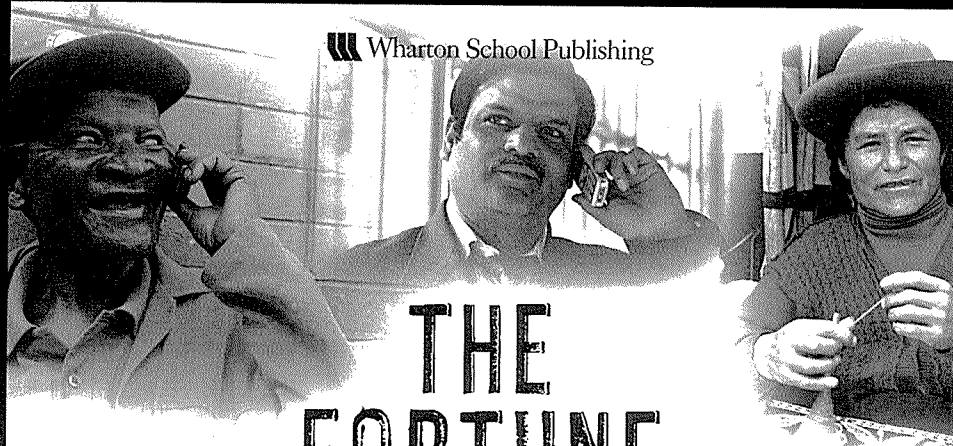


REVISED AND UPDATED 5TH ANNIVERSARY EDITION

Wharton School Publishing



THE FORTUNE AT THE BOTTOM OF THE PYRAMID

ERADICATING POVERTY THROUGH PROFITS



PRAHALAD

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5th
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Coauthor of the International Best Seller *COMPETING FOR THE FUTURE*

New
Introduction:
Private Sector and
Poverty:
Progress During
2004-2009

Five years is not a long time to evaluate the diffusion of an idea; much less its impact on the ground. It has been less than five years since the book *The Fortune at the Bottom of the Pyramid: Eradicating Poverty Through Profits* was published. The first article on the subject appeared in 2002.¹ At the time, the proposition that the private sector had a critical role to play in alleviating global poverty was generally met with skepticism. The idea that they could have the greatest impact through creating profitable businesses serving the 5 billion people who represented the “invisible, unserved market” was even more radical. I am profoundly grateful for the people in government, nongovernmental organizations, and large corporations who were willing to listen and experiment. The poor, of course, have long been hungry for change. Their enthusiasm and insights have been a huge inspiration to me.

We are a long way from solving the problem of global poverty. But I find reason to be optimistic that the conditions for creating significant and sustainable change are emerging rapidly. First, the idea that the private sector can and should be involved in creating market-based

solutions for the world's poorest consumers is gaining credibility. The market success of some multinationals that have taken up the challenge has created momentum. Respected business leaders such as Bill Gates championing the cause of *creative capitalism* has also contributed to a shift in perception.

Second, actively engaging with consumers in Bottom of the Pyramid markets has resonated with consumers in developed markets as well. The attitudes of the general public have begun to shift away from direct aid to an exchange of ideas and capital. For as little as \$25, anyone can evaluate business plans and extend micro loans to Bottom of the Pyramid entrepreneurs through Kiva.org. A few clicks on Novica.com grants access to a network of traditional crafts and artisans, and purchases are accompanied with a note from the artist. Cell phones are a part of the lives of the rich and poor alike. Today, citizens are engaging with each other in ways that would have been difficult to imagine even a few years ago. As a result, awareness of the conditions and nuances of the Bottom of the Pyramid is increasing. This has translated for the push for companies to help in uplifting the Bottom of the Pyramid from civil society, governments, and nongovernmental organizations.

Support—or pressure—for companies to be involved in the Bottom of the Pyramid will not create sustainable growth. The original inspiration for this book—eradicating poverty through profits—seems more tangible today than it did five years ago. There is evidence today that the innovations in the Bottom of the Pyramid can and have produced profitable business, and consumers in these markets have shown that they are as savvy and demanding as those anywhere else. Through my work with the United Nations Development Commission and large multinationals, the most encouraging lesson in this journey has not been in just the validation of the business model originally put forth. Far more significant is the emergence of the Bottom of the Pyramid as a platform for global innovation in some cases; a development which has important implications.

In this introduction to the 2009 edition of this book, I briefly assess the impact of the idea and include the perspectives of executives who have led major initiatives in Bottom of the Pyramid markets. I also address some of the emerging questions regarding Bottom of the Pyramid markets. There are five major themes I talk about explicitly:

1. How has the role of the private sector evolved in poverty alleviation?
2. What have large firms, including multinationals, learned as they actively pursue nontraditional opportunities in the Bottom of the Pyramid markets?
3. What are the key lessons for developing these market opportunities?
4. Are these markets forcing a “new social compact” for business?
5. What are the emerging “rules of engagement” that should inform our approach to Bottom of the Pyramid markets?

The Role of the Private Sector

Until recently, little attention was paid to the role of the private sector in poverty alleviation. The Millennium development goals were originally developed without recognition of the role that the private sector could play. It was later that the social compact with the private sector was formulated by the then Secretary General of the United Nations, Mr. Kofi Annan. The pioneering work on this topic was done by a Blue Ribbon Commission organized by the United Nations Development Program on private sector and poverty. The report was issued in 2004.² I had the privilege of serving on that commission. The United Nations Development Program is now fully engaged with the idea of the private sector's contribution to poverty alleviation.³ Similarly, organizations such as the World Economic Forum have focused private sector groups in developing solutions to poverty—be it the Social Entrepreneurship Forum or the group of firms collaborating to fight global hunger. The acceptance of the role of the private sector in poverty alleviation by civil society is somewhat mixed. Some are willing to accept a role for the private sector and some, as should be, are more skeptical. However, increasingly, large private sector firms and civil society organizations are learning to work together in a collaborative fashion. There is growing recognition that marrying the local knowledge of the nongovernmental organization with global reach of the multinational firm can create unique and sustainable solutions. Needless to say, the private sector cannot solve all problems but can bring technical and financial resources, the disciplines of organization, accountability, and entrepreneurial drive to bear on the problems.⁴

Who and What Is the Bottom of the Pyramid? What Have We Learned?

There is a lot of discussion on what the Bottom of the Pyramid market is and who constitutes that market. The original definition of the Bottom of the Pyramid was based on a simple premise. The concept was originally introduced *to draw attention to the 4-5 billion poor who are unserved or underserved by the large organized private sector, including multinational firms.* This group, until recently ignored by the private sector, could be a source of much needed vitality and growth. The assumptions influencing the focus on the Bottom of the Pyramid were also explicit: *“Four billion poor can be the engine of the next round of global trade and prosperity. Serving the Bottom of the Pyramid consumers will demand innovations in technology, products and services, and business models. More important, it will require large firms to work collaboratively with civil society organizations and local governments. Market development at the Bottom of the Pyramid will also create millions of new entrepreneurs at the grass root level—from women working as distributors and entrepreneurs to village level micro enterprises (page 2 in the original book).*

Needless to say, four billion people cannot be a monolith. They represent extreme variety—in their levels of literacy, rural-urban mix, geographical mix, income levels, cultural and religious differences, and every other conceivable basis for segmentation. This extreme variety does lead to multiple perspectives on the Bottom of the Pyramid. The Bottom of the Pyramid is like a kaleidoscope. No single view illuminates the total opportunity. Every twist helps focus on a specific facet of the opportunity or problem. This variety supports major disagreements among scholars and practitioners on what constitutes the Bottom of the Pyramid. Moreover, the term Bottom of the Pyramid evokes different images. Not surprisingly, readers tend to attribute their own definition to the idea. I called it the Bottom of the Pyramid because that was the reality as I saw it. The goal was to ensure that the rich—the top of the pyramid—could be sensitized to those who are less fortunate. Some did not like the idea of the bottom of the pyramid; they called it the Base of the Pyramid—a bottom-up view.⁵ Segmenting the 4 billion was not far off. Some talked about the Next Billion.⁶ Some focused on the Next 4 Billion.⁷ Some focused on the Bottom Billion.⁸ Some tried to get back to the old ways of categorizing the market as A to E; categories C, D, and E constituting the BOP. There is also significant debate on who are at

the Bottom of the Pyramid—people living on less than \$2/day? Less than \$1/day? What about people earning more than \$2/day but still in poverty without adequate access to world class (not the same as luxury) goods and services? The extensive study by World Resources Institute/International Finance Corporation has given granularity to the composition of the next 4 billion by country and by income level. It has also shown that Bottom of the Pyramid consumers account for \$5 trillion in Purchasing Power Parity terms.

The Bottom of the Pyramid debate has led to new perspectives on the opportunity. There is a focus on the Middle of the Pyramid, or the aspiring middle class. A recent study by the *Economist* concluded that half the world can be classified as the emerging middle class; defined as a population living on \$2–13 at 2005 Purchasing Power Parity prices. They have discretionary income and spend on education, health, energy, transportation, and personal care. This market by some estimates includes 2.6 billion people in 2005 and is rising fast. Asia alone is expected to have approximately 60 percent of the global middle class.⁹ Many firms now classify the Bottom of the Pyramid market as “emerging consumer markets” or just emerging markets. Obviously this is a more emotionally neutral term. More important, this view of Bottom of the Pyramid markets—the emerging consumers—shows the respect and the commitment of managers in large firms who have spent time and resources to understand this opportunity. This is a significant change from the position even five years ago.

We can draw multiple lessons from the heated debates about what constitutes the Bottom of the Pyramid during the last five years:

1. There is a clear recognition that four billion micro consumers and micro producers *constitute a significant market and represent an engine of innovation, vitality, and growth.* This is a *new category for all*—be it managers, governments, or civil society organizations. We need to understand it. It is clear, however, that this emerging market will force a fundamental rethinking of our approach to business.
2. The 4 billion people who constitute the Bottom of the Pyramid are not a monolith. For those who want to engage in this opportunity, there is *no single universal definition of the Bottom of the Pyramid that can be useful.* The definition must fit the focus for productive engagement. For example, micro-finance organizations in India might have a different definition of the poor from ones in Kenya or Brazil or the USA.

