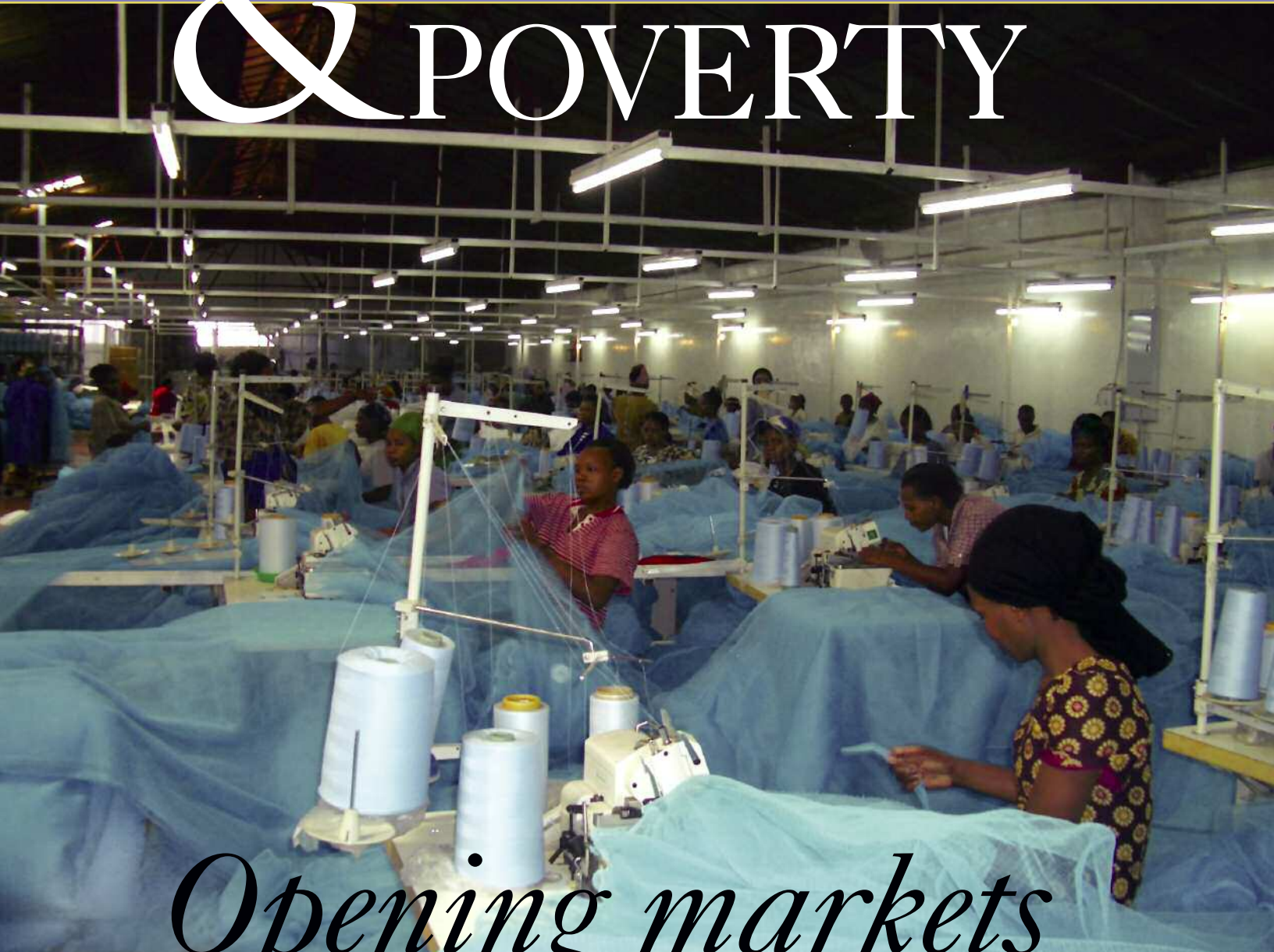


# CBUSINESS & POVERTY



*Opening markets  
to the poor*

*Guest Editorial*

DJORDJIJA B. PETKOSKI, V. KASTURI RANGAN, AND WILLIAM S. LAUFER

IN RECENT YEARS, business has played a significant role in alleviating poverty, especially in sectors such as telecommunications, information technology, and microfinance. Certain initiatives in these sectors, such as microfinance in urban Latin America and wireless telecommunication in Asia, have yielded impressive results, creating unrealistic benchmarks against which other corporate programs are being judged. Although businesses have made significant contributions in some sectors, in many others they have been unable to “move the needle” on poverty.<sup>1</sup>

It can be argued that the private sector may have contributed to broadening the gap between the rich and the poor and to environmental degradation, but business has also helped improve the quality of life in many low-income areas.<sup>2</sup> There have been quiet but strong links among economic growth, innovation, and development. This article is not intended to defend once again the fundamental economic rationale for capitalism and its potential role in alleviating poverty. Rather it is meant to bolster that premise with current examples and practices and to urge businesses to adopt a more proactive role in the



◀◀◀◀ Opposite page:  
Tanzanian factory  
workers sewing  
anti-malarial  
Olyset Nets in a  
joint venture  
between Japanese  
MNC Sumitomo  
Chemical and  
local manufacturer  
A to Z Textile Mills.

