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SESSION III: GOODS, SERVICES AND JOBS FOR THE POOR
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GOODS, SERVICES AND JOBS FOR THE POOR

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EXECUTIVE SUMMARY:

Market-based solutions have the potential to provide goods, services and jobs for the poor at scale. Success in microcredit and a slew of exciting new ventures have led to an explosive growth in expectations, but the data on the ground is less rosy. Few models are reaching scale. The reason for this is that these models are tackling some of the world's toughest problems in difficult environments and, hence, require both innovative solutions and the removal of ecosystem barriers. Addressing these twin challenges takes significant resources, time and persistence. There are also high chances of failure and, even in successes, returns may be moderate. However, given the upside in terms of social impact at scale, it is important to support such solutions, and philanthropies and aid donors have a vital role to play in this.

WHAT'S THE ISSUE?

Historically, efforts at development have focused on two relatively separate paths. The private sector focuses on economically attractive opportunities to provide products and services and, in the process, grows the economy, generates tax revenues and creates jobs. The government focuses on providing an enabling environment for the private sector and, along with donors, philanthropies and nonprofits, addresses market failures and provides public goods, especially for the poor. Both these paths have had limited success in effectively serving the poor. In the past 10-15 years, there has been an increasing recognition of, and interest in, a third path to development—leveraging the effectiveness of the private sector to benefit the poor—using market-based solutions to provide goods, services and livelihoods to the poor (also known as the “bottom of the pyramid” or the BoP). Part of the attractiveness of these solutions is that they are commercially viable and, hence, can be self-sustaining and scalable without requiring huge and ongoing subsidies.

There have been some exciting market-based solutions that have demonstrated this potential. Microcredit has reached hundreds of millions of low income households. Solar lanterns are now serving 5 to 10 million households in India and Africa.

These successes have led to an explosive growth in expectations—from the investment community to governments. A recent J. P. Morgan report¹ sized the impact investing market (i.e., investing in commercial ventures that create social impact) as a “trillion dollar asset class.” Governments and philanthropic players have initiated Social Impact Funds to harness the private sector to address problems of poverty (e.g., the India Inclusive Innovation Fund and Africa Enterprise Challenge Fund).

While many of the solutions appear promising, few are reaching scale. A study² by Monitor Inclusive Markets of the most promising market-based solutions in Africa identified 439 ventures, of which 130 were commercially viable and 59 were at scale or clearly on the path to scale. A Monitor analysis of 50 inclusive businesses in Africa indicated that net operating margins were, at best, between 10 and 15 percent—a far cry from the “market returns” many investors are expecting.

Also, most of the solutions were being developed by social enterprises and not corporations. The hope that corporations would increasingly serve the BoP, including areas of social benefits, is not materializing at the rate required to produce scale impact. While corporations in some industries are extending their products and services to the BoP (e.g., companies that produce fast-moving consumer goods and pharmaceuticals are using smaller pack sizes, and telecom companies are using prepaid services), these are typically in situations where the business model for the higher end market can easily be extended to the BoP. Only a limited number of corporations have tried to develop the new models that are required to engage this segment. Of those that have tried, few have succeeded.³

WHAT NEEDS TO HAPPEN AND WHY?

This lack of scale from social enterprises and low interest from corporations is not difficult to understand. At the end of the day, these market-based solutions are tackling some of the toughest problems of society that the private sector, the government and the social sector have not been able to address. Tackling these problems requires **innovative business models** and **operating in difficult environments**.

Typically, an effective business model will require innovation in multiple areas. One good example is Husk Power Systems (HPS), which provides off-grid energy in rural Bihar, India. Its core innovation is a pioneering technology that transforms rice husk into gas, which is then used to generate electricity. In addition to this core technological innovation, HPS had to create a distribution system (which it does using low-cost bamboo poles), develop a low-cost metering and theft protection system (the company says it has the world’s lowest cost smart meters), and create a simple tariff structure and corresponding billing and collection system, as its customers were not familiar with buying electricity. In addition, as it was difficult to source gas-powered generators, the company developed the capability to convert diesel-powered generators! Finally, because HPS had difficulty sourcing skilled staff in rural Bihar, it started “Husk University” to train the workers it needed.

¹ O’Donohoe, N., Leijonhufvud, C., Saltuk, Y., Bugg-Levine, A. and Brandenburg, M. (2010) *Impact Investments, An Emerging Asset Class*, J. P. Morgan Global Research, Rockefeller Foundation and GIIN.