3. We can choose to serve any segment of the 4 billion. No institution—a firm or nongovernmental organization—needs to serve all of the Bottom of the Pyramid. They can pick and choose. Serving the “next billion” is as legitimate as serving “the bottom billion.”
4. There is a segment of the 4 billion who are so destitute, so deprived, and so consumed by war and disease that they need other forms of help. Government subsidies, multilateral aid, and philanthropy are all legitimate tools to deal with this segment. Even here, *our goal should be to build capacity for people to escape poverty and deprivation through self-sustaining market-based systems.*
5. Active engagement at the Bottom of the Pyramid markets requires a new and an innovative approach to business. *Retrofitting business models from the developed markets will not work.*¹⁰

I believe that the debate of what the Bottom of the Pyramid is will continue. But the world of business is moving beyond definition. The concept of the emerging consumer allows each firm to decide which segment of the Bottom of the Pyramid it wants to serve. Some firms, such as Unilever that have a long history of working in developing markets, now focus on “Straddling the Pyramid”—participating across the entire spectrum of opportunities often with the same category of products. It is fair to say that the idea of the Bottom of the Pyramid as an opportunity has taken root. Does this mean that it represents a viable business?

Bottom of the Pyramid as a Business Opportunity

While the cases in this book were intended to illustrate that there are viable business opportunities at the Bottom of the Pyramid, there was a lot of skepticism. Over the years, there is accumulating evidence that this segment represents a viable business. Consider for example, the growth of the cell phone. By 2011, more than 4 billion cell phones will be in use. Most of this growth is in the Bottom of the Pyramid markets. From sub-Saharan Africa, China, Southeast Asia, India, and Latin America and Eastern Europe, there is not a single country where the poor have not taken to the cell phone. India alone added approximately 11 million new subscribers in January 2009. Many successful firms have emerged out of this opportunity. Many are new firms, and many are new

businesses in older firms. Mobile Telephone Networks from South Africa, CelTel in Sub Saharan Africa, a dozen competitors in India led by Bharati Airtel, and Globe in the Philippines are some examples. The market capitalization of the three of the top five (two are not listed) leading players in wireless in India is approximately \$57 billion as of June 2008. In January 2009, in a depressed market, it was \$38 billion.

The cell phone revolution has demonstrated beyond doubt that there is a market for world-class goods and services if they can be made available at affordable prices. For example, a “cell phone minute” costs less than \$ 0.01 in India, probably the lowest rate per minute anywhere. The industry had to create its own ecosystem of mini entrepreneurs who sold prepaid cards and also charged the cell phones. The Bottom of the Pyramid business is quite critical for both the infrastructure players, such as LM Ericsson, and device makers, such as Nokia and Motorola.

The spread of the cell phone has made this the device of choice for not only communications but also some computing, entertainment, and the delivery of a wide variety of services such as medical care (as described in the Voxiva case in this book and reconfirmed in the update). Financial service organizations are also rapidly developing systems to use the cell phone for financial transactions (see the ICICI case update). Remittances are routinely handled through the cell phone. The cell phone, we can say, has shown that the Bottom of the Pyramid is not just a market but also a source of innovations in business models and applications. It has transformed the lives of the poor. We can “do well and do good” simultaneously. Most important, the rate of diffusion among the Bottom of the Pyramid around the world has shown how willing and capable the poor are to accept and benefit from advanced technology. The cell phone has broken several long-held beliefs: *There is no market at the Bottom of the Pyramid; they won't pay, they will not accept or do not need advanced technologies; the Bottom of the Pyramid cannot be a source of innovation; and multinationals do not need them.* Maybe some multinational firms can ignore this market. Not if you are Nokia, Motorola, Nestle, Unilever, or Microsoft. However, being a multinational or a large domestic firm does not guarantee success; *the capacity to adapt and innovate at the Bottom of the Pyramid does.*

A large number of firms have benefited from a focus on the Bottom of the Pyramid markets. They span multiple geographies and industries. For example, the success of the following local firms is common knowledge. The goal here is not to give an exhaustive list but an indicative list.

Brazil	Casas Bahia (retail)
	Habibs (fast food)
	Bradesco (banking)
Mexico	Elecktra (retail, banking)
	Grupo Bimbo (food)
	Patrimonio Hoy (housing)
Philippines	Globe (telecom, water)
Bangladesh	Grammen (micro finance, telecom, food)
India	Amul (dairy)
	Aravind Eye Hospital, Jaipur Foot, Narayana Hrudayalaya (health care)
	ITC e-Choupal (agriculture)
	SKS Finance (micro finance)
	Airtel (telecom)
South Africa	Pick and Pay (retail)
	Mobile Telephone Networks (telecom)
Chile	Savory, by Nestlé (ice cream)
	Brestler, by Unilever (ice cream)

More importantly, we see a large number of multinational firms either start new initiatives in Bottom of the Pyramid markets or reinforce their existing presence in the Bottom of the Pyramid. Some notable new entrants are such well-known firms as Microsoft (software), DSM (food supplements), Royal Philips (health care), Thomson Reuters (information), GlaxoSmithKline (pharmaceuticals), Intel (computing), Vodafone (telecom), ING (microfinance), and Monsanto (agriculture). Again this is an indicative list. Many of the CEOs were gracious enough to share their experiences and what they learned with us. Their letters are included in this volume.

The large private sector is learning rapidly that there is a significant market at the Bottom of the Pyramid. In some industries the size and attractiveness of the Bottom of the Pyramid markets are well established. Retailing, fast-moving consumer goods, micro finance, telecom, and agri-business, belong to this category. Computing, health and wellness-oriented food, health care, education, pharmaceuticals, and energy are

emerging as major opportunities. Affordable and modern housing, water, and transportation are still elusive at the Bottom of the Pyramid. Firms are also learning that this market cannot be approached with the mindset of their traditional markets. There is a need for experimentation and innovation. We certainly will witness more efforts in this direction. We need to ask: Why can't we create markets in every sector that we have created in telecom through wireless? Why not apply the same level of innovation, eco system development, and focus on affordability as we did in cell phones? This question is asked more and more in corporate boardrooms.

Key Lessons from Experiments

Even at this early stage of experimentation at the Bottom of the Pyramid, multinational firms are learning valuable lessons. Although the market is large and potentially lucrative, this potential cannot be realized unless managers are willing to experiment and innovate. They have to selectively "forget" traditional developed market approaches to business. The dominant lessons follow:

1. *The innovation sandbox (embrace constraints)*: The primary task of the private sector is often converting the Bottom of the Pyramid consumers from unorganized, inefficient local monopolies (for example, local moneylenders, local medics) to an organized and efficient private sector. In some cases, it is to ensure that Bottom of the Pyramid consumers are aware of the new products and services (for example, micro insurance). *Awareness, Access, Affordability, and Availability* are the key ingredients to market development at the Bottom of the Pyramid. It is useful to start with an *innovation sandbox*, a set of critical constraints that must become non-negotiables in the developmental process. The innovation sandbox must be specific to the firm, its target segment, and the business. However, some broad guidelines apply. In most cases, we can include
 - (a) *Scalability*. Unless the solution can be scaled, it is little use in changing people's lives. Moreover, most Bottom of the Pyramid businesses tend to be low margin, high volume, high return on capital businesses. The businesses are volume-sensitive and scale is critical.

- (b) A *new price-performance envelope* or a new value proposition is critical. Affordability dictates that we must start with a $Price - Profit = Cost$ and not $Cost + Profit = Price$ perspective.
- (c) *Modern technologies*. Increasingly it is becoming obvious that dramatic cost reductions are not possible without a judicious use of modern science in the development of products, services, and information technology in delivery of those services.
- (d) *International standards* of quality, safety, ecological sustainability, and aesthetics.

We can conceive of these constraints as the boundaries of an innovation sandbox, and all innovations must take place within it. These boundary conditions, when set, must not be relaxed.¹¹

All elements of the business—capital intensity, work flow, volume, manufacturing and logistics, design of products, its maintenance, pricing, use of people, skill development, and building an ecosystem of specialized suppliers—must be challenged and examined without relaxing the self-imposed constraints. A typical innovation sandbox might look like Figure Intro.1.

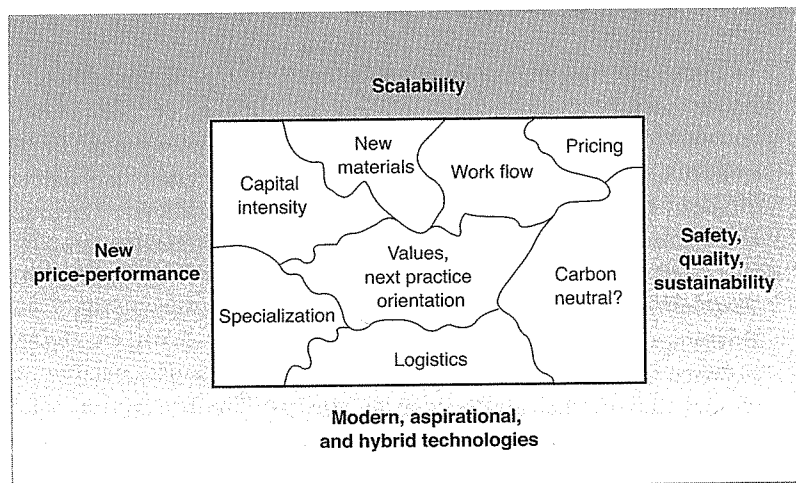


Figure Intro.1 The innovation sandbox.

Within the sandbox, there can be multiple innovations—be it centered on capital intensity or workflow. This approach—constrained innovation—is a critical ingredient to create fresh thinking in the organization. None of the boundary conditions can be met with traditional ways of doing business.