◀◀◀◀ Left:  
Owners of a home  
newly completed  
through participation  
in the progressive  
housing program  
for low income  
communities,  
Patrimonio Hoy.

development of markets that benefit the poor. Our perspective is that a company's responsibility is not only to increase its investors' wealth, but also to help create wealth for the 4 billion or so people at the Base-of-the-Pyramid (BoP) who make do with incomes of less than \$5 per day, as characterized in the article on the Next Four Billion.

Poverty is an economic, social, cultural, political, and moral phenomenon and we believe it is necessary to address these dimensions in an integrated fashion—one that contributes to sustainable global development. Nestlé's Milk District Model illustrates this approach. By providing opportunities for training, education, and a steady income to poor rural farmers in exchange for a consistent milk supply, Nestlé effectively integrated poverty alleviation into a business model that was mutually beneficial: the company has been able to increase its supply of fresh milk and poor communities have benefited from job security, improved nutrition, and a better standard of living.

There are many ways in which business can help in opening markets to the poor, ranging from multinational corporations (MNCs) and local small and medium enterprises (SMEs) to corporate foundations, business alliances, and small entrepreneurs from both developed and emerging economies.

## Business models that engage the poor

NEW BUSINESS MODELS have focused mainly on cost structure, innovative distribution methods, and logistics, and have ignored the need to develop market institutions. Productive corporate engagement at the BoP will require an in-depth understanding of the meaning of "market based solutions;" clarification of the types of markets (informal vs. organized markets); and understanding how companies can connect factor and product markets to help create job opportunities.

Companies, particularly large ones, can have a much greater impact on the BoP by contributing to the creation of more efficient markets and by complementing market institutions, rather than just selling products to the poor. In less developed countries, poverty alleviation should be approached primarily through wealth creation, including access to jobs, healthcare, education, and vocational training, even before providing access to consumable goods and services that improve the quality of life of the poor. Of course, wealth creation and consumption are complementary, but there is a hierarchy.

In building wealth, business models need to include mechanisms to deal with the following challenges:

- Increasing the productivity and real income of the poor.
- Enhancing job creation opportunities through direct employment or self employment, supported by products and services that boost productivity.
- Moving away from the "traditional consumers" concept to the concept of "productive consumers." (Developing self-esteem and dignity among consumers can be achieved both by creating conditions for employment and by paying decent salaries).<sup>3</sup>

How businesses address these issues depends on many factors, such as industry structure, company vision, size, loca-

tion and ownership structure. The lessons learned from company experiences can serve as building blocks in achieving innovative, sustainable, and scalable solutions.

Companies such as Nestlé, Unilever and CEMEX have shown that through innovative business solutions they can both operate profitably within a given (underdeveloped) institutional framework, and simultaneously directly facilitate the development and strengthening of market institutions. Unilever's experience with the "Shakti Revolution" in India illustrates that helping to empower underprivileged rural women by fostering entrepreneurship and creating income opportunities can be more important than sales alone, since it encourages the growth of a sustainable consumer base.

## Building a BoP business culture

TO BETTER ENGAGE THE POOR, business needs to understand their values, aspirations, and the contributions they can make to value creation for themselves and others. Only limited efforts have been made to change the sometimes deep-seated assumptions that business leaders make about the poor, assumptions that are partly caused by a wide cultural and socioeconomic divide and a lack of direct interaction.

Incorporating poverty alleviation into corporate strategy always requires internal change in companies, and sometimes even redefining organizational values and cultures. These changes may include developing an entrepreneurial spirit for, a clear vision of, and a readiness to support new and risky BoP ventures. Not only it is necessary to capture the attention of corporate executives and senior managers, but an effort must be made to explicitly connect business growth and profitability with BOP markets. As the case of Sumimoto Chemical illustrates, consistent corporate backing for BOP ventures can lead employees to identify innovative market based solutions. In Sumimoto Chemical's case, that solution came in the form of an insecticide infused mosquito net to protect vulnerable African populations against Malaria. The company's management philosophy, known as the "Sumimoto Spirit," aims to "generate profit not only for the company but also for society," and has helped motivate their employees to reach the BoP. Similarly, the multinational cement producer CEMEX chose to put an interdisciplinary team of its own employees on the ground in Mexico to better understand the social and home-building practices of low-income communities, and used that knowledge to develop a successful product line of housing just for the poor. Unilever's commitment to improving the lives and livelihoods of the poor in India is driven by the recognition that "the health of business is inextricably linked with the health of society."

