"Bottom of the pyramid" strategies combine the profit motive with development objectives. However, the idea that a multinational corporation might simultaneously drive profit and alleviate poverty has not become a reality; it requires a revised, more modest definition of promised outcomes so they may better integrate with corporate interests.

Bringing Bottom of the Pyramid into business focus

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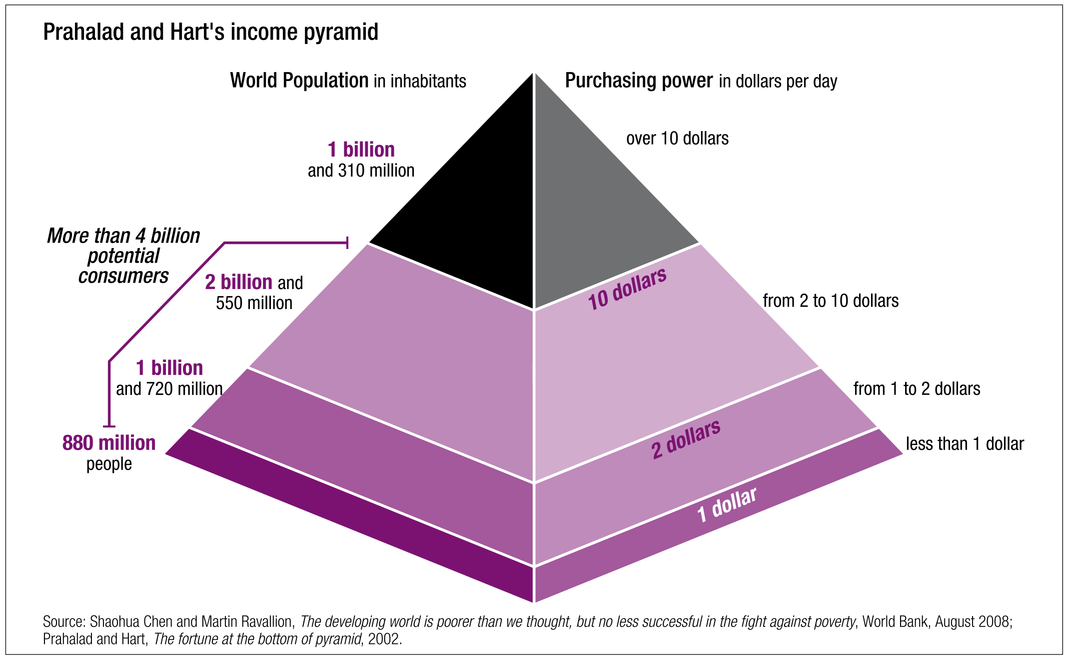
Like the popular Tex-Mex cuisine found across the United States, Bottom of the Pyramid (BOP) has been an effort to fuse two very different cultures. In place of culinary traditions, BOP has attempted to blend the core capabilities and resources of big business with the heart of global development institutions – a visionary fusion of profits with poverty alleviation (Prahalad and Hammond, 2002; Prahalad and Hart, 2002).

But the theory that global corporations could simultaneously drive profits and alleviate poverty by selling products and services to the world's four billion poorest consumers has proven less than palatable in practice. Over the more than dozen years since the concept was put forward, numerous business experiments to reach BOP consumers have failed to support the profit opportunity half of the hypothesis (Karamchandani, Kubzansky and Lalwani, 2011; Karnani, 2007).

Visibility into the challenge is further obscured by well-publicized corporate ventures deemed successes in the popular press by virtue of simply being operational and having expanded a pilot – actual profitability and return on investment remain far from certain. Two often referenced successes are the Hindustan Lever's Shakti initiative, an effort to build a door-to-door, rural sales channel in remote villages of India for the company's personal care and home care products by recruiting and training women micro-entrepreneurs from self-help groups; and ITC's e-choupal, which provides rural Indian farmers with market and agricultural data via village-based internet kiosks.

The disappointment hasn't been confined to the business-side of the equation. The broader development community's assessment of initial corporate ventures was less

FIGURE 1 **Estimating the size of the BOP market**



Source: Shaohua Chen and Martin Ravallion, *The developing world is poorer than we thought, but no less successful in the fight against poverty*, World Bank, August 2008; Prahalad and Hart, *The fortune at the bottom of pyramid*, 2002.

