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Changing Poverty and Inequity through Business

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Abstract

Business has the capacity to positively change the global problem of poverty and inequity but traditional ways of doing and thinking about business must be transformed and revolutionized. This paper will illustrate how business can become an innovative tool for social change by focusing on the pioneering principals of microfinance and the market Base of the Pyramid (BOP). These two business models will be examined in a macro and micro context to allow the reader to fully envision how the concepts can be used to change the brutal reality of the World's demographics. Latin America is focused on throughout the paper because it is saturated with poverty (nearly 1/4 of Latin Americans live on under \$2 US per day) and has the highest rate of inequity in the World.

This paper proves that if business does not harness the ideas of Microfinance and the market of the BOP, economic and social consequences have the potential to become more devastating. These two business models enforce that there is an opportunity to make a profit while providing much needed services and products to the poor. The prospects of using business to fight poverty and inequity are vast and the results can be extraordinary.

Introduction

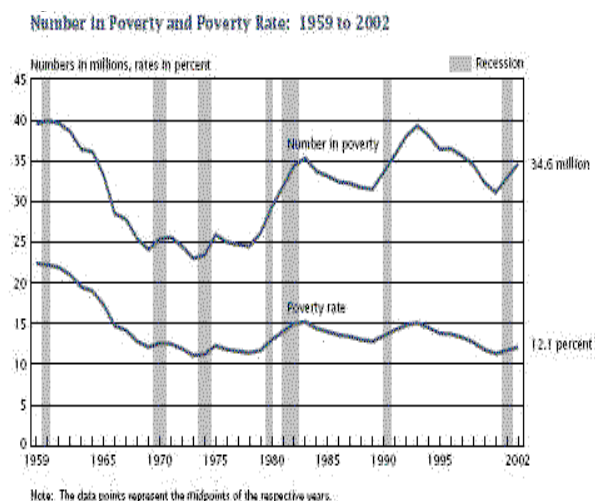
The poverty of our century is unlike that of any other. It is not, as poverty was before, the result of natural scarcity, but of a set of priorities imposed upon the rest of the world by the rich. Consequently, the modern poor are not pitied...but written off as trash. The twentieth-century consumer economy has produced the first culture for which a beggar is a reminder of nothing. ~John Berger

Poverty and Inequity have surrounded and saturated Latin America like a fog; the poor seldom see the horizon of hope and do not have the luxury to be guided through it. This report is not trying to solve the problems of poverty and inequity, but it will illustrate how business can become a revolutionary tool for social change. The report encompasses the concepts of microfinance and the market at the Base of the Pyramid (BOP). These two business

models enforce that there is opportunity to make a profit while providing much needed services and products to the poor.

Currently microfinance and BOP markets have been successful, but they have not evolved rapidly enough to change the demographics of our world (Figure 1). These innovative ideas have essentially not been fully created and have an immense amount of potential. A parallel can be drawn with the business opportunities, which are related to the phenomenon of global warming. The truth is global warming, like poverty, is a global issue, which we have created; therefore we can also create solutions. Business will become a major factor in the eradication of poverty and inequity, the BOP markets and microfinance reinforce the concept that business can effectively and efficiently solve the problems of the poor (their customers).

Figure 1 - Poverty and Inequality in Latin America



Latin American has faced the problems of inequality and poverty since the arrival of the Spanish colonialists in the late 1400s. Humankind's tendency to conquer would continue. It has been over 500 years since the arrival of the Europeans to Latin America and the issues of slavery, exploitation, poverty and inequality continue to be part of everyday life (Figure 2). Latin America hosts the world's highest rate of income distribution and has the most unbalanced distribution of

resources (Hofman and Centeno 2004). The Gap between the rich and the poor is immense and the phenomenon of globalization has continued to allow this gap to increase. An example of this is Brazil; Currently, it boasts the world's 10th strongest economy and in a shocking 73rd place in social development. This extreme inequality and poverty has created many problems such as violence, drug abuse, crime and, most importantly, it has suppressed the ability for the Poor's dreams to turn into reality.