It is also important to understand the complementarities between philanthropy, corporate social responsibility (CSR), and service to the poor, as these approaches cannot be easily separated. Some CSR initiatives have recently been criticized as mere token philanthropic attempts to address the needs of the poor. But if companies allowed themselves to engage only in activities where business goals and poverty alleviation were

perfectly aligned, there would likely be fewer activities at the BoP. CSR activities have the advantage of providing a forum for businesses to learn about the needs of the poor.

ZMQ, a small to medium sized Indian software company, has combined its philanthropic commitment (12 percent of its profits) with its core competencies in developing ICT learning tools for social development in order to sponsor and create products and tools to bridge the digital divide. In one such venture, the company funded the development of a technology package to build the capacity of grass-roots women in using livelihood-generating technologies. The Global Alliance for Improved Nutrition (GAIN) has formed a Business Alliance to explore the space between philanthropy and strategic private sector interest by developing new business models to fortify food with necessary vitamins and minerals and making it available and affordable to the poor. Large companies, such as Abbott Laboratories, often utilize their corporate foundations to explore the complementarities between philanthropy and CSR. Abbott Fund, in partnership with the Government of Tanzania, is engaged in a major project that is modernizing the country's health system. By improving hospitals' physical infrastructure, training programs and working conditions, and utilizing the latest IT, the partners are expanding access to quality HIV/AIDS testing and health care for the poor.

## Market capacity building

IN DEVELOPING COUNTRIES, companies often need to deal with weak institutions or a lack of formal market mechanisms. In Unilever's business expansion in India, the company had to work around many infrastructure and institutional challenges, such as poor transport links and high rates of illiteracy.

In this context, it is crucial for business to address certain questions:

- To what extent do "organized or well-developed markets" capture the costs and benefits of the poor?
- What access do the poor have to these markets?
- Why do the poor pay more for the same or similar goods and services than the rich?
- How can level playing fields that provide equal opportunities for the poor be created?

These are important questions, because although informal markets can facilitate commerce, they can also engender abuse, create huge income inequality and exploitation, and become a barrier to entry and growth. Examples in this issue of Development Outreach illustrate how companies like Nestlé, CEMEX, Unilever, and Sumimoto have overcome the barriers of the informal economy and the lack of institutional and physical infrastructure, and ultimately helped the poor integrate into the official economy. Unilever developed a new business model to engage local entrepreneurs to set up direct-to-consumer retail operations, with training from the company and support from self-help groups or microfinance banks. In 2007, Project Shakti estimated that 46,000 entrepreneurs (mainly female) had reached more than three million rural Indian households.

## The role of Multinational Corporations (MNCs)

IT IS DIFFICULT TO GAUGE how many of the 63,000 MNCs<sup>4</sup> are ready and willing to incorporate poverty alleviation issues into their business strategies. While the relatively small role of MNC's in creating local employment has been well documented, their real contribution may be in setting performance benchmarks in developing markets. These would become the benchmarks that most local businesses would have to meet in order to gain legitimacy and trust in the communities in which they function.

MNCs need to recognize what they do well and what they do poorly in BoP markets. Large companies are typically good at integrating the poor into the global production system and facilitating market transactions for increased productivity as part of their supply chain,<sup>5</sup> but not necessarily at creating jobs through direct employment. But MNCs do have the power to shape institutional environments to be more supportive of job creation, and build partnerships with government, NGOs, international financial institutions (IFIs), and donor agencies. For example, the International Finance Corporation (IFC), the private sector arm of the World Bank Group, has been successfully working with the private sector to engage local businesses in the global supply chain, as illustrated in the articles on its Lighting Africa project and partnership with BP in Azerbaijan.