The work of Prahalad and Stuart (2002) revealed the existence of nearly 4 billion poor consumers whose needs were not being sufficiently taken into account by the market. The idea of developing specific products for this segment of the population is the logical next step.

than rosy. Seeing efforts that – to their eyes – were little more than attempts to sell products to the poor, the term "poverty wash" entered into the BOP lexicon (Karnani, 2007). In response to this critique, academics (including the author) and development practitioners urged corporations pursuing BOP markets to also expand the incomes of the poor by sourcing from them and incorporating them into their value chains (Drayton and Budinich, 2010); to empower and build local capacity by co-creating new businesses and products in close partnership with low-income communities (Simanis et al., 2008a; Simanis, Hart and Duke, 2008b); and to conduct rigorous assessments on the poverty-alleviation impacts of their ventures (London, 2009). In short, corporations were being asked to do what non-profits do.

It's not surprising, then, that the locus of corporate interest in BOP has steadily shifted away from the profit-and-loss side of the business to the philanthropic and social responsibility departments. Danone's partnership with Grameen Bank to bring wholesome yogurt to the poor in Bangladesh through a network of rural women entrepreneurs is one such high-profile effort. Rather than a fusion of competitive returns on investment with development impact – the vision that spurred initial enthusiasm among corporations – many of today's BOP ventures are corporate-funded development projects justified on the basis of their reputational value to the company. While

such corporate-social responsibility efforts do indeed bring tremendous value to the communities where they operate and should continue to be encouraged and expanded, they are a shadow of the initial vision.

The goal of this chapter is to help revive corporate interest in the BOP as a profit opportunity by bringing a business-focus back to the field. To do so, I summarize what I believe are key misconceptions concerning the roots of business success/failure in low-income markets, and the poverty alleviation potential of corporations more broadly. The issues reach from the field-level all the way up to the boardroom. I hasten to add that not only have I contributed to some of these misconceptions, but I have also guided and closely advised a number of failed corporate BOP business ventures that drew from this blueprint. This article is therefore based on hands-on experience and personal learning and reflects a fundamental re-thinking of some of my earlier positions.

Misconception 1: Build it right and they will come

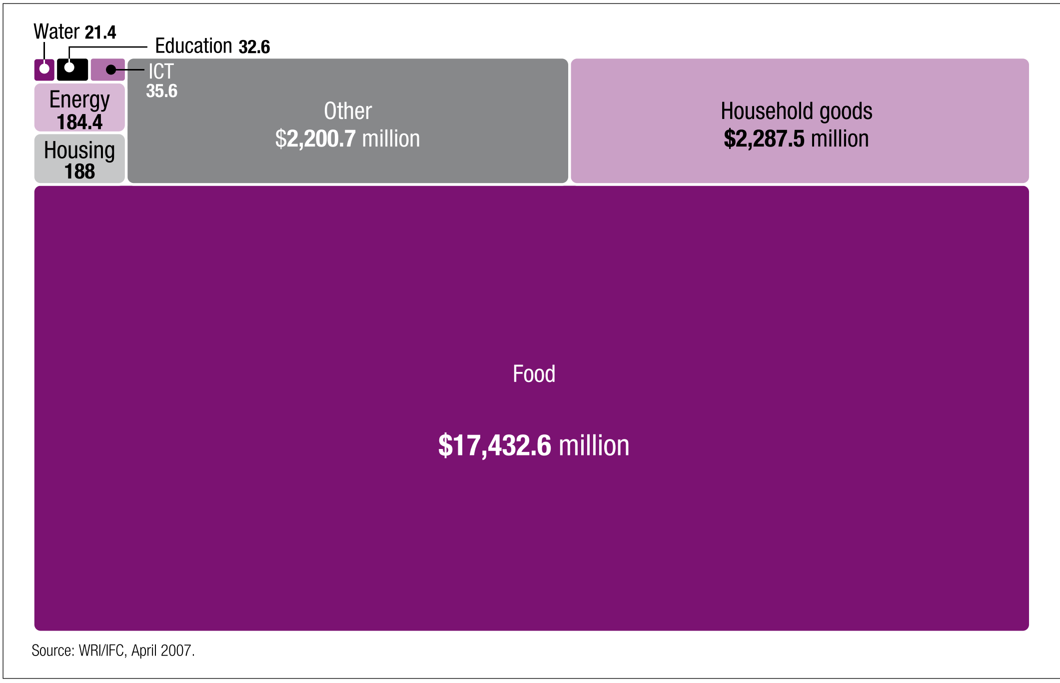
First, it's common to hear and read today that the true challenge of BOP markets is, first-and-foremost, one of understanding poor consumers' needs and translating those needs into high-quality products. Companies, so the argument goes, simply don't understand how these consumers live, what they value and what their aspirations are. Should a product fail to attract sufficient consumer demand to be profitable – as so often is the case – the company is faulted for not having truly heard the voice of the customer.