Figure 2

In Latin American Countries (LAC) a small percentage of people have control over the government and the resources. The rich and

Poverty in Latin America and the Caribbean 1981-2001

Share of people living on less than \$1 a day (%)

1981	1984	1987	1990	1993	1996	1999	2001
9.7	11.8	10.9	11.3	11.3	10.7	10.5	9.5

Share of people living on less than \$2 a day (%)

1981	1984	1987	1990	1993	1996	1999	2001
26.9	30.4	27.8	28.4	29.5	24.1	25.1	24.5

Source: 2004 World Development Indicators

powerful reap all of the benefits of the country's economy through the work of the poor. The poor gain nothing as the rich gain everything.

"The richest one-tenth of the population of Latin America and the Caribbean earn 48 percent of total income, while the poorest tenth earn only 1.6 percent ... In industrialized countries, by contrast, the top tenth receive 29.1 percent, while the bottom tenth earn 2.5 percent (The World Bank Group 2004)."

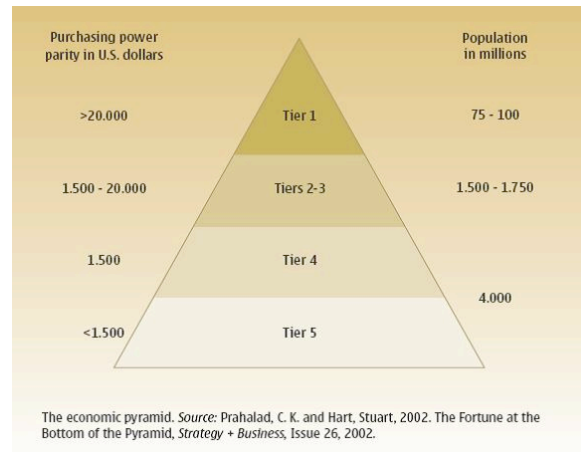
This theme of the haves and the have-nots is best illustrated in high traffic urban areas such as Downtown Buenos Aires or Rio De Janeiro. This is where the poor and rich are pushed together.

From Mexico to Argentina this vicious cycle of poverty and inequity has become a way of life. The number of people who live below the poverty line is alarming and the recent financial crises of the region have worsened the situation. It is estimated that 128 million people (24.5% of the total population) in Latin America and the Caribbean live in Poverty (living on less than \$2 a day) and 50 million of these people live in extreme poverty (living on less than \$1 per day) (The World Bank Group 2004). The poverty rate from 1981 – 2001 is shown in Figure 2 and shows a minimal amount of positive change. The problems of inequity and poverty in LA have not seen much improvement in the last two decades, although numerous local, national and international organizations have desperately tried to combat these issues. The solutions these institutions have implemented have been largely ineffective and inefficient.

The Role of Business

Business, in the current and traditional state, has not catered to the base of the pyramid (BOP) market segment (Figure 3) because of closed mindedness, lack of innovation and government policy shortcomings. As markets in North America and Western Europe continue to become exhausted and saturated, the world's business community must find new ways to make profits. The credit crisis in America is a perfect example of how Americans have extended their purchasing abilities too far and do not have enough income to support their current lifestyles. Either big business finds new markets or the world's economy may be in grave danger.

Figure 3 - The Economic Pyramid



New and dynamic business models are slowly directing their attention to the vast and growing market of the world's poor. The idea of the poor as a market is ironic yet realistic. "The primary role of business is to provide "the engine for Growth"... this unrealized potential offers both a commercial and social opportunity (IBLF n.d.)." Businesses can make a profit by providing products and services to the poor, but traditional business models, which cater to the top three tiers of the pyramid, need to be reevaluated and drastically changed. Until now business along with government policy have allowed poverty and inequality in Latin America to flourish and reproduce. The business community has the opportunity to impregnate poor communities with hope while making a profit.

The Opportunity at the Base of the Pyramid

There are over 4 billion people who are living at the base of the pyramid and the estimated Purchasing Power Parity ranges from 1.3 trillion dollars to 13 trillion dollars (Warnholtz 2007). Either way, this virtually untouched market is desperately waiting for the chance to be sold products and services which have been adapted to suit their lifestyles.