² Kubzansky, M., Cooper, A. and Barbary, V. (2011) *Promise and Progress – Market-based solutions to Poverty in Africa*. Monitor Group.

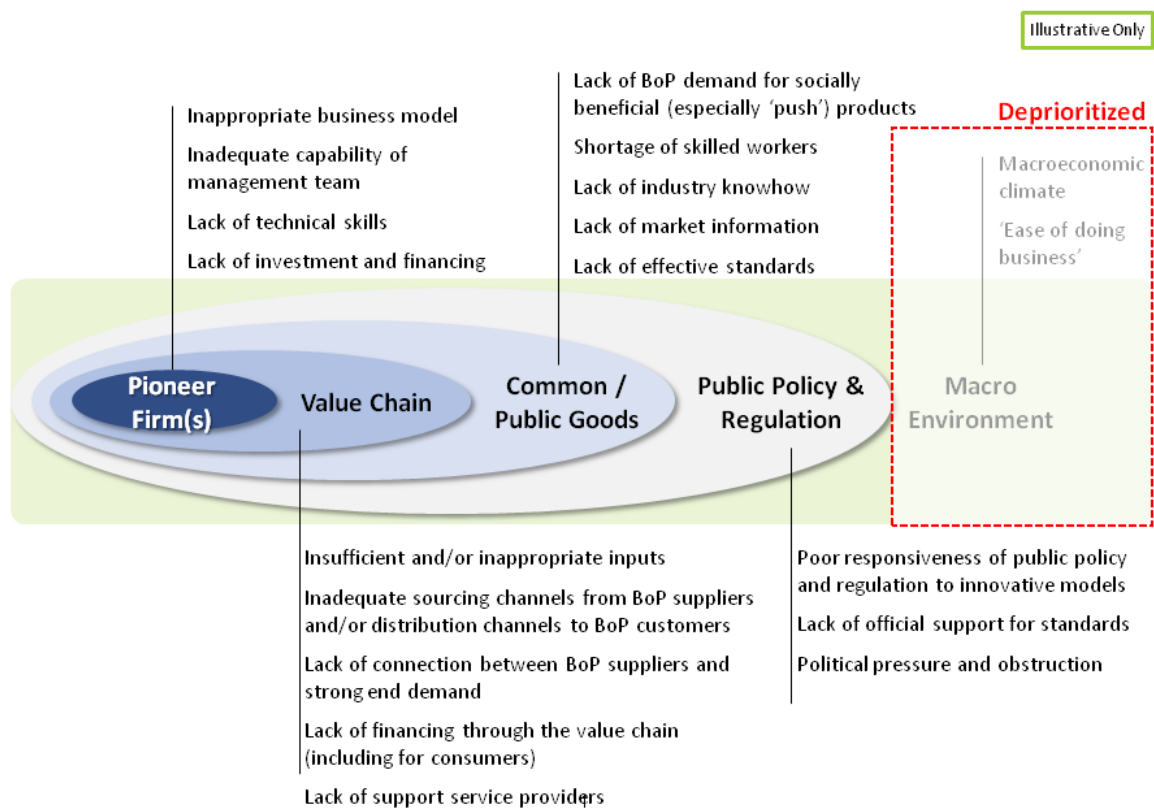
³ Karamchandani, A., Kubzansky, M. and Lalwani, N. (2011). *Is the Bottom Of the Pyramid Really for You?* Harvard Business Review

It is difficult to identify all elements of a solution upfront. The core innovation may be created and tested, along with a detailed business plan—what the customer will get, how it will be delivered and the economics of the venture—in other words, a “blueprint” of the business. However, the real work begins when one starts “validating” the business model on the ground. Issues that one has not previously thought of crop up, plans have to be modified and new elements developed. Often, one has to rework the entire business model.

The development and validation of the business model requires creativity and business acumen, not to mention significant financial resources, time and persistence. At the end of the day, the model may or may not work and, even if it does work, financial returns may be limited (as margins tend to be low and, once a model is proven, copycats emerge).

The challenge is not just limited to the business model. As mentioned earlier, these market-based solutions have to work in difficult environments.

“Eco-system” barriers to scale



Our experience with over 1000 ventures in this space has helped us understand the layers of challenges that one of these ventures must deal with, beyond the business model. In addition to the challenges faced by most new ventures, such as getting finance and building a team, these ventures also have to assemble the value chain to deliver their solutions (e.g., create distribution and arrange for financing for the value chain, including for customers), work on what are typically considered

public goods (e.g., educate the customer on the value of the product, especially for “push products” like insurance and clean drinking water) and address regulatory issues and policy.