2. *Build an ecosystem*: Because the Bottom of the Pyramid markets have remained underserved by the organized private sector, they have remained local and fragmented. To build a scalable model, managers must invest time and energy to build an appropriate ecosystem. For example, it is impossible to enlarge the market for cell phones without building a large network of micro entrepreneurs who will sell prepaid cards. There are more than one million such entrepreneurs—some established neighborhood and village grocery stores that added this to their portfolio and some new entrepreneurs in India today. Similarly, to get access to rural markets, Unilever built a large network of shakti ammas—rural entrepreneurs who educate and distribute their products. Micro finance firms built and use self-help groups. ITC created village level operators of kiosks. Often, these ecosystems include micro entrepreneurs, micro producers, small- and medium-size enterprises, and nongovernmental organizations. Market development at the Bottom of the Pyramid needs a new ecosystem. The ecosystem inevitably consists of large and small firms. A typical ecosystem as is obvious from the multiple cases in this book and elsewhere will consist of (a) large firms, (b) small- and medium-size enterprises, (c) micro entrepreneurs (as in shakti ammas or farmers), (d) civil society organizations, and often (e) the public sector. All have to collaborate to build a viable business. As a group, they constitute the ecosystem, and each contribute differently to the overall task of accessing and serving the Bottom of the Pyramid consumer. During the last five years, many such ecosystems have evolved. It is easier today to attach oneself to an existing system if it is appropriate. It is appropriate to say that in the Bottom of the Pyramid

Ecosystems > Investment Capacity

No amount of investment is a substitute for the skills and knowledge that an ecosystem can provide. The message is “don’t go it alone.”

3. *Co-create solutions*: Managers who are used to developed markets are often surprised by the sophistication and demands of the Bottom of the Pyramid markets. It is not just about making cheap versions of the products sold in developed markets. Bottom of the Pyramid markets demand that managers acquire “local knowledge and local trust” before they develop markets—be it micro consumers or micro producers. It is unrealistic to expect farmers to sell their meager

crops to ITC and abandon their local trader unless they develop trust in ITC. Similarly, don't expect people to abandon their moneylender before they know that the micro-finance arm of the bank is reliable and will stay with them. Neither should we expect them to change their habits before they are confident that the new animal feed is both efficacious and will be available when needed.

There are three different pressures that must be understood. The role of the private sector is to bring world-class products and global standards of quality and safety to these markets. At the same time, the solutions must be locally responsive. *Global-local tension* is real. Secondly, to provide high quality at low cost, firms must focus on capital intensity of the business and the overheads. Traditional ways of doing business will not do. A *lean business and organization* is required. This represents a major tension in multinational firms as this challenges their existing business models. Finally, firms have to *rapidly learn* about the local consumers, their needs, and their aspirations at low cost.

Large private sector firms are finding that they need to collaborate with others to accomplish these goals. Gaining local knowledge, accessing specialized skills, reducing capital intensity and overheads, gaining trust, and becoming locally relevant requires that they start co-creating solutions. No firm has all the skills and the capability to do this. It is desirable that managers learn to co-opt both consumers and civil society and other institutions to build a co-creation platform. British Petroleum is developing a biomass stove for the rural poor with input from consumers, nongovernmental organizations, and the Indian Institute of Science. The nongovernmental organizations help identify and build a network of jyoti Ammas—local village level entrepreneurs who sold the stoves. They also help build a network of biomass pelletizers.¹² In the Bottom of the Pyramid collaborative capacity and integrative capacity (the capacity to integrate the contributions of multiple players into a coherent whole) is more valuable than investment capacity. It is fair to say

Collaborative Capacity > Investment Capacity

Co-creation reduces investment needs as more share in the investment. It reduces risk as the key players jointly develop the solution. For example, in the case of British Petroleum, the BP team, the Indian Institute of Science, nongovernmental organizations, and the village level consumers, jointly developed the stove. Managers must learn that

the Bottom of the Pyramid markets require a new level of collaboration between civil society and the private sector. It also requires a new respect for consumers as co-creators of solutions and not just passive recipients of a product or service.

4. *A new concept of scale:* Scale can be achieved in many ways. The Bottom of the Pyramid forces us to think differently. Consider the question: "I want to build a dairy that is world scale with a capacity to process 6 to 7 million kilograms of milk per day. How do I plan for it?" This question often gets people calculating how many cattle and how big a cattle farm one should have. Amul in India, the largest processor of raw milk in the world, originates the milk in 10,000 plus villages covering more than 2.2 million farmers. Each one might have only one or two heads of cattle. But by building village level collection centers that aggregate raw milk from a large pool of farmers, and processing it centrally, Amul built *virtual scale*. By paying the farmers for quality (for example, volume and fat content) and by sophisticated logistics from collection centers to world-class processing units, Amul totally avoided the problems of managing large herds centrally. Decentralized origination, centralized processing, and marketing seem to be the key.

This model is becoming fairly popular. Nestle just replicated the Amul model in the Northern Indian province of Punjab. They collect and process 1.5 million kgs of milk a day from farmers. ITC collects soybean and wheat from more than 2.5 million farmers in a similar fashion with ITC e-Choupal. Jaipur Rugs uses more than 40,000 contract workers spread all over northern India to weave rugs using traditional and new patterns. The Aravind Eye Care Facility uses village level camps to identify those who need surgery. Last year they examined 2.2 million outpatients and treated 285,000 who needed surgery. It is safe to say that the capacity to organize highly distributed and independent suppliers (for example, farmers) and contractors (for example, weavers) or potential consumers (for example, patients) and build a reliable logistics systems is more critical than investment capacity. ITC, Jaipur Rugs, and Amul are nodal firms. They provide the intellectual infrastructure, standards of performance, customer interface, and the technology backbone. It is safe to say that in the Bottom of the Pyramid

Building a Nodal Organization > Investment Capacity

The Bottom of the Pyramid allows a new approach to scale and organization. Further, most of these organizations are very lean. Most of the systems are self-regulating and do not need much supervision.

5. *Use technology:* It is normal to assume that Bottom of the Pyramid markets are not high-tech markets. Those managers who grew up with the concepts such as “product life cycle view of international business” (meaning that all new technology solutions are developed in the West, and they move to poor and developing countries over time) will find Bottom of the Pyramid markets providing a big surprise. You will find Aravind or Narayana Hrudayalaya using the latest medical technology. For example, Narayana Hrudayalaya prefers digital to analog products even if they are expensive. An analog X-ray machine might be inexpensive, but the film is not. Capital expenditure is lower but variable costs are higher. A large throughput system (scale) makes this an unattractive proposition. Further, digital X-ray allows pictures to be uploaded for examination by experts at remote locations. Similarly, Airtel uses the most advanced technology. It converted its fixed costs into variable costs by outsourcing infrastructure investments to LM Ericsson and IBM. Airtel pays a fee for each consumer added; a variable cost.

The use of information technology to manage the logistics and manufacturing infrastructure is widespread. ITC depends on its network of PCs to engage and connect with the farmers. The ITC network is the heart of its operation. Jaipur Rugs is starting to invest in an IT system that tracks each weaver and each order along its highly distributed system. Remittances and rudimentary banking functions are moving to the cell phone. There is a tense negotiation between telecom operators and the financial services firms in Africa and India.

The lessons are clear. Advanced technology is critical for ensuring the quality of product or service delivered. More important, advanced technologies wisely deployed reduce the overall costs (for example, cost per patient, cost per minute of cell phone usage, cost per transaction), if the investments can be leveraged with high levels of usage. Capital expenditure in the absolute (for example, \$1 million dollars) is different from asking what if we had 5,000 patients per week rather than 50? Secondly, advanced technologies lead to innovative and new applications, such as cell phone-based banking.

Finally, IT solutions provide real-time information on inventories in the system, receivables, and the changing patterns of consumption. Well-developed IT systems provide real-time alerts to managers.

6. *Sustainability will emerge as a source of innovations at the Bottom of the Pyramid:* The planet is under stress—be it access to water, deforestation, pollution, or green house gas emissions. This is a familiar story. What if we added an additional 3 to 4 billion people as micro producers and consumers to the current 2 billion? Sustainability will become a major impediment. Nobody can deny that the poor have a right to a better standard of living—be it access to safe water, better food and sanitation, and better education. The pressure to serve an additional 3 to 4 billion and at the same time protect the environment will focus attention on sustainability as never before. New innovations, large and small, will be needed. For example, given interruptions in power and water supply, an Indian firm, Godrej, has introduced a washing machine that remembers when the power was cut off in the washing cycle. When power resumes, it starts where it left off rather than from the beginning. This saves both water and power. Packaging is getting its due attention. Biodegradable and new forms of packaging are becoming an imperative. So are new sources of renewable energy. We should expect to see the Bottom of the Pyramid as a major source of ecologically sustainable innovations in the near future.
7. *The challenge is market development:* The biggest challenge to managers who are trained to “serve existing markets efficiently” is to change their mindsets when they approach BOP markets. The cell phone or microcredit are good examples. Airtel had to develop the market. The tele-density in India in 2002 was so low that it was pathetic. They and others had to build an urban and now a rural market for connectivity and value-added services. In every instance of success, managers had to “forget” traditional ways of approaching the business and develop a new and innovative approach. For example, Airtel had to give up on average revenue per customer or user (ARPU) as a measure of attractiveness and focus on the contribution per minute of cell phone time. This is true for Airtel as much as for ICICI, Aravind, or Voxiva. The goal is to build new markets, organize the “unorganized markets,” build new ecosystems, and create new business models. The challenge is about innovating the management processes within the firm that allows managers in the

field to defy received wisdom and build a model that works. It is beyond “recontextualizing” the existing business models. It is about management innovation and market development.

8. *Bottom of the Pyramid markets are evolving rapidly*: It is important that we recognize that the Bottom of the Pyramid markets are evolving rapidly. Just measuring the Bottom of the Pyramid segments by income (as is done normally) hides the interesting transitions that are taking place in the market. It is better to use life style measures (LSMs) of the Bottom of the Pyramid consumers. What life style do they aspire to? What life style do they invest in? How do we explain a resident of a slum without clean drinking water and sewage, focusing on kitchen appliances, cell phones, and color televisions? How do we explain a poor mother investing in her son’s education through private tuition even when she goes hungry? Or a farmer investing in his cattle before improving his house? Two forces are at work here. First, individuals are making choices to their life style that do not necessarily follow our perceptions of what someone at a particular income level should do. Better informed and better focused on the aspirations for themselves and their families, their decision-making criteria are changing rapidly. We see it in their approach to health care, education, and connectivity. Secondly, the economic pyramid, as predicted in the original version of this book, is slowly morphing into a diamond; not all around the world but certainly in major markets such as China, India, South Africa, Turkey, Brazil, and Indonesia. This will have a profound impact on the opportunities for growth.