Stuart Hart, a renowned business professor at Cornell, is the founder of the BOP theory and believes targeting the BOP is a positive sum game where all stakeholders can be

provided for (Meyers 2005). "While most MNCs tend to ignore the people earning \$1,500 a year or less -- about two thirds of the world's population -- Hart contends that this is a lost social, environmental and financial opportunity (Meyers 2005)." Major multinational corporations are embracing Hart's ideas and believe he is right about the vast opportunities at the BOP. Hart strongly believes business must transform into "a more inclusive form of capitalism -- one that seeks to lift the entire human community, not just the 800 million richest -- and does so in a way that does not destroy the planet (Meyers 2005)."

The current marketing strategies of big business, which are directed towards people with high disposable incomes, will not work at the BOP; Therefore, marketing strategies must move from style based to substance based. A poor mother is not worried about the brand of shoes she is going to buy for her son, but she is worried about how long they will last. Best business practices of the developed world will not hold strong in the BOP markets of developing nations. A major drawback to this concept is if business is not socially and environmentally responsible, many new problems will be created.

SC Johnson at the BOP

C K Prahalad argues in his popular book, *The Fortune at the Bottom of the Pyramid*, that selling to the poor people at the 'bottom of the pyramid' (BOP) can simultaneously be profitable and help eradicate poverty (Karnani 2007). He argues in his book that this market segment is very lucrative and is a serious opportunity for big business (Karnani 2007). Large Multi-National Corporations such as SC Johnson have begun to embrace this market of 4 billion people.

In 2005, SC Johnson began a BOP protocol in Kenya; this project focused on both rural applications and urban applications. The two areas, which were focused on, were Kibera, (one of the world's largest slums) which is located just outside of Nairobi, and Nyota,

which is located in the agricultural rift valley (Base of the Pyramid Protocol n.d.). The goal of SC Johnson's protocol was to identify business opportunities in the regions. The area of Nyota is particularly important for SC Johnson because it produces a natural insecticide pyrethrum. SC Johnson uses this insecticide in many of its products, illustrating this MNC is not primarily driven by corporate responsibility (Base of the Pyramid Protocol n.d.). Primary data for the protocol was gained by having members of the team live with the potential consumers. Below is a testimonial of Justin DeKoszmovszky, a JC Johnson BoP Intern:

"It was clear from the start that the Protocol was not business as usual. We were generating deeper, more holistic relationships and very new insights into a potential consumer group by learning from them, living with them and partnering with them. We were co-creating new business models and routes to market that met the requirements and challenges of business in the BoP. It was crucial that the BoP enterprises created not be charity from any partner's perspective. Rather, to be sustainable, the new initiative had to be valuable and profitable for everyone involved (DeKoszmovszky 2005)."

Justin's testimonial reinforces that the traditional business model must be disregarded and that to succeed in this market businesses must be innovative, dynamic and think outside of the box.

Unilever at the BOP

Unilever is another large MNC that has decided to direct attention to the BOP market. Currently, there is a heated debate going on about Unilever's product "Fair and Lovely," a skin whitening cream which is marketed and sold to BOP in India (Leonard 2007). CK Prahalad has directed one side of the debate; Arneel Karnani has headed the other. (Leonard 2007). Both of these men are renowned professors and experts in business but have very different opinions on the BOP market. Prahalad believes the cream is socially positive while Karnani believes the cream is promoting racial ideals. The two

professors have been debating via essays, which have been published online (Leonard 2007).

Prahalad's essay "Selling to the Poor" tries to show the positive effects the skin whitening cream can have on the women in India who live at the BOP. This passage from "Selling to the Poor" illustrates Prahalad's views:

Beyond such benefits as higher standards of living and greater purchasing power, poor consumers find real value in dignity and choice. In part, lack of choice is what being poor is all about. In India, a young woman working as a sweeper outdoors in the hot sun recently expressed pride in being able to use a fashion product -- Fair and Lovely cream, which is part sun screen, part moisturizer, and part skin-lightener -- because, she says, her hard labor will take less of a toll on her skin than it did on her parents'. She has a choice and feels empowered because of an affordable consumer product formulated for her needs (Leonard 2007).

Prahalad's essay promotes Unilever's efforts to providing products to the BOP and he believes this product is a progressive step towards the evolution of the BOP market theory. As for Karnani, he is opposed to Unilever's product in India and believes the BOP markets will create more problems than solutions. In his essay "The Fortune at the BOP: A Mirage" he writes:

This is no empowerment! At best, it is an illusion; at worst, it serves to entrench her disempowerment. Women's movements in countries from India to Malaysia to Egypt obviously do not agree with Hammond and Prahalad, and have campaigned against these products. The way to truly empower this woman is to make her less poor, financially independent, and better educated; we need social and cultural changes that eliminate the prejudices that are the cause of her deprivations (Leonard 2007).

