by a given social issue work together constructively despite vastly different perspectives, cultures, and ideologies. To realize that potential, collective impact requires a new kind of leadership, sometimes called *system leadership.* There is never just one system leader; multiple individuals, representing different constituencies, lead together.

System leaders must frame their own intentions and the overall situation in a way that motivates and builds trust among all participants. Even as they are accountable to their own organizations and keep their priorities in mind, they must help others in the

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coalition understand how the health of the whole system benefits each party. System leadership requires persistence and the ability to listen deeply and see reality through the eyes of other stakeholders.

Consider Ron Gonen and Rob Kaplan, cofounders of the Closed Loop Fund. Gonen led New York City's recycling program; prior to that, he started Recyclebank, a company that has promoted recycling in more than 4 million U.S. households. Kaplan spearheaded Walmart's efforts to reduce greenhouse gas emissions throughout its supply chain and was responsible for packaging sustainability. Together the two are experienced in all aspects of recycling and product supply chains—from municipal collection to retail procurement, and across business, nonprofits, and politics—giving them the credibility and insight to engage all parties. Such cross-sector experience is essential among system leaders and enables them to speak the language and appreciate the motivations of each sector.

A company's choice of the right internal champion for system leadership is critical both to bringing the company to action and to keeping the other partners focused on the common agenda. For example, Kaplan first helped Walmart appreciate the link between its emissions and broader recycling-system failures and then raised awareness among the company's product purchasers, helping them "see" the hidden savings that could be obtained by using recycled materials. And he was instrumental in helping McMillon secure public commitments from the CEOs and presidents of other corporations.

Why Business Misses the Opportunity

Despite their powerful incentives and unique capacity to support large-scale social change, companies rarely step up. Our research suggests that they encounter three obstacles.

Questions of legitimacy. Trust is a precondition for successful collaboration. And although companies are often respected, they are more likely to be feared than trusted. After all, they're in the self-interested pursuit of profit. So they may be viewed as not having the legitimacy to initiate social progress.

However, companies that pursue shared value and engage in collective-impact efforts recognize that their long-term profitability depends on a healthy society. They aim their strategies at achieving social outcomes that mesh with public priorities, such as the UN's Sustainable Development Goals. And, as we have said, they do not lead in any conventional sense; the participants collectively determine the agenda and the actions to be taken.

Competitive free riders. When one company improves the market ecosystem, it almost always improves conditions for its competitors. Nestlé spent 40 years working to raise the productivity of dairy farmers in Moga, India—efforts that not only strengthened its own business but also produced a cluster of thriving local competitors. Many companies are understandably reluctant to bear the costs when rivals will share the benefits.

But despite the free-ride opportunity, companies that create shared value often enjoy a sustained advantage. Take Novo Nordisk, the world's leading provider of insulin to manage diabetes. In the 1980s diabetes was virtually undiagnosed, and thus untreated, in China, even though nearly 10 million people there suffered from the disease. In 2002 the company established the World Diabetes Foundation and worked with the Chinese Ministry of Health, the Chinese Academy of Sciences, and others to train more than 200,000 health providers and educate more than 2 million patients. It funded medical research and a widespread media campaign to combat the social stigma associated with the disease. These efforts have saved some 500,000 "disability-adjusted life-years."

Novo Nordisk's actions unquestionably improved conditions in China for any insulin supplier; yet in initiating the change and building close relationships with suppliers, distributors, the government, and others, the company established a $1.3 billion market for itself and gained a commanding advantage that later entrants have been unable to weaken. It currently has a 59% market share in China; its larger global competitors, Eli Lilly and Sanofi, have Chinese market shares of just 15% and 5%, respectively. Similarly, although Yara's participation in SAGCOT improved conditions for any fertilizer company operating in Tanzania, the company saw its market share there rise from 35% to 52%.

Investment justification. Most companies relegate social issues to their philanthropy, citizenship, or CSR departments, thus perpetuating the separation of social problems from core operations and strategy. They rarely examine changing ecosystem conditions through the rigorous business lens that would reveal their significance to a company's financial prospects. Shared value

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BARRIERS IN THE ECOSYSTEM

Companies are accustomed to thinking of strategy in terms of the activities under their direct control. They recognize the importance of a broader market ecosystem, but research has focused on the ecosystem of competition or of "coopetition" among related companies rather than on the social factors that affect markets. Yet every company that pursues shared value in the face of inhospitable market conditions will encounter barriers in its ecosystem. Private- or public-sector intermediaries may be incapable of supplying basic infrastructure and services to end users—or those intermediaries may not even exist. Misaligned government policies or informal rules often perpetuate existing deficits, and ingrained behaviors and cultural norms may prevent the adoption of new solutions. The further a company looks beyond its own value chain to the causes of market failure—situations in which socioeconomic conditions prevent conventional business models from succeeding—the less control and perceived legitimacy it has, and the greater the cost, complexity, and time frame of change. These factors keep many companies from even contemplating an effort to alter the external context.

creation is a strategy that requires expertise in both societal *and* business issues; projects must be subject to the same analysis as any other capital investment. If companies do not accurately assess the business case for such projects, they will miss the justification for investing the required funding and management attention, which may greatly exceed those of normal philanthropic or CSR projects. If shared value projects are successful, however, the returns from ecosystem change may dwarf those from equivalent investments that companies would not hesitate to make in R&D or marketing.

Collective impact also requires a long-term vision and a commitment of resources that are insulated from quarterly or even annual review. Interim budget fluctuations can undermine the steady progress and trust necessary for collective-impact efforts. Although the total project costs may be large, they are borne by many participants, so they generally won't show up as a significant factor in any major company's financial statements and should not affect the short-term performance for which shareholders rigidly hold companies accountable. However, companies must tailor their investments to the nature and timing of the changes pursued. If they seek long-term results, for instance, then separate, special-purpose funds (Danone's Ecosystem Fund is one example) may be the most appropriate channel for investment.

SIMPLE PROBLEMS should be amenable to simple solutions. Binary partnerships with other companies, government agencies, or NGOs can often overcome one or a few obstacles in the local ecosystem. However, leading companies have begun to realize that addressing the complex social problems at the root of market failures is often the only way to achieve their ambitious shared value strategies. In such situations, the ability to understand and catalyze collective impact is essential.

The greatest impediments to this promise of social and economic progress are the internal barriers that prevent companies from taking action. Cost should not be a problem if the business case is well understood: In all the examples mentioned here, the initiating company garnered substantial economic returns and saw significant benefits to society from relatively modest capital investments. But corporate executives often lack the courage and the vision to wade into the social sector, engage openly with civil society, understand the business case, and pursue a longer-term strategy in cooperation with others.

Leading social change in the service of shareholder value is immensely challenging. The problems will take years to solve, and the results won't show up in the quarterly performance targets at which managers typically aim. Governments and NGOs won't always welcome corporate leadership. Yet businesses are essential players, able to unlock possibilities for change on issues that have long been impervious to intervention. Without their participation, we will neither meet shareholders' growth expectations nor remedy the world's most urgent social failures.

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