We could add to the lessons learned. However, it is important to note that this is a rapidly changing and evolving opportunity. As micro consumers, micro producers, and micro entrepreneurs and innovators, the poor are rapidly becoming sophisticated and demanding. Managers need to develop the capacity to anticipate and continuously adapt.

Business and the New Social Compact

Business leaders who have engaged themselves actively with the Bottom of the Pyramid have started to reexamine the role of business in society. Many CEOs have come to look at business with a new lens—the Bottom of the Pyramid lens. Mr. Patrick Cescau, the retired CEO of

Unilever, is one of them. His views reflect the growing appreciation of the role of the private sector in protecting the planet and at the same time serving the poor.

“For one, there is a growing recognition that the social and environmental challenges facing us in the twenty-first century are so complex and so multi-dimensional that they cannot be solved by governments alone. Industry has to be part of the solution. But perhaps the biggest catalyst for change has been the increasing awareness within business itself that many of the big social and environmental challenges of our age, once seen as obstacles to progress, have become opportunities for innovation and business development. We have come to a point now where the agenda of sustainability and corporate responsibility is not only central to business strategy but has become a critical driver of business growth.”

Recently, Bill Gates surprised his colleagues by suggesting that we need to reexamine the role of capitalism. His solution was to move to “creative capitalism.”¹³ He defined it as

There are two great forces of human nature: self-interest, and caring for others. Capitalism harnesses self-interest in a helpful and sustainable way, but only on behalf of those who can pay. Government aid and philanthropy channel our caring for those who can’t pay. But to provide rapid improvement for the poor we need a system that draws in innovators and businesses in a far better way than we do today.

Such a system would have a twin mission: making profits and also improving lives of those who don’t fully benefit from today’s market forces. For sustainability we need to use profit incentives wherever we can. At the same time, profits are not always possible when business tries to serve the very poor. In such cases there needs to be another incentive, and that incentive is recognition. Recognition enhances a company’s reputation and appeals to customers; above all, it attracts good people to an organization. As such, recognition triggers a market-based reward for good behavior. In markets where profits are not possible, recognition is a proxy; where profits are possible, recognition is an added incentive.

The challenge here is to design a system where market incentives, including profits and recognition, drive those principles to do more for the poor.

I like to call this idea creative capitalism, an approach where governments, businesses, and nonprofits work together to stretch the reach of market forces so that more people can make a profit, or gain recognition, doing work that eases the world’s inequities.

Then there are those who promote the idea of Social Capital. This movement is led by Prof. Mohammed Yunus of Grameen Bank fame. There is a lot of ferment and discussion in understanding the role of markets and the role of capitalism. There are skeptics. Many wonder whether market-based solutions are the answer. The real issue we must focus on is not whether markets can solve all problems. They might not. The real issue is this: "How do we bring to bear *the entrepreneurial and innovative energy of private enterprise to solve the critical problems facing humanity?*" In many cases, as we have already seen, private enterprise must work collaboratively with civil society, governments, and aid agencies and philanthropy to create innovative solutions. For these solutions to be sustainable, creating a surplus (profit) is critical.

These debates are healthy. I do not believe that we should look for an easy or quick solution to these complex questions. We must cultivate the ability to experiment and refine our thinking. Although the final outcome of this debate is not clear, it is obvious that private sector involvement in Bottom of the Pyramid markets has spawned a new debate. It has challenged our assumptions about the role of business in society. Businesses recognize that they must regain their social legitimacy. This will be determined by how businesses approach poverty and sustainability. Our focus on the role of capitalism and the Bottom of the Pyramid might be hiding a bigger and intellectually more demanding question and a bigger opportunity.

Democratizing Commerce: The Challenge for the 21st Century

I believe that the real challenge for the 21st century is democratization of commerce. Often, the debate about private sector involvement in the Bottom of the Pyramid centers on questions such as "Is globalization good or bad for the poor?" If we phrase the question this way, almost by definition, there will be people taking either side. However, if we accept globalization is like gravity and that there is no point in denying gravity; but great benefit to defying it and build a plane, then we can ask the question differently: "How do we make the benefits of globalization accessible to all?" This formulation of the question allows us to be more creative and entrepreneurial. Therefore, I would like to define "democratizing commerce" as *bringing the benefits of globalization to all micro consumers, micro producers, micro innovators, micro investors, and micro entrepreneurs.*

As shown next, we start with the assumption that everybody must have the right to the benefits of globalization. This implies that as individuals we have multiple roles—as consumers, producers, investors, innovators, and entrepreneurs. At a minimum, all must be treated with dignity and self-esteem—as micro consumers. They must be able to exercise choice and must have access to world-class goods and services. World class does not mean luxury. A cell phone that the poor get is world class; it might not have a fancy case, a fine camera, or a great color display. But in its core functionality, it is no different. Treating people as consumers is not the same as creating a wasteful consumer culture. The CEO of the Acumen Fund, Jacqueline Novogratz, had this to say:

We agree with Dr. Prahalad that choice is where dignity starts, and that the world will change only when we view truly low-income individuals as full participants in their local economies and communities, as producers and consumers, rather than as passive recipients of charity.

We have to start with respect for individuals irrespective of their current condition. Deciding "what is good for them" is against the very spirit of co-creation. Yes, we can educate them on the risks and benefits of choices. But they must exercise their choice. Those of us who have had the pleasure to see firsthand the extraordinary intelligence of the "uneducated" and how they "make do with what they have" are convinced that capability building for personal choice is a critical component of democratization of commerce.

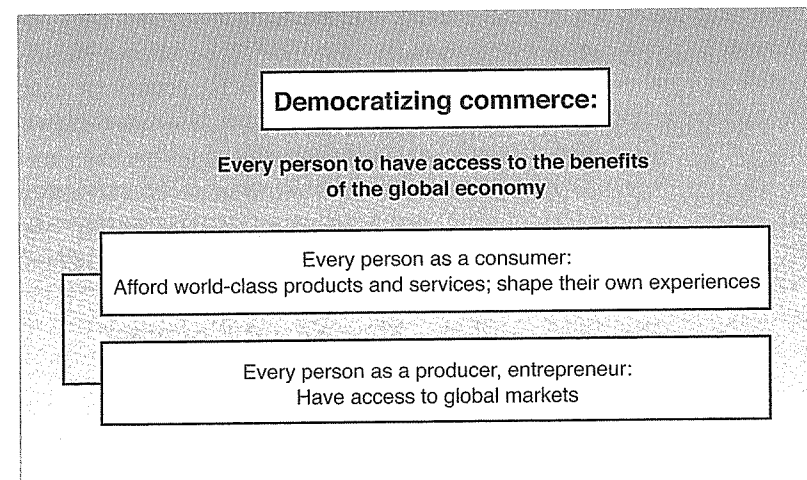


Figure Intro.2 Democratizing commerce.

Although we treat all with respect as “consumers,” we must also ensure that all can participate in the global economy as micro producers, micro entrepreneurs, and micro investors. Increasingly, this is becoming a reality. The case of Amul, ITC e-Choupal, Jaipur Rugs, and Nestlé are examples of connecting rural, subsistent farmers to regional, national, and global markets. There are now a large number of examples of organizing the poor to ensure that they have the benefits of information—as in the case of farmers using cell phones to check weather and price information before they sell to farming cooperatives or working with large firms such as ITC or Nestlé. At the same time, individuals must have access to become entrepreneurs. The story of village level entrepreneurs—Shakti Ammas (Unilever), Jyoti Ammas (BP), Grammen Bank, and self-help groups all over the world, demonstrate that given a chance, the poor are willing to be entrepreneurial and invest in their own success. There are those entrepreneurial women who start a “salon” in their neighborhood, to those who settle for a more traditional opportunity of raising cattle or chickens. The key is that they learn to be self-reliant, confident, and capable of understanding investment and returns, credit, and profit. Finally, we have to provide opportunities for them to save and become micro investors. Access to savings accounts and modern finance is key to fulfill this role. Many of them are also innovators. Today, there are opportunities for them to be organized and their innovations recognized. Prof. Anil Gupta has built an incredible database of micro innovators from villages, and this role is getting recognized.

Democratization of commerce is based on everyone having the right to exercise their roles as micro consumers, micro producers, micro entrepreneurs, micro investors, and micro innovators. *Access to information* removes the first impediment to building this brave, new world. Information asymmetry has always been at the heart of poverty. It was information asymmetry that allowed local moneylenders to have sway over the poor farmers; or buyers have advantage over fishermen who had no idea of what the prices were. Secondly, *access to credit and micro finance products* (including micro insurance) from the organized sector—micro-finance institutions and banks—allows people to build equity and escape usurious moneylenders and continuous struggle with poverty. *Access to regional and national markets*, coupled with information, allows them to get a “fairer” wage. When organized and connected, the poor have a

fighting chance to get a fair wage for their work. Finally, they, as micro innovators, can find a market for their innovations if they are organized.

I do recognize that what we are seeing are a “ray of hope” and weak signals that suggest that we can democratize commerce. We have to actively engage the private sector in a collaborative relationship with civil society, governments, and philanthropists. However, the organizing idea that illuminates this new social compact must be

- Respect for the rights of the individual
- The use of transparent transactions or a focus on market-based solutions
- Scalability to solutions
- Reducing the rural-urban, rich-poor divide through information technology and organization
- Focus on entrepreneurship and innovation
- Focus on ecologically sustainable solutions

Five years after the initial publication of this book, I am more excited and energized about the possibilities of the Bottom of the Pyramid than ever before. The capacity for change and creative thinking I have seen from everyone who has embraced the challenge—from nongovernmental organizations, multinationals, and the poor themselves—has been inspirational. A change this ambitious cannot happen overnight. There have been setbacks, missteps, and disappointments. But that is true with all fundamental change. I am hopeful that the debate about the Bottom of the Pyramid has shifted away from convincing people that there is a market to debating how best to serve it. I am confident that the simple fact that so many more people are searching for answers will lead to better and more complete solutions.