The debate between the two men shows how the BOP markets are product sensitive and for true progress to be made the right products and services must be offered.

KX Industries at the BOP

This idea of penetrating the market at the BOP has created a new type of business model, which is concerned with substance rather than style. The most dynamic firms will succeed in this emerging market. For example, KX industries has created a water filter which is both cheap and effective; it can provide water to a family for around \$10 a year (Subramaniam 2006).

The United Nations predicts that 1.3 billion people lack sufficient access to drinking water and they estimate by 2050 the number will rise to 4 billion (Subramaniam 2006). This filter has the potential to help millions of people while making a profit but KX Industries must find a way to successfully market their product to the BOP. The idea of providing to the BOP is still at a conception phase but will soon become a vital part of the poverty puzzle.

Microfinance

Business is slowly recognizing the opportunities of becoming part of sustainable development and many experts believe there is a huge potential in providing financial services for the poor. Microfinance is becoming a popular topic among business people, governments, academics and the general public. This form of business seems revolutionary and has attracted much support and interest. The potential for growth in this sector is enormous because of the amount of people living in the BOP. Microfinance is a BOP business, which currently has both strengths and weaknesses.

Background of Microfinance

Microfinance is nothing new, but Mohammad Yunus, who is the founder of Grameen Bank (Grameen means village), has turned this idea into a revolutionary weapon in the war on poverty and inequality (Infoplease n.d.). Yunus made his first loan in 1974 and founded the Grameen Bank in 1976 (Infoplease n.d.). The concept of microloans was harnessed by Yunus and, in honor of his success, he was awarded the Nobel Peace

Prize in 2006 (Infoplease n.d.). The Grameen Bank works all over the World but has only offered its' financial services to seven LAC (refer to Figure 4). Although Yunus' success has been grand, the consumers at the BOP continue to grow and the need for financial services is in great demand (refer to Figure 5). Countries like Haiti and Nicaragua have the highest percentage of people living on less than one dollar a day in the Americas; both country's poverty rate hovers around 50%. This type of poverty is unacceptable and should not be tolerated.

Figure 4 -The Grameen Bank Areas of Operation

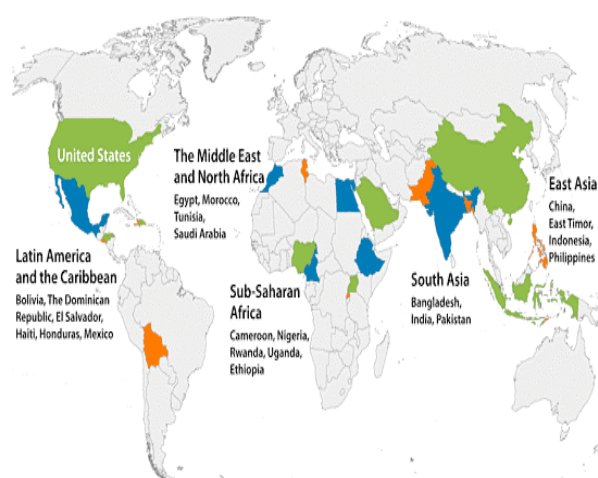


Figure 5

**MFI Growth Has Been Rapid:
Number of Microenterprise Loans and Growth**

December 1998	1,520,000
December 2000	1,914,000
June 2003	3,241,000
Total growth (1998-2003)	113%
Average annual growth	18.3%
<i>Source: IDB and CGAP surveys of 17 LA countries</i>	

The revolutionary idea of microloans has spread across the World from India to Bolivia and has allowed the microloan model to evolve into microfinance. Microfinance does

not only provide microloans. In theory, it is a business model that enables the user or consumer to benefit from multiple services. The main segments of microfinance include microinsurance, micropayments and microsavings. These three segments together offer the World's poor the opportunity to begin a new life where the joys of security and optimism are present and constantly growing. Currently, most providers of microfinance only provide their customers with the service of microcredits.