## The role of local companies

PRODUCTIVE ENGAGEMENT with the poor requires new business models that take into consideration both access to local knowledge and issues of trust. Business objectives should go beyond lowering the cost of doing business at the BoP and improving access to customer groups. They should also aim to build legitimacy and good will by tapping into local knowledge and leveraging social capital as a means of gaining access to market intelligence and building legitimacy in the eyes of the poor. Local companies can normally do this better than (and complement) MNCs. Of course, it is difficult to generalize, as some MNCs, such as Nestle and Unilever, have been present in many emerging economies for decades. Similarly, CEMEX has been very successful in launching an innovative housing program for low-income communities. Partnership initiatives, such as GAIN and UNICA, create space for collaborative action. The GAIN Business Alliance allows both MNCs and local companies to learn from each other, share results, and partner with development organizations. The Brazilian Sugar and Ethanol Industry Association, UNICA, jointly with the World Bank Institute, launched a capacity development program for sugar producing companies from Sao Paulo, which helps individual companies to incorporate social and environmental issues into their corporate strategy and contribute to community development.<sup>6</sup>

Local companies are often best positioned to provide goods and services to the poor while at the same time helping MNCs to expand their business at the BoP. For example, the key to

Sumimoto Chemical's success has been its partnership with a local Tanzanian company A to Z Textile Mills, which resulted in technology transfer, quality improvement, and creation of local employment for the poor who had no previous experience in manufacturing and wage-based jobs. India's ICICI Bank initiative is based on the assumption that economically viable occupations already exist in most regions of India, and that with proper support even the very poor can almost immediately engage in them without specialized skill building. The key, they have found, is providing access to finance, which ICICI created through creative partnerships between banks and a network of local financial institutions.

## Measuring impact

TO FULLY ASSESS EFFECTIVENESS, it is important to capture economic, social, cultural, and environmental impacts. Measures of success should not be limited to output and profitability indicators but should also take into account issues of equity and the balance between corporate, legal, and social obligations. It is essential to measure social values from the poor's perspective, and to understand what is important for them in terms of quality of life, empowerment, and security. Transparency and accountability must also be part of the initiative since corruption hurts the poor the most.<sup>7</sup> Companies like Unilever, CEMEX and Nestlé, through direct engagement with the poor, reduce the risk of corruption that affects the poor in their daily business transactions when operating in informal markets.

We also need to capture positive and negative cross-sectoral effects as well as improvements in market institutions. There is a growing need for companies, development organizations, and academia to create new models that capture the development multiplier effect. In Nestlé's engagement with poor rural farmers in China, for example, the local banking system benefited when the company provided its new suppliers with cash payments, leading to a new customer base for banks in previously low-income areas.


## Action agenda for the future

TO MEET THE NEEDS of 4 billion people is a daunting challenge that can only be met by taking successful models to scale. We need to look not only within existing markets, but also among countries and continents, to find solutions that "travel well", particularly between developing countries. Companies can play an important role in transporting best practices across borders, as the ZMQ and DEFTA Partners examples illustrate for countries in Asia and from Asia to Africa.

Effective poverty alleviation requires collective action by MNCs, local companies, governments, IFIs, and NGOs. Building successful partnerships is highly complex and requires clarification of roles, responsibilities, and incentive structures. Who is in a position to change the rules of engagement with the poor? How can corporate gaming be prevented to avoid increasing poverty and environmental degradation, particularly when institutions are weak? Where does the

value-creating potential lie within various stakeholder groups? How do we best organize initiatives and provide incentives to collaborate in developing more comprehensive and innovative models of engagement? And what are the most innovative ways of complementing the efforts of government, multilateral development banks, and development agencies?

To be sustainable, business initiatives need to be owned and informed by the developing country stakeholders themselves. The issues are global but most of the solutions are local. New mindsets and open dialogue with local entrepreneurs are prerequisites for collective action. The DEFTA Partners example clearly illustrates that partnership between entrepreneurs from both developed and emerging economies can play a critical role in creating innovative development solutions. DEFTA Partners, in collaboration with BRAC, a local development organization based in Bangladesh, are investing in improving the country's communication infrastructure, thus providing access to millions of poor people.

We hope that the examples presented in this issue will be used to help local beneficiaries define the challenges, set their own agendas, and successfully implement the best possible solutions. 

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### Endnotes

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<sup>2</sup> Ray Goldberg and Kerry Herman, Harvard Business School case: *Alleviating Poverty and Malnutrition*, President and Fellows of Harvard College, 2007.

<sup>3</sup> Maria Flores Letelier, Fernando Flores, and Charles Spinosa, *Creating and Developing Productive Customers in Emerging Markets*, California Management Review, Fall 2003.

<sup>4</sup> UNCTAD. (2000.) *World Investment Report, 2000: Cross-Border Mergers and Acquisitions and Development*. United Nations. Geneva.

<sup>5</sup> Diana Farrell, Jaana K. Remes, and Heiner Schulz, *The truth about foreign direct investment in emerging markets*, *McKinsey Quarterly*, February 2004. WC: 1995.

<sup>6</sup> Corporate Social Responsibility Program for the Sugar and Ethanol Industry in Sao Paulo, Brazil, Activity Report, The World Bank, World Bank Institute, UNICA, 2006.

<sup>7</sup> The World Bank Group, *The World Development Report, 2004: Making Services Work for the Poor*, World Bank Group, 2004.