While these challenges are significant, the potential upside is huge, as can be seen from micro-credit and contract farming, two models that have scaled. There are a number of stakeholders committed to seeing the field of market-based solutions succeed, and the key is to (i) have reasonable expectations and (ii) provide the nurturing environment that will allow more market-based solutions to scale and leverage them for developmental impact⁴.

RECOMMENDATIONS AND NEXT STEPS

First of all, we need to have **realistic expectations** around both the applicability of these solutions and the effort it will take to get them to scale. Market-based solutions are not a panacea. While there are many areas where these solutions can be effective, there are others where commercially viable models do not exist and, therefore, services need to be provided by government or by philanthropy. Even for market-based solutions that have the potential to create social impact at scale, getting these solutions both to work and to scale takes significant time, resources and effort, and many innovative efforts will fail. Also, financial returns are likely to be modest, especially for pioneer enterprises. These barriers need to be recognized by all stakeholders, including the impact investing community, many of whom feel they can get market returns from such ventures.

Second, **business models matter**, and we need to focus on getting them right. As mentioned earlier, these are tough problems for which traditional solutions are not working and creative new solutions are needed. These solutions usually involve multiple innovations and are not easy to develop. Even where a great idea exists, it is unlikely to work at first go. Instead, it requires significant on-the-ground validation and refinement, which in turn require resources, time and persistence.

Third, **we need to attract more of the right people and players into this space**. Our experience has been that the majority of the entrepreneurs in this field are people with great ideas and passion, but who lack experience in business or in scaling organizations. We believe that future success hinges on being able to attract more *business builders*—professionals who have experience in building scaled businesses—into this field. It would also be good to attract more corporations into this space, as they already have many of the capabilities and resources required to develop and scale market-based solutions. It will be important, though, given that financial returns may be modest or take time, that corporations take a wider, longer-term perspective as they design, test and implement such initiatives.

Fourth, **we should build conducive ecosystems** to accelerate models toward scale. As mentioned earlier, there are numerous *ecosystem* barriers to be addressed, even if one gets the business model right, because one is working in difficult environments. These barriers can range from assembling value chains to creating public goods to addressing regulatory issues and policy. Many impact investors and companies are unwilling or unable to even consider addressing these barriers (particularly in regulation and policy) and, yet, for the majority of market-based solutions, resolving these barriers is key to success. Policy and regulation is typically geared toward existing markets,

⁴ There is often an assumption that, because such market-based solutions have the potential to create social impact, they will create the impact. It would be useful to monitor the impact and find ways to ensure the impact is created.

models and players, and may unwittingly strangle new innovations before they have the opportunity to have impact at scale. Policymakers need to recognize this challenge and adapt policies to allow innovative market-based solutions to succeed and scale. Also, as new innovations come to market and scale, there is often a need to redefine or create standards and mechanisms for appropriate regulation.

Fifth, **“soft capital” from philanthropies, aid donors and governments is critical to the development of market-based solutions**, from nurturing pioneer enterprises to addressing ecosystem barriers. Developing and validating effective business models requires significant financial resources, time and persistence. As our team highlighted in a recent⁵ report, given the high level of risk and the modest rates of return even when pioneering ventures succeed, there is a need for funding and support that is interested in developmental impact and willing to accept low or even negative financial returns. Meanwhile, ecosystem building can create powerful externalities that could help many firms operate and scale successfully, but whose value is difficult for any one investor or firm to capture and monetize. We believe that philanthropies, donors and governments need to step into these gaps to provide much-needed support.

Last, but not least, we need to **get better at blending and coordinating a range of different types of capital and different interventions from players across the private and public sectors**, recognizing the complex, multi-faceted nature of the challenge of scaling market-based solutions. The evidence suggests that market-based solutions can be helped in reaching scale by having dedicated *market facilitators* who can work with different actors to bring these otherwise disparate elements together and guide the development of new, inclusive markets over time. We are now conducting further research into this and hope to have findings to share in early 2014.

Acknowledgements: The points laid out in this brief have been developed over the past seven years through the work of the Monitor Inclusive Markets team. In specific, we'd like to acknowledge the thought leadership of Mike Kubzansky, now with Omidyar Networks, who co-started Monitor Inclusive Markets and led its work in Africa.

⁵ Harvey K., Karamchandani, A., and Katz, R. (2012) *From Blueprint to Scale – The case for Philanthropy and Impact Investing*. Monitor Inclusive Markets and Acumen