In fact, this was the theory at the very start of the BOP movement in the late 1990s – that companies, by working closely together with BOP consumers to "co-create" an offering, would crack the code. This view was also appealing from a development perspective, as it was consistent with the core tenets of what is called "participatory development" – a development approach popularized in the 1980s which calls for the close and active participation of the poor in the design and implementation of all solutions. Such deep participation empowers the poor, builds capabilities and ensures that solutions are appropriate for the local context (Chambers, 1983, 1997).

So what happened? Companies got on the ground, did in-depth research (in all of the projects I've led and advised in Africa and India, the teams and I did homestays in the slums and villages we aimed to serve), engaged the community in "co-creation" using various participatory techniques, launched products that seemed to address pressing needs, and then… failed. In many cases, there was no demand after all that co-creation and engagement – even for products that seemed so important to a healthy, normal life; such as clean water solutions, nutrient fortified food products, smoke-free stoves, etc.

What became clear to me is that needs aren't the same thing as a market (Simanis, 2009; Simanis, 2010). A market is a lifestyle built around a product. When a market exists, consumers have embedded a product and its value proposition into the fabric of their lives – buying and using it is second nature. In that case, market researchers and product designers can get really good consumer data, and it makes sense to work

FIGURE 2 **What is the BOP market made of?**



According to the WRI (2007), well-adapted products could meet a variety of basic needs of the poor. The two largest markets are the improvement of food and household equipment.

closely with consumers to improve a product's functionality.

But for most products launched in the BOP, there is no market – instead, a market has to be created. With market creation, traditional consumer research and data are fuzzy signals at best, as consumers have no reference point for understanding the value of the new functionality, nor the various changes to their existing routines, budgets and lifestyles that product adoption will entail. So it's possible to collect lots of data and get extensive consumer feedback – but when push comes to shove and consumers are asked to hand over money for the product they endorsed in the abstract, they balk.

Successful market creation requires a very different approach to product positioning and go-to-market strategies more broadly. The primary objectives are to help kick-start an initial consumer "sensemaking" process – a trial-and-error based form of experimentation – that invites consumers to figure out on their own terms how a product fits into their lives and the value it holds, and to then catalyse a bandwagon effect that, in sociological terms, normalizes the offering and makes it seem a necessary and vital part of any person's life. Specific marketing techniques that I've used with success in the field include pricing for repeat usage (rather than one-time sampling) and including "props" or familiar items from the consumers' context as part of the offering (as part of a rewards programme, for example). I've also tested and refined a "seed group" strategy that creates an initial group of committed users through workshops geared

towards encouraging participants to model key behaviours associated with the offering and begin feeling part of a high-visibility brand community.

Misconception 2: Target high volumes at low margins and price points

A second misconception that dates back to the very first BOP articles is that profitability is a matter of setting low margins and price points, and generating high volumes. The mathematics seemed intuitively correct: BOP consumers spend a scant dollar a day, but make up two-thirds of the world's population. Mathematics aside, I believe this proposed revenue model was quickly and uncritically accepted because it helped assuage the potential reservations of managers and executives in terms of making money off the proverbial backs of the poor: getting by on razor-thin margins seemed the morally correct way of doing business at the BOP.

However, basing a revenue model on intuition and emotional resonance has proven to be a recipe for failure. The low price/low margin/high volume strategy simply doesn't work in the majority of BOP markets, as it inevitably requires an impractical penetration rate of the target market (Simanis, 2012). Two factors account for this:

One, costs in BOP markets are much higher than in traditional markets. Compensating for poor infrastructure (e.g., outage-prone power grids, pot-holed roads) and absent or inefficient social institutions (e.g., corrupt law enforcement agencies, poor school systems) with back-up diesel generators and in-house employee literacy training programmes drives up operational costs beyond the levels found in traditional markets. The poverty penalty to which low-income consumers are subjected, which results in their paying more than their middle-class counterparts for essentially the same goods and services (Prahalad and Hammond, 2002), exists also on the supply side of the equation.