It used to be that the rich felt a sense of entitlement. I hope that as a result of more companies engaging with the poor, they too begin to feel a sense of entitlement—to dignity, choice, and mobility. I believe that this change will help not only people across the world, but society and the environment as well, because it will require change and innovation on a massive scale. It is too early to pronounce Bottom of the Pyramid markets an unqualified successes. I think, however, there are enough signals to illustrate that the “invisible hand” of entrepreneurs reaching out to the invisible markets of the world has the capacity to help create the solutions that people—and the planet—so desperately need.

Endnotes

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PART II

The Original Text of the Book

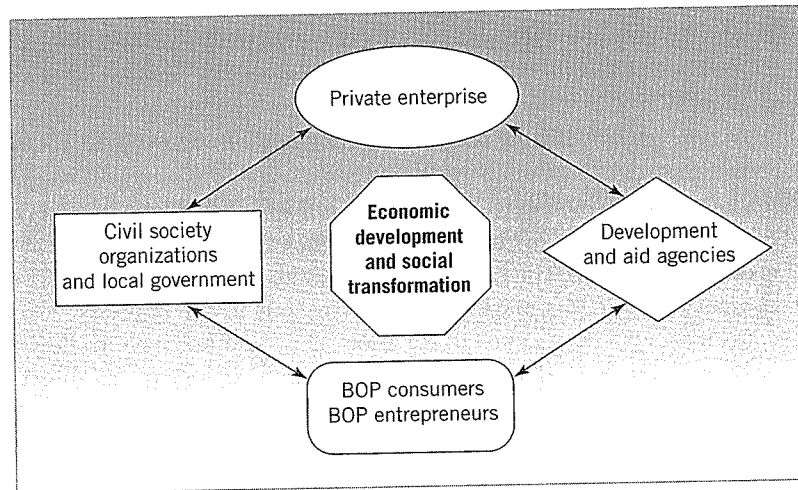
- Chapter 1 ■ The Market at the Bottom of the Pyramid
- Chapter 2 ■ Products and Services for the BOP
- Chapter 3 ■ BOP: A Global Opportunity
- Chapter 4 ■ The Ecosystem for Wealth Creation
- Chapter 5 ■ Reducing Corruption:
Transaction Governance Capacity
- Chapter 6 ■ Development as Social Transformation

The objective of this section is to *build a framework* for poverty alleviation. We start with a simple proposition. If we stop thinking of the poor as victims or as a burden and start recognizing them as resilient and creative entrepreneurs and value-conscious consumers, a whole new world of opportunity can open up. Four billion poor can be the engine of the next round of global trade and prosperity. They can be a source of innovations. Serving the BOP consumers will demand innovations in technology, products and services, and business models. More important, it requires large firms to work collaboratively with civil society organizations and local

governments. Market development at the BOP can also create millions of new entrepreneurs at the grass roots level—from women working as distributors and entrepreneurs to village-level micro enterprises. These micro enterprises will be an integral part of the market-based ecosystem. It requires organizational and governance innovations as well.

The vision that is presented in the following pages is the co-creation of a solution to the problem of poverty. The opportunities at the BOP cannot be unlocked if large and small firms, governments, civil society organizations, development agencies, and the poor themselves do not work together with a shared agenda. Entrepreneurship on a massive scale is the key. This approach can challenge the prejudices about the “role and value added” of each group and its role in the economic development at the BOP.

In these chapters, you find the opportunities for co-creation among the various players. More important, the poor themselves are willing to experiment, learn, and change. While we focus on the role of the private sector, the importance of collaboration across the various groups becomes obvious. The interconnectedness of the approach to economic development and social transformation as visualized below becomes obvious.



Part II outlines how that can be accomplished by isolating principles from successful, large-scale experiments involving the entire private sector ecosystem. Most of the examples of successful experimentation are taken from the case studies included later in the book. The bottom line is simple: It is possible to “do well by doing good.”

I

The Market at the Bottom of the Pyramid

Turn on your television and you will see calls for money to help the world’s 4 billion poor—people who live on far less than \$2 a day. In fact, the cry is so constant and the need so chronic that the tendency for many people is to tune out these images and the message. Even those who do hear and heed the cry are limited in what they can accomplish. For more than 50 years, the World Bank, donor nations, various aid agencies, national governments, and, lately, civil society organizations have all fought the good fight, but have not eradicated poverty. The adoption of the Millennium Development Goals (MDG) by the United Nations only underscores that reality; as we enter the 21st century, poverty—and the disenfranchisement that accompanies it—remains one of the world’s most daunting problems.

The purpose of this book is to change that familiar image on TV. It is to illustrate that the typical pictures of poverty mask the fact that the very poor represent resilient entrepreneurs and value-conscious consumers. What is needed is a better approach to help the poor, an approach that involves partnering with them to innovate and achieve sustainable win-win scenarios where the poor are actively

engaged and, at the same time, the companies providing products and services to them are profitable. This collaboration between the poor, civil society organizations, governments, and large firms can create the largest and fastest-growing markets in the world. Large-scale and wide-spread entrepreneurship is at the heart of the solution to poverty. Such an approach exists and has, in several instances, gone well past the idea stage as private enterprises, both large and small, have begun to successfully build markets at the *bottom of the pyramid (BOP)* as a way of eradicating poverty.

The economic pyramid of the world is shown in Figure 1.1. As we can see, more than 4 billion constitute the BOP. These are the people who are the subject matter of this book.

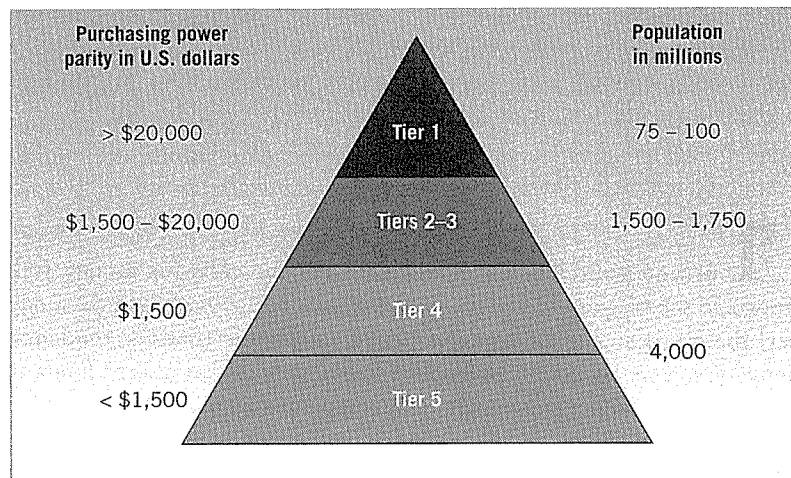


Figure 1.1 The economic pyramid. *Source:* C.K. Prahalad and Stuart Hart, 2002. *The Fortune at the Bottom of the Pyramid, strategy+business*, Issue 26, 2002. Reprinted with permission from *strategy+business*, the award-winning management quarterly published by Booz Allen Hamilton. www.strategy-business.com.

THE BOTTOM OF THE PYRAMID (BOP)

The distribution of wealth and the capacity to generate incomes in the world can be captured in the form of an economic pyramid. At the top of the pyramid are the wealthy, with numerous opportunities for generating high levels of income. More than 4 billion people live at the BOP on less than \$2 per day. They are the subject matter of this book.

As you turn these pages, you will discover companies fighting disease with educational campaigns and innovative products. There are organizations helping the handicapped walk and helping subsistence farmers check commodity prices and connect with the rest of the world. There are banks adapting to the financial needs of the poor, power companies reaching out to meet energy needs, and construction companies doing what they can to house the poor in affordable ways that allow for pride. There are chains of stores tailored to understand the needs of the poor and to make products available to them.

The strength of these innovative approaches, as you will come to appreciate, is that they tend to create opportunities for the poor by offering them choices and encouraging self-esteem. Entrepreneurial solutions such as these place a minimal financial burden on the developing countries in which they occur.

To begin to understand how all of this is remotely possible, we need to start with some basic assumptions:

- First, while cases certainly can be found of large firms and multinational corporations (MNCs) that may have undermined the efforts of the poor to build their livelihoods, the greatest harm they might have done to the poor is to ignore them altogether. The poor cannot participate in the benefits of globalization without an active engagement and without access to products and services that represent global quality standards. They need to be exposed to the range and variety of opportunities that inclusive globalization can provide. The poor represent a “latent market” for goods and services. Active engagement of private enterprises at the BOP is a critical element in creating inclusive capitalism, as private-sector competition for this market fosters attention to the poor as consumers. It creates choices for them. They do not have to depend only on what is available in their villages. If large firms approach this market with the BOP consumers’ interests at heart, it can also lead to significant growth and profits for them. These characteristics of a market economy, new to the BOP, can facilitate dramatic change at the BOP. Free and transparent private-sector competition, unlike local village and shanty-town monopolies controlled by local slum lords, can transform the “poor” into consumers (as we illustrate with examples). Poverty alleviation can become a business development task shared among the large private sector firms and local BOP entrepreneurs.

- Second, the BOP, as a market, provides a new growth opportunity for the private sector and a forum for innovations. Old and tired solutions cannot create markets at the BOP.
- Third, BOP markets must become an integral part of the work of the private sector. They must become part of the firms' core businesses; they cannot merely be relegated to the realm of corporate social responsibility (CSR) initiatives. Successfully creating BOP markets involves change in the functioning of MNCs as much as it changes the functioning of developing countries. BOP markets must become integral to the success of the firm to command senior management attention and sustained resource allocation.

There is significant untapped opportunity for value creation (for BOP consumers, shareholders, and employees) that is latent in the BOP market. These markets have remained "invisible" for too long.

It is natural for you to ask this: If all of this is so obvious, why has this not yet occurred?