Spending time with people who are unemployed or who live below the poverty line is astonishing because you gain first hand knowledge about how they have learned to live on basically nothing by efficiently using their resources. Knowing how to turn nothing into everything is the key to business. The resourcefulness of the poor people who have been encountered is truly motivating.

Microfinance in Latin America

Microfinance in Latin America has not had the same exposure as many other parts of the world such as India and Africa (Merolae 2007). Microfinance is spread unevenly across Latin America; countries such as Bolivia and Honduras have gained most of the attention from MFIs (Merolae 2007) (Figure 6).

Currently, many traditional financial providers are becoming interested in the potential for profits by providing services for the poor. Microfinance is slowly being directed towards the hands of private business instead of relying on NGOs to provide the service. Microenterprises employ a major sector of working people in Latin America (Figure 7); this illustrates the need for microfinance.

Figure 6

Share of Microenterprises in Latin America with MFI Credit

Country	Date of Household Survey	Number of Single-Person Firms	Number of Firms with 1-5 Employees ^a	Total Number of Microenterprises	Number of Microenterprises with MFI Credit	Share of Microenterprises with MFI Credit
Bolivia	1999	1,300,313	62,008	1,362,321	379,117	27.83%
Nicaragua	1998	377,148	40,422	417,570	84,285	20.18%
El Salvador	1998	606,569	60,617	667,186	93,808	14.06%
Honduras	1999	832,941	58,239	891,180	107,054	12.01%
Chile	1998	1,069,139	138,045	1,207,184	82,825	6.86%
Guatemala	1998	1,328,476	93,238	1,421,714	71,187	5.01%
Costa Rica	1998	232,328	78,891	311,219	12,794	4.11%
Ecuador	1998	1,396,139	298,524	1,694,663	65,719	3.88%
Dominican Republic	1998	1,315,016	77,172	1,392,188	49,437	3.55%
Colombia	1999	5,726,653	775,152	6,501,805	219,240	3.37%
Paraguay	1998	319,113	668,213	987,326	30,203	3.06%
Peru	1997	4,102,561	2,763,632	6,866,193	185,431	2.70%
Panama	1999	267,854	21,150	289,004	6,390	2.21%
Mexico	1998	8,503,552	1,770,393	10,273,945	67,249	0.65%
Uruguay	1998	314,891	27,018	341,909	1,600	0.47%
Brazil	1999	16,567,943	2,421,810	18,989,753	62,485	0.33%
Argentina	1998	1,807,615	103,555	1,911,170	4,940	0.26%
Venezuela	1999	2,906,975	340,296	3,247,271	2,364	0.07%
Latin America Total Firms		48,975,225	9,798,375	58,773,600	1,526,128	
Latin America - Weighted Average Share^b						2.60%
Latin America - Unweighted Average Share^c						6.15%

Sources: Household surveys for number of microenterprises; Christen (2000) for number of microenterprises with MFI credit, except for Panama. Christen's data refer to the second half of 1999 and cover most of the larger regulated financial institutions and NGOs lending to microenterprises, but do not cover credit unions. Data for the number of microenterprises with MFI credit for Panama are obtained from the IDB loan files, refer to December 1999, and are as follows: Multicredit Bank 3881, Credifinandes 1549, and Mi Banco 960.

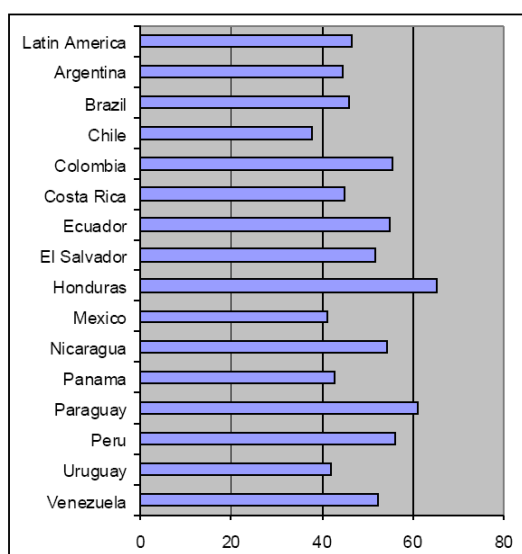
^a Unlike the other 15 countries in the table, in the Dominican Republic, Colombia, and Brazil, the number of firms with 1-5 employees is not counted directly, but, rather, is calculated as 83% of the total number of firms with 1 or more employees. This 83% share is the overall ratio for the other 15 countries, taken as a whole, of the number of firms with 1-5 employees divided by the total number of firms with 1 or more employees.