And because of the market creation issue discussed above, acquiring and retaining customers demands a very high-touch sales and marketing strategy. Getting people to value new-to-the-world functionality and changing long-held routines and behaviours –even when it can save their lives – is extremely difficult. Think about the massive campaigns and the measures taken just to get people to wear seatbelts and bicycle helmets or to use condoms. All this drives up costs and pushes out break-even timelines, as corporations have to pay for awareness building and behaviour modification through future profits (even if it forms partnerships with local NGOs, self-help groups and governments, as they too don't work for free).

The second factor is that business units in low-income markets come pre-set with an "efficient scale" that is extremely small. In economics, "efficient scale" refers to the size of business facilities, equipment, and operations that generate the highest level of efficiency and, thereby, maximize profits. Consider the previously mentioned e-Choupal venture by ITC that provides poor farmers with agricultural information: each one of their internet kiosks serves farmers living within just a five kilometres range. The main culprit behind this phenomenon is poor transportation infrastructure. Dismal road quality across rural areas drives up costs rapidly when companies

try to access consumers living further away from their base of operations. On the flip side, consumers are constrained to doing most all of their shopping within their own villages (or very nearby) because of the disproportionately high cost of local transportation. Consider that in rural Ghana the cost of a five-mile return trip using the public mini-bus is approximately $1.40. That's more than 20% of the average daily spend of a four-person farming family.

The upshot is that the business unit is forced to meet its sales volume target from the consumer base living in a narrow geographical range – one holding little more than a cluster of villages in rural areas, or several neighbourhoods in the case of larger slums. The only way to cover these disproportionately high operational costs and generate a return within a reasonable time frame without essentially converting an entire target market into repeat customers is by generating what accounting calls a high contribution per transaction (the sale price minus a product's variable costs). To raise contribution levels, a company has to raise its gross margin (by decreasing variable costs) and/or raise its sale price.

To generate very high contributions within a BOP context, companies inevitably have to restructure the entire business model: beginning with the value proposition, the pricing structure and down through the supply chain. Several generic strategies that I've outlined in prior published work that are effective in boosting contribution levels include offering a bundle comprised of bulk-format products; integrating an "enabling service" that engages customers in an activity linked to the bundle so that they self-teach themselves to maximize product functionality; and aggregating customers into peer groups (Simanis, 2012).

Misconception 3: High profits are unethical

A related misconception, or perhaps misunderstanding to be more accurate, concerns what constitutes an appropriate or reasonable profit level for corporations at the BOP. It's a topic for which I too have received criticism based on my argument above that very high gross margins are necessary for profitability in low-income market contexts.

While there are certainly ethical and moral dimensions to this debate, I believe that a significant portion of the confusion – particularly between the non-profit sectors and business – stems from something far less philosophical: definitional inconsistency. In other words, people are talking past one another, as they are using the word "profit" to mean very different things.

The term in common business usage refers (mainly) to three very different things – gross profitability, operational profitability, and investment profitability. When I wrote that companies needed very high profit levels, I was referring to the first two. As explained above, high gross profitability (sales minus variable costs) is necessary because of the higher-than average operational costs in these markets. If you don't start off with very high gross profitability, a business unit will find itself in the red when those operational costs are subtracted.

What is often misunderstood by those outside the business sector is that a venture can generate seemingly high year-on-year operational profitability – more or less the

equivalent of net profits – but still have negative investment profitability. Investment profitability is a measure of a project's overall return on investment and represents the payoff to the people (e.g., shareholders) who risked their money to make the project possible. It's a situation that the pharmaceutical industry – which is characterized by enormous upfront research and development costs and years of clinical trials before sales can begin – periodically struggles to explain to the public. Take, for example, a business that generates $1,000,000 of operating profits every year. If $2,000,000 was invested to launch the business and it is up and running in two years, the business has strong investment profitability by almost any measure; but if $20,000,000 was invested and it took five years to start seeing those profits, those risking their money are faring very poorly when they take into consideration inflation and the guaranteed returns they could have received by simply putting their money into a savings account.

Low-income market opportunities, much like the pharmaceutical industry, invariably require very high operational profitability to generate a positive return on investment. The reasons are two-fold. The first is that many of these opportunities won't see profits for many years, given the extensive market research, development of new products, and pilot tests that are necessary before sales start in earnest.

The problem is quite literally compounded in emerging markets, as the discount rate used to assess the present value of future profits is very high – 30% or more in many corporations. To put that in perspective, the present value of $1,000,000 of net profits earned ten years from a project's starting point is only $72,000 when a 30% discount rate is used.