The Power of Dominant Logic

All of us are prisoners of our own socialization. The lenses through which we perceive the world are colored by our own ideology, experiences, and established management practices. Each one of the groups that is focusing on poverty alleviation—the World Bank, rich countries providing aid, charitable organizations, national governments, and the private sector—is conditioned by its own dominant logic. Let us, for example, examine the dominant logic of each group as it approaches the task of eradicating poverty.

Consider, for instance, the politicians and bureaucrats in India, one of the largest countries with a significant portion of the world's poor. India is home to more than 400 million people who qualify as being very poor. The policies of the government for the first 45 years since independence from Great Britain in 1947 were based on a set of basic assumptions. Independent India started with a deep suspicion of the private sector. The country's interaction with the East India Company and colonialism played a major part in creating this mindset. The experience with the indigenous private sector was not very positive, either. The private sector was deemed exploitative of the poor. This suspicion was coupled with an

enormous confidence in the government machinery to do what is "right and moral." For example, the government of India initiated a series of large industrial projects in the public sector (owned by the Indian government) in a wide variety of industries, from steel to food distribution and global trading in essential commodities. India's general suspicion of the private sector led to controls over its size and expansion. Some sectors of economic activity were reserved for small-scale industries. In textiles, for example, the "hand loom sector" dominated by small firms was given preference. There was no credible voice in public policy for nurturing market-based ecosystems that included the large and the small in a symbiotic relationship. The thinking was cleanly divided among the public sector (mostly large firms with significant capital outlay as in steel), the private sector with large firms strictly controlled by the government through a system of licenses, and a small-scale sector. The focus of public policy was on distributive justice over wealth creation. Because of the disparities in wealth and the preponderance of the poor, the government thought its first priority must be policies that "equalized" wealth distribution. Taxation, limits on salaries of top managers, and other such measures were instituted to ensure distributive justice. The discussion further polarized around the somewhat contrived concepts of rural poor and urban rich. The assumption was that the rural population was primarily poor and the urban population was relatively rich. However, the data increasingly does not support this distinction. There are as many rural rich as there are urban poor. Poverty knows no such boundaries. In the developing world, more than one-third of the urban population lives in shanty towns and slums. These traditional views reflect the philosophy behind actions taken by bureaucrats and politicians. During the last decade, a slow but discernable transition has been taking place from the traditional to a more market-based outlook.

This much-needed and desirable transition is in its infancy. The dominant logic, built over 45 years, is difficult to give up for individuals, political parties, and sections of the bureaucracy. This is the reason why politicians and bureaucrats appear to be vacillating in their positions. Most thinking people know where they have to go, but letting go of their beliefs and abandoning their "zones of comfort" and familiarity are not easy. We also believe that it is equally difficult for a whole generation of BOP consumers to give up their dependence on governmental subsidies.

We have explicitly focused on ideology and policy and not on the quality of implementation of projects focused on the poor, be it building roads and dams or providing basic education and health care. The distinct role of corruption, which seems so endemic to developing countries in general, deserves separate treatment (see Chapter 5, "Reducing Corruption: Transaction Governance Capacity").

Private-sector businesses, especially MNCs (and large local firms that emulate their MNC competitors), also suffer from a deeply etched dominant logic of their own, which restricts their ability to see a vibrant market opportunity at the BOP. For example, it is common in MNCs to have the assumptions outlined in Table 1.1. These assumptions dictate decision and resource allocation processes for developing countries and BOP markets in particular.

Table 1.1 The Dominant Logic of MNCs as It Relates to BOP

Assumption	Implication
The poor are not our target customers; they cannot afford our products or services.	Our cost structure is a given; with our cost structure, we cannot serve the BOP markets.
The poor do not have use for products sold in developed countries.	We are committed to a form over functionality. The poor might need sanitation, but can't afford detergents in formats we offer. Therefore, there is no market in the BOP.
Only developed countries appreciate and pay for technological innovations.	The BOP does not need advanced technology solutions; they will not pay for them. Therefore, the BOP cannot be a source of innovations.
The BOP market is not critical for long-term growth and vitality of MNCs.	BOP markets are at best an attractive distraction.
Intellectual excitement is in developed markets; it is very hard to recruit managers for BOP markets.	We cannot assign our best people to work on market development in BOP markets.

Adapted from C.K. Prahalad and Stuart Hart, *The Fortune at the Bottom of the Pyramid*, *strategy+business*, Issue 26, 2002. Reprinted with permission from *strategy+business*, the award-winning management quarterly published by Booz Allen Hamilton. www.strategy-business.com.

These and other implicit assumptions surface in every discussion of BOP markets with managers in MNCs and those in large domestic firms in developing countries that fashion their management practices after those at successful MNCs. These biases are hard to eradicate in large firms. Although the dominant logic and its implications are clear, it is our goal in this book to challenge and provide counterpoints. For example, BOP markets enable firms to challenge their perspectives on cost. We will show that a 10 to 200 times advantage (compared to the cost structures that are oriented to the top of the pyramid markets) is possible if firms innovate from the BOP up and do not follow the traditional practice of serving the BOP markets by making minor changes to the products created for the top of the pyramid.

Most charitable organizations also believe that the private sector is greedy and uncaring and that corporations cannot be trusted with the problems of poverty alleviation. From this perspective, profit motive and poverty alleviation do not mix easily or well. Aid agencies have come full circle in their own thinking. **From aid focused on large infrastructure projects and public spending on education and health, they are also moving toward a belief that private-sector involvement is a crucial ingredient to poverty alleviation.**

Historically, governments, aid agencies, nongovernmental organizations (NGOs), large firms, and the organized (formal and legal as opposed to extralegal) business sector all seem to have reached an implicit agreement: Market-based solutions cannot lead to poverty reduction and economic development. As shown in Figure 1.2, the dominant logic of each group restricts its ability to see the market opportunities at the BOP. The dominant logic of each group is different, but the conclusions are similar. During the last decade, each group has been searching for ways out of this self-imposed intellectual trap. To eradicate poverty, we have to break this implicit compact through a BOP-oriented involvement of the private sector.

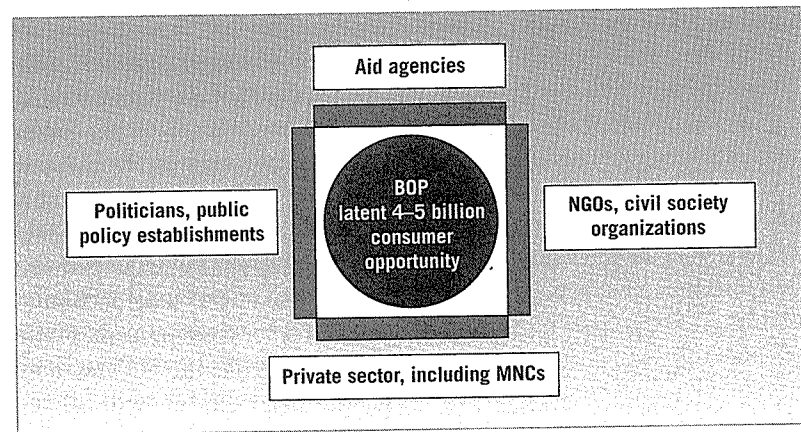


Figure 1.2 The influence of dominant logic.

We have to change our long-held beliefs about the BOP—our genetic code, if you will. The barrier that each group has to cross is different, but difficult nonetheless. However, after we cross the intellectual barrier, the opportunities become obvious. The BOP market also represents a major engine of growth and global trade, as we illustrate in our subsequent stories of MNCs and private firms from around the world.

The Nature of the BOP Market

The nature of the BOP market has characteristics that are distinct. We outline some of the critical dimensions that define this market. These characteristics must be incorporated into our thinking as we approach the BOP.

There Is Money at the BOP

The dominant assumption is that the poor have no purchasing power and, therefore, do not represent a viable market.

Let us start with the aggregate purchasing power in developing countries where most of the BOP market exists. Developing countries offer tremendous growth opportunities. Within these markets, the BOP represents a major opportunity. Take China as an example. With a population of 1.2 billion and an average per capita gross domestic product (GDP) of U.S. \$1,000, China currently represents a \$1.2 trillion

economy. However, the U.S. dollar equivalent is not a good measure of the demand for goods and services produced and consumed in China. If we convert the GDP-based figure into its dollar purchasing power parity (PPP), China is already a \$5.0 trillion economy, making it the second largest economy behind the United States in PPP terms. Similarly, the Indian economy is worth about \$3.0 trillion in PPP terms. If we take nine countries—China, India, Brazil, Mexico, Russia, Indonesia, Turkey, South Africa, and Thailand—collectively they are home to about 3 billion people, representing 70 percent of the developing world population. In PPP terms, this group's GDP is \$12.5 trillion, which represents 90 percent of the developing world. It is larger than the GDP of Japan, Germany, France, the United Kingdom, and Italy combined. This is not a market to be ignored.

Now, consider the BOP within the broad developing country opportunity. The dominant assumption is that the poor do not have money to spend and, therefore, are not a viable market. Certainly, the buying power for those earning less than U.S. \$2 per day cannot be compared with the purchasing power of individuals in the developed nations. However, by virtue of their numbers, the poor represent a significant latent purchasing power that must be unlocked. For example, all too often, the poor tend to reside in high-cost ecosystems even within developing countries. In the shanty town of Dharavi, outside Mumbai, India, the poor pay a premium for everything from rice to credit. Compare the cost of everyday items of consumption between Dharavi and Warden Road (now redesignated B. Desai Road), a higher-income neighborhood in Mumbai. The poverty penalty in Dharavi can be as high as 5 to 25 times what the rich pay for the same services (see Table 1.2). Research indicates that this poverty penalty is universal, although the magnitude differs by country. The poverty penalty is the result of local monopolies, inadequate access, poor distribution, and strong traditional intermediaries. Large-scale private-sector businesses can “unlock this poverty penalty.” For example, the poor in Dharavi pay 600 to 1,000 percent interest for credit from local moneylenders. A bank with access to this market can do well for itself by offering credit at 25 percent. Although 25 percent interest might look excessive to a casual observer, from the point of view of the BOP consumer, access to a bank decreases the cost of credit from 600 percent to 25 percent. The BOP consumer is focused on the difference between the local moneylender rates and the rates that a commercial bank would charge. The bank can make a

reasonable profit after adjusting for risk (10 percent over its traditional, top-of-the-pyramid customers). We argue later that the BOP consumers do not represent higher risk.