^b Calculated as (total number of microenterprises with MFI credit)/(total number of microenterprises).

^c Calculated as the unweighted average of the 18 individual-country percentages shown in the final column.

Figure 7

Microenterprise Share of Employment, 2002 (%)
(from *Panorama Laboral*, 2003, ILO)



Mujeres 2000 – Microfinance in Argentina

It is estimated that Argentina has around 200 microfinance institutions (MFI) and the majority of these institutions are informal (not recognized by the Government) (Merolae 2007⁵²). Currently in Argentina there is no legislation to control who enters this type of business. This creates problems because basically anyone can lend money without having the proper credentials. Less than 1% of all financial institutes represent microfinance but, in Argentina, there has been exponential growth in this sector in the last few years (Merolae 2007). The growth of MFIs in LAC is also rapidly increasing (refer to Figure 5). This is both positive and negative; the more MFIs in the market allow for more competition, but it also creates a need for more capital, which is not currently available (Merolae 2007). Most of the capital comes from charitable donations or from government subsidies (Merolae 2007).

⁵² The information gathered from Maria Merolae was obtained in a personal interview. Maria works for Mujeres 2000 as a volunteer. She also studies at la UCA in Buenos Aires. An explicit verbal agreement was established between Matt Tanner and Marie Merolae to allow her interview to be published in this report.

Mujeres 2000 was founded in 2000 and is a non-profit organization, which works only with microcredits. Currently, Mujeres 2000 is providing loans to 179 women in the Greater Buenos Aires area. Since its conception, 350 loans have been lent to women entrepreneurs totaling \$300,000. This microcredit organization provides its loans through donations from people, business and other non-profit organizations.

Mujeres 2000 provides loans only for women because they have proven to be the better candidates than men. Lending money to women is very common in this sector of finance and seems to be a best business practice. Women have the ability to make payments because they have the superior organizational skills, their children's futures motivate them and they desperately want to leave the vicious cycle of poverty (Merolae 2007). One of the major problems Mujeres 2000 has had is that the women get discouraged from obtaining loans because the process takes sometimes months to complete; these women do not have the time to wait because they are evidently living their lives on a day to day basis (Merolae 2007).

Mujeres 2000 is having success, but the organization reflects how many MFI are operated. The organization has only one employee who is paid (volunteer based), the interest rates are high (20% annual interest rate) when compared to financial institutions who provide services to the traditional market and, the market is being entered by firms without restrictions or government regulation (Merolae 2007). The future of microfinance is in private business where the bottom line is the motivator not empathy.

The Future of Microfinance

The future of microfinance is uncertain, but the expansion of providing financial services to the BOP is inevitable. Microfinance has currently not been the most efficient nor the most effective solution for providing loans to the poor; the high interest rates are a prime example of this. The lack of competition in

many of these impoverished areas is a major factor to high interest rates. Without the opportunity to use other financial services, the poor are forced to deal with inflated interest rates.

Soon, the small MFIs will be pushed out of this sector because the competition from formal financial providers will be too much for them to handle. Large financial firms like large MNC will be forced to enter these BOP markets because the traditional markets will not offer enough room for growth. The concept of providing financial services to the poor will evolve rapidly within the next decade, but microfinance may not be the final solution. The idea of using the Islamic form of banking has yet to emerge, but this type of lending without interest may soon replace microfinancing.

The Future for the BOP

The reality of the BOP markets illustrates that there is an enormous amount of potential for MFIs to penetrate a large market. Both microfinance and the market at the BOP are examples of how business is tackling the problems of inequity and poverty. These powerful tools can both be used to equalize the world's playing field and will continue to evolve through business. The 4 billion people living at the base of the pyramid need alternatives to improve their life. The common misperception that these people are incapable of providing for themselves is false. This report reveals how capable and motivated the world's poor are and, with some well guided help from business, the world's poor will transcend from their lives of poverty. The future generation of business will positively change the demographics of our world.

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