The second reason is that the upfront investment costs needing to be recouped are often quite high, as many BOP opportunities demand extended, multi-country project teams, draw on a wide range of corporate capabilities, and entail extensive investment in assets and new business infrastructure (particularly on the distribution side).

As this suggests, very high gross and operational profitability do not automatically lead to "unfair" levels of investment returns. By that same token, an "investment-worthy opportunity" is also not inherently extortionist – it is simply one that covers within a given period of time those upfront expenditures, the income forgone or what economists call the opportunity cost (i.e., a guaranteed return on the money, usually equal to the interest rates paid by government-backed securities), and the risk that an investor assumes. As one might imagine, the opportunity costs in developing and emerging markets are higher (because inflation levels are generally much higher in emerging markets, thereby pushing up interest rates), and there is a lot more business risk because of the market creation issue. So it's not a case of trying to make more money off the backs of the poor; rather, it is the challenging nature of the investment climate that sets a high bar for corporate BOP ventures.

That said, once some of these markets are established, the necessary level of investment profitability will probably start to decline, as business risk decreases and competition increases. It is a dynamic that financial analysts call a "reversion to the mean". It's already taking place in some markets in the micro-finance industry (Porteus, 2006), thus forcing companies to maintain their investment profitability by reducing

their costs (as competition often doesn't allow them to increase their prices – in fact, companies usually face pressure to decrease prices). That's the so-called magic of markets and why they generally result in increasing consumer value over time.

Misconception 4: Corporations should use a blended value approach to BOP

The final misconception reaches the very heart of what makes a corporation a corporation. Increasingly, the rhetoric in the BOP space urges corporations to take a much broader approach to assessing the value of their investments – to base resource allocation decisions not simply on the expected returns to shareholders, but also on the value generated in poor communities. By this view, corporations should invest in expanding BOP ventures even if they fail to reach an internal hurdle rate of return, as the societal value of tackling poverty and providing for the unmet needs of the poor should essentially be viewed as offsetting that loss.

This discussion has been confounded by the advent of the impact investing field, which invests in social entrepreneurs first and foremost to generate a social or environmental impact and secondly to generate some financial return, and by the concept of the "social business" proposed by Nobel Prize winner and Grameen Bank Founder Mohammed Yunus. Yunus' social business is a business established to solve a social problem that covers its operational costs but pays no dividends to investors; all profits are reinvested in the business (Yunus, 2007).

The argument is absolutely understandable and certainly appealing. But it's a platitude, and fails to give due recognition to how institutions function, in particular how the need to appeal to key resource providers dictates behaviour. This view, known as resource dependence theory, essentially states that all organizations are dependent on outside resources; to maintain a flow of those resources and ensure the organization's survival, organizations have to perform first and foremost along dimensions important to the primary providers of those resources (Pfeffer and Salancik, 1978). So it's not just publicly-traded corporations that are beholden to these outside forces, but so too social enterprises, non-profits, churches, teachers associations and town hall assemblies. As Bob Dylan penned in song, "it may be the Devil or it may be the Lord, but you're gonna have to serve somebody."

So organizations that operate under various "non-profit" legal designations – like social enterprises/entrepreneurs, impact investment funds, multilaterals, and foundations to name a few – aren't acting benevolently in using a blended value approach: *they have an obligation to their resource providers to do so and to prioritize social impact over profits*. Why? Because people give resources to these organizations so that they impact on external social and environmental issues – not for the sake of growing the organization for the sake of itself. Self-obsolescence is, in fact, a sign of a mission accomplished.

That's not the case for corporations – the overwhelming majority of company investors (e.g., shareholders) give funds specifically so that the company grows itself in order to repay the original investment with a dividend, much like banks are expected

to pay interest on customers' savings deposits. So the changes in people's lives that a company's products and operations bring about are simply a means to the company's growth and longevity.

The point is that different institutions present different constraints and different boundaries to those working within them because of their differing obligations to resource providers. A corporation cannot do "BOP business" the same way as a social enterprise. For corporations to make BOP business part of their core operations, as Prahalad, Hart, Hammond and others initially envisioned, BOP resources will have to be allocated and the investments managed according to what capital markets and the shareholders that supply them with money set as the key benchmark of success: namely, rates of return better than or comparable to alternative investment opportunities. Corporations can, and hopefully increasingly do, bring progressive values to bear on how they achieve that target, but those values are not by themselves going to pay the bills, let the company continue growing, and attract additional investment capital.