Table 1.2 The Poor and High-Cost Economic Ecosystems

Item	Dharavi	Warden Road	Poverty Premium
Credit (annual interest)	600–1,000%	12–18%	53.0
Municipal grade water (per cubic meter)	\$1.12	\$0.03	37.0
Phone call (per minute)	\$0.04–0.05	\$0.025	1.8
Diarrhea medication	\$20.00	\$2.00	10.0
Rice (per kg)	\$0.28	\$0.24	1.2

Source: Reprinted with permission from *Harvard Business Review*. "The Poor and High Cost Economics Ecosystems." From "Serving the World's Poor Profitably" by C.K. Prahalad and Allen Hammond, September 2002. Copyright © 2002 by the Harvard Business School Publishing Corporation, all rights reserved.

These cost disparities between BOP consumers and the rich in the same economy can be explained only by the fact that the poverty penalty at the BOP is a result of inefficiencies in access to distribution and the role of the local intermediaries. These problems can easily be cured if the organized private sector decides to serve the BOP. The organized sector brings with it the scale, scope of operations, and management know-how that can lead to efficiencies for itself and its potential consumers.

The poor also spend their earnings in ways that reflect a different set of priorities. For example, they might not spend disposable income on sanitation, clean running water, and better homes but will spend it on items traditionally considered luxuries. Without legal title to land, these residents are unlikely to invest in improving their living quarters, much less the public facilities surrounding their homes. For example, in Dharavi, 85 percent of the households own a television set, 75 percent own a pressure cooker and blender, 56 percent own a gas stove, and 21 percent have telephones. In Bangladesh, women entrepreneurs with cell phones, which they rent out by the minute to other villagers, do a brisk business. It is estimated that the poor in Bangladesh spend as much as 7 percent of their income on connectivity.

Access to BOP Markets

The dominant assumption is that distribution access to the BOP markets is difficult and, therefore, represents a major impediment for the participation of large firms and MNCs.

Urban areas have become a magnet for the poor. By 2015, there will be more than 225 cities in Africa, 903 in Asia, and 225 in Latin America. More than 368 cities in the developing world will have more than 1 million people in each. There will be at least 23 cities with more than 10 million residents. Collectively, these cities will account for about 1.5 to 2.0 billion people. More than 35 to 40 percent of these urban concentrations will be composed of BOP consumers. The density of these settlements—about 15,000 people per hectare—will allow for intense distribution opportunities.

The rural poor represent a different problem. Access to distribution in rural markets continues to be problematic. Most of the rural markets are also inaccessible to audio and television signals and are often designated as "media dark." Therefore, the rural poor are not only denied access to products and services, but also to knowledge about what is available and how to use it. The spread of wireless connectivity among the poor might help reduce this problem. The ability to download movie and audio clips on wireless devices might allow firms to access traditionally "media dark" areas and provide consumers in these locations with newfound access to information about products and services. However, this is still an evolving phenomenon restricted to a few countries.

The BOP does not lend itself to a single distribution solution. Urban concentrations represent a problem distinct from that of the distribution access to dispersed rural communities. Worldwide, the cost of reach per consumer can vary significantly across countries. A wide variety of experiments are underway in these markets to find efficient methods of distributing goods and services. One such experiment, Project Shakti at Hindustan Lever Ltd. (HLL) in India, is a case in point. HLL created a direct distribution network in hard-to-reach locales (markets without distribution coverage through traditional distributors and dealers). HLL selected entrepreneurial women from these villages and trained them to become distributors, providing education, advice, and access to products to their villages. These village women entrepreneurs, called Shakti Amma ("empowered mother"), have unique knowledge about what the village needs and which products are in demand. They earn between Rs.

3,000 and 7,000 per month (U.S. \$60–\$150) and, therefore, create a new capacity to consume for themselves and their families. More important, these entrepreneurial women are increasingly becoming the educators and access points for the rural BOP consumers in their communities. This approach is not new. Avon is one of the largest cosmetics operations in Brazil and has used a similar approach by leveraging more than 800,000 “Avon ladies” as distributors to reach even the most remote regions of Amazonia.¹

The BOP Markets Are Brand-Conscious

The dominant assumption is that the poor are not brand-conscious. On the contrary, the poor are very brand-conscious. They are also extremely value-conscious by necessity.

The experience of Casas Bahia in Brazil and Elektra in Mexico—two of the largest retailers of consumer durables, such as televisions, washing machines, radios, and other appliances—suggests that the BOP markets are very brand-conscious. Brand consciousness among the poor is universal. In a way, brand consciousness should not be a surprise. An aspiration to a new and different quality of life is the dream of everyone, including those at the BOP. Therefore, aspirational brands are critical for BOP consumers. However, BOP consumers are value buyers. They expect great quality at prices they can afford. The challenge to large firms is to make aspirational products affordable to BOP consumers. These consumers represent a new challenge for managers with increased pressure on costs of development, manufacturing, and distribution. As a result, BOP markets will force a new level of efficiency in the MNCs, as we demonstrate in Chapter 2, “Products and Services for the BOP.”

The BOP Market Is Connected

Contrary to the popular view, BOP consumers are getting connected and networked. They are rapidly exploiting the benefits of information networks.

The spread of wireless devices among the poor is proof of a market at the BOP. For example, by the end of 2003, China had an installed base of 250 million cell phones. India had an installed base of approximately 30 million. The Indian market is growing at about 1.5 million handsets per month and reached 100 million handsets by 2005. Brazil already had 35 to 40 million. Both the current market size and the growth rates suggest that the BOP market is a critical factor in worldwide wireless

growth. Telecommunications providers have made it easier for BOP consumers to purchase handsets and service through prepaid cards. The proliferation of wireless devices among the poor is universal, from Grameen Phone in Bangladesh to Telefonica in Brazil. Further, the availability of PCs in kiosks at a low price per hour and the opportunity to videoconference using PCs are adding to the intensity of connectivity among those at the BOP. The net result is an unprecedented ability of BOP consumers to communicate with each other in several countries. The technology of wireless and PC connectivity allows the BOP population to actively engage in a dialogue with each other, with the firms from which they want to purchase goods and services, and with the politicians who represent them.

Connectivity also allows the BOP consumers to establish new patterns of communication away from their villages. With cell phones and TV, the BOP consumer has unprecedented access to information and opportunities to engage in a dialogue with the larger community. As a result, word of mouth among BOP consumers is becoming a potent force for assessing product quality, prices, and options available to them. The spread of good bargains and bad news can be rapid. For example, in India, it appears that some consumers found worms in chocolates sold by Cadbury, a large and very successful MNC. Ten years ago, this would have been a nonevent, but with access to multiple and fiercely competitive TV channels, wireless, and Internet, the news spread so rapidly across India that not just managers within Cadbury but all managers involved in the “fast-moving consumer goods” industry were surprised and worried.²

BOP Consumers Accept Advanced Technology Readily

Contrary to popular belief, the BOP consumers accept advanced technology readily.

The spread of wireless devices, PC kiosks, and personal digital assistants (PDAs) at the BOP has surprised many a manager and researcher. For example, ITC, an Indian conglomerate, decided to connect Indian farmers with PCs in their villages. The ITC e-Choupal (literally, “village meeting place”) allowed the farmers to check prices not only in the local auction houses (called *mandis*), but also prices of soybean futures at the Chicago Board of Trade. The e-Choupal network allowed the farmers access to information that allowed them to make decisions about how much to sell and when, thus improving their

margins. Similarly, women entrepreneurs in southern India, given a PC kiosk in their villages, have learned to videoconference among themselves, across villages on all kinds of issues, from the cost of loans from various banks to the lives of their grandchildren in the United States.³ Chat rooms are full of activity that none of us could have imagined. Most interestingly, in Kerala, India, fishermen in traditional fishing boats, after a day of productive work, sell their catch to the highest bidders, using their cell phones to contact multiple possible landing sites along the Kerala coast. The simple boats, called catamarans, have not changed, but the entire process of pricing the catch and knowing how to sell based on reliable information has totally changed lives at the BOP.⁴ The BOP consumers are more willing to adopt new technologies because they have nothing to forget. Moving to wireless from nothing is easier than moving to wireless from a strong tradition of efficient and ubiquitous landlines.

The Market Development Imperative

The task of converting the poor into consumers is one of market development. Market development involves both the consumer and the private-sector firm. We consider the risks and benefits to the private-sector firm later. Here, we reflect on the incentives for the BOP consumer, who is so far isolated from the benefits of access to regional and global markets, to participate. What are the benefits to the BOP consumer? Our examples are drawn primarily from the stories that appear in the book.

Create the Capacity to Consume

To convert the BOP into a consumer market, we have to create the capacity to consume. Cash-poor and with a low level of income, the BOP consumer has to be accessed differently.

The traditional approach to creating the capacity to consume among the poor has been to provide the product or service free of charge. This has the feel of philanthropy. As mentioned previously, charity might feel good, but it rarely solves the problem in a scalable and sustainable fashion.

A rapidly evolving approach to encouraging consumption and choice at the BOP is to make unit packages that are small and, therefore, affordable. The logic is obvious. The rich use cash to inventory convenience. They can afford, for example, to buy a large bottle of shampoo to avoid multiple trips to the store. The poor have unpredictable income streams. Many subsist on daily wages and have to use cash conservatively. They tend to make purchases only when they have cash and buy only what they need for that day. Single-serve packaging—be it shampoo, ketchup, tea and coffee, or aspirin—is well suited to this population. A single-serve revolution is sweeping through the BOP markets. For example, in India, single-serve sachets have become the norm for a wide variety of products, as shown in Table 1.3.

Table 1.3 Creating the Capacity to Consume: Single-Serve Revolution

Single-Serve Value at Retail		
Rs.	\$	Typical Products
0.50	0.01	Shampoo, confectionary, matches, tea
1.00	0.02	Shampoo, salt, biscuits, ketchup, fruit drink concentrate
2.00	0.04	Detergent, soap, mouth fresheners, biscuits, jams, spreads, coffee, spices
5.00	0.10	Biscuits, toothpaste, color cosmetics, fragrance, bread, cooking oil, skin cream

Note: Shampoo and biscuits are shown under different price ranges because these items are available in multiple single-serve and low unit pack quantities.

The number of products sold in the single-serve format is rapidly increasing. The format is so popular that even firms producing high-end merchandise have to adopt it to remain viable long-term players in the growing markets. For example, in the shampoo business, the situation in the Indian market is shown in Figure 1.3.

Measured in tons, the size of the Indian shampoo market is as large as the U.S. market. Large MNCs, such as Unilever and Procter & Gamble (P&G), are major participants in this market, as are large local firms. Because the poor are just as brand-conscious as the rich, it is possible to buy Pantene, a high-end shampoo from P&G, in a single-serve sachet in India. The entrepreneurial private sector has created a large market at the BOP; the penetration of shampoo in India is about 90 percent.

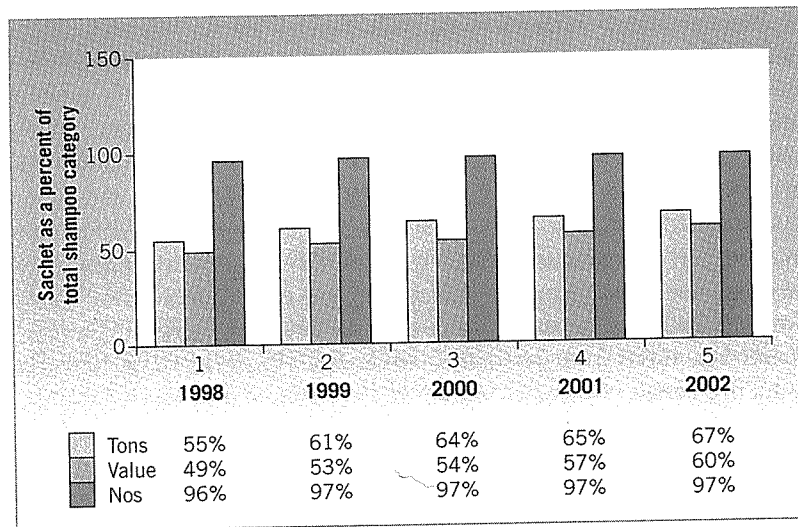


Figure 1.3 Single-serve sachet as a percentage of total shampoo market in India.

A similar approach to creating capacity to consume is through innovative purchase schemes. More BOP consumers in Brazil can buy appliances through Casas Bahia because the firm provides credit even for consumers with low and unpredictable income streams. Through a sophisticated credit rating system coupled with counseling, Casas Bahia provides access to high-quality appliances to consumers who could not otherwise afford them. At the same time, the firm ensures that its consumers are not overstretched. The default rate is low at 8.5 percent, compared to more than 15 percent for competitor firms. Casas Bahia has also created a new pool of repeat customers. CEMEX, one of the world's largest cement companies in Mexico, follows a similar approach in its "do-it-yourself" business focused on the BOP market. The idea is to help the consumers learn to save and invest. By creating a pool of three women who save as a group and discipline and pressure each other to stay with the scheme, CEMEX facilitates the process of consumption by bundling savings and access to credit with the ability to add a bathroom or a kitchen to their homes.

Creating the capacity to consume is based on three simple principles best described as the "Three As":

1. *Affordability.* Whether it is a single-serve package or novel purchasing schemes, the key is affordability without sacrificing quality or efficacy.
2. *Access.* Distribution patterns for products and services must take into account where the poor live and their work patterns. Most BOP consumers must work the full day before they can have enough cash to purchase the necessities for that day. Stores that close at 5:00 PM have no relevance to them, as their shopping begins after 7:00 PM. Further, BOP consumers cannot travel great distances. Stores must be easy to reach, often within a short walk. This calls for *geographical intensity of distribution.*
3. *Availability.* Often, the decision to buy for BOP consumers is based on the cash they have on hand at a given point in time. They cannot defer buying decisions. Availability (and therefore, *distribution efficiency*) is a critical factor in serving the BOP consumer.

Of course, the ideal is to create the capacity to earn more so that the BOP consumers can afford to consume more. The ITC e-Choupal story illustrates how farmers with access to the Internet and thereby access to the prices of commodities around the world can increase their incomes by 5 to 10 percent. These farmers can decide when and how much to sell based on their understanding of the likely price movements for their products. Modern technology not only allows them to realize better prices, but also to improve their logistics. The aggregation of food grains allows for efficiencies for both the farmer and the buyer.

By focusing on the BOP consumers' capacity to consume, private-sector businesses can create a new market. The critical requirement is the ability to invent ways that take into account the variability in the cash flows of BOP consumers that makes it difficult for them to access the traditional market for goods and services oriented toward the top of the pyramid.

The Need for New Goods and Services

The involvement of the private sector at the BOP can provide opportunities for the development of new products and services.

Amul, a dairy cooperative in India, has introduced good-quality ice cream at less than \$0.05 per serving, affordable by all at the BOP. This product is not only a source of enjoyment; the milk in it is also a source

of nutrition for the poor. Now, Amul is planning to introduce a natural laxative-laced ice cream called "isabgol-enriched." It is too early to tell whether the product can be a success. However, the experimentation is what the game is about. Similarly, the popularization of pizza by the same company allows the poor to obtain an adequate quantity of protein.⁵ PRODEM FFP, a Bolivian financial services company, has introduced smart automated teller machines (ATMs) that recognize fingerprints, use color-coded touch screens, and speak in three local languages. This technological innovation allows even illiterate BOP consumers to access, on a 24-hour basis, high-quality financial services.⁶ CEMEX, as we saw earlier, provides access to good quality housing. Through Tecnosol, the BOP consumers in rural Nicaragua have access to clean energy from renewable sources—solar and wind power. Previously, these consumers did not have access to grid-based electricity and were dependent on more expensive sources, such as kerosene and batteries. Now they have energy that is affordable enough to run their households. Casas Bahia not only sells appliances, but has also introduced a line of good-quality furniture oriented toward the BOP markets. Furniture has become one of the fastest growing businesses for the company and a source of pride and satisfaction to its consumers.

Dignity and Choice

When the poor are converted into consumers, they get more than access to products and services. They acquire the dignity of attention and choices from the private sector that were previously reserved for the middle-class and rich.

The farmers we interviewed at an ITC e-Choupal were clear. The traditional auctioning system at the government-mandated markets (mandis) did not offer them any choices. When they went to a mandi, they had to sell their produce at the prices offered on that day. They could not wait for better prices or haul their produce back to their villages. More important, the local merchants who controlled the mandi were not respectful of the farmers. One farmer remarked, "They make rude comments about my produce. They also raise the prices in the auction by \$0.02 per ton. It is as if they have already determined the price you will get and they go through the motions of an auction. It used to be very demeaning." Not any longer. Now, the same farmers can access information on the Web across all the mandis and can decide where, when, and at which prices they want to sell. Similarly, women in

self-help groups (SHGs) working with ICICI Bank in India also have had their dignity restored. As a group, they decide which borrowers and projects receive loans. This involvement of women in leadership development and in learning about finances and bank operations has given them a new sense of personal worth. The single-serve revolution has created a revolutionary level of choice for consumers at the BOP. For example, the "switching costs" for the consumer are negligible because she can buy a sachet of shampoo or detergent or pickles; if she is not satisfied with her purchase, she can switch brands the next day. Firms must continuously innovate and upgrade their products to keep customers interested in their brands, thereby improving quality and reducing costs.

Trust Is a Prerequisite

Both sides—the large firms and the BOP consumers—have traditionally not trusted each other. The mistrust runs deep. However, private-sector firms approaching the BOP market must focus on building trust between themselves and the consumers.

This is clearly evident when one visits a Casas Bahia store. BOP consumers here venerate the founder, Mr. Klein, for giving them the opportunity to possess appliances that they could not otherwise afford. Although the shanty towns of Sao Paulo or Rio de Janeiro can be dangerous to outsiders, Casas Bahia trucks move freely around without worry. The same is true for Bimbo, the provider of fresh bread and other bakery products to the BOP consumers in Mexico. Bimbo⁷ is the largest bakery in Mexico, and its trucks have become symbols of trust between the BOP consumers and the firm. The truck drivers are so trusted that often the small store owners in the slums allow them to open their shops, stock them with bread, and collect cash from the cash boxes without supervision. Both Casas Bahia and Bimbo believe that the truck drivers who deliver their products to the BOP consumers are their ambassadors and neither company will outsource the delivery process. In fact, all managers at Bimbo must work as truck drivers for the company to become better educated about their customers.

MNCs often assume that the default rate among the poor is likely to be higher than that of their rich customers. The opposite is often true. The poor pay on time and default rates are low. In the case of ICICI Bank, out of a customer base of 200,000, the default rate is less than 1 percent. The default rate at Grameen Bank, a microfinance pioneer in

Bangladesh, is less than 1.5 percent among 2,500,000 customers. The lessons are clear. Through persistent effort and the provision of world-class quality, private-sector businesses can create mutual trust and responsibility between their companies and BOP customers. Trust is difficult to build after 50 years of suspicion and prejudice based on little evidence and strong stereotyping.

Benefits to the Private Sector

We have identified the immediate benefits of treating the poor as consumers and the poverty alleviation process that can result as businesses focus on the BOP. It is clear that the consumers (the poor) benefit, but do the private-sector businesses benefit as well? The BOP market potential is huge: 4 to 5 billion underserved people and an economy of more than \$13 trillion PPP. The needs of the poor are many. The case for growth opportunity in the BOP markets is easy to make. However, to participate in these markets, the private sector must learn to innovate. Traditional products, services, and management processes will not work. In the next chapter, we discuss a philosophy of innovation focused on BOP markets.

Endnotes

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