The situation may change and a blended value approach may in fact eventually become a shareholder demand – but that day is a long way away, as institutional contexts evolve very slowly. So if you want a seat at that table today and to get corporations directing their core capabilities and core resources to social and environmental issues, the goal has to be re-framed in a way that it synchronizes with the norms, pressures and daily reality of the managers – not the other way around. As renowned 1970s community organizer Saul Alinksy argued in his seminal book, *Rules for Radicals*, if you aren't communicating within the experience of your audience, you simply aren't in the game (Alinsky, 1971).

And that is exactly what has happened to the BOP field over the last decade. We (I include myself here) got too caught up with our own beautiful theories and abstract concepts (like mutual value creation, inclusive business) and lost sight of the pressure on managers to meet next quarter's sales and earnings forecast. We theorized ourselves out of being relevant. As I noted in the introduction, the consequence is that companies are turning away from the space or only approaching it as a corporate social responsibility project. And that's a real loss, as companies can bring unique value to the poor.

But it's a loss caused as much by the perverse pressures that drive corporate decisions, as it is by the field's lack of creativity in re-framing these concepts and goals in a way that can speak to managers – from those sitting in the "C-Suite" (the top senior executives), right down to those in the field (Simanis and Milstein, 2012). We as a field need to start putting into practice our own recommendation about avoiding top-down or so-called "push solutions." Instead we need to get on the proverbial shop floor and come up with solutions that work for the very managers whose annual performance reviews depend on successfully implementing them.

Consider the total quality management (TQM) and just in time (JIT) management revolutions as case studies. I would wager that these management practices – ones today considered baseline skills for any respectable company – have had an order-of-magnitude greater impact on reducing firm's and industries' environmental impacts than all "environmental management initiatives" combined. But TQM and JIT have

FIGURE 3 Misconceptions of the BOP approach

	Conventional wisdom	Emerging reality
Product	**Co-designing products** enables the unique needs of BOP consumers to be met and to open **new markets**.	Getting BOP consumers to adopt new functionalities and product routines requires **market creation strategies**.
Business model	**Low margin**, low price and high volume models are key to success in BOP markets.	The majority of BOP markets require a **very high contribution** per transaction (high volumes plus high price points).
Investment model	Aiming for high **profitability** in BOP markets is **unethical**.	The challenging investment climate in the BOP demands **high gross profitability** and **high operational profitability**.
BOP paradigm	Corporations should consider aggregate **social, environmental and economic value** when making and evaluating BOP investments.	Make BOP **part of core business operations** by re-framing poverty alleviation goals in traditional business economic outputs.

Source: Erik Simanis.

The BOP approach, as it has been conducted, has raised hopes, achieved mobilization and led to disappointments. In the experience of the author, it is often the principles adopted by stakeholders for product definition, along with market research that have resulted in unsatisfactory outcomes. Other approaches are possible.

had such a profound environmental impact precisely because they were not undertaken for that purpose.

The goals, practices, language and metrics of TQM and JIT are focused on enabling a company to drive profitability and top-line growth – the environmental benefits were derivative of achieving the core institutional objective. It's going to take the same kind of framing and approach if corporations are to make BOP and the creation of social value a part of their core operations.

Conclusion

Audacity and bold visions are powerful and necessary tools for change. By freeing oneself from the limitations of current reality, they open minds, instil hope, catalyse motivation and spur action. The BOP concept has unquestionably had such an effect.

But visions alone – no matter how often they are repeated or how boldly they are proclaimed – will not result in lasting institutional change. Sustained change requires bringing a vision back down to earth and re-embedding it into the day-to-day realities and practices that give institutions their shape and form. That process, however,

is one of mutual adaptation and negotiation – not only will the organization change, but so too the vision. And that's an unsettling process, as it requires letting go of the purity of one's vision and frequently contenting oneself with half-wins and incremental advancements.

Today, the BOP concept is faced with such a decision: either we adapt the vision to meet the realities of the corporation, or we risk the concept fading entirely from corporate business agendas. To be clear, it's not a question of going back to "business as usual" and giving up on the vision of a better world. Rather, bringing a business focus back to the BOP concept is an exciting next phase in an on-going process of change – one that will demand creativity and open up new waves of research and new opportunities for interaction and learning among academia, the development sector and global business. It is my hope that this article helps to shine a light on some of the potential new pathways that can make BOP a lasting part of corporate business agendas. ■

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