Innovation for the Base of the Pyramid: a categorization of inclusive business innovations in Latin America

Abstract

Based on an inductive case study qualitative research approach, this study makes a contribution to management literature by developing theory for the understanding of inclusive business models at the base of the pyramid. The task is approached by the concurrent comparison of the theory and the data obtained from multiple case sampling. Available literature on innovation processes identifiable in BoP markets was reviewed and compared against the experiences illustrated in 30 inclusive business case studies from Latin America that had been previously documented by recognized international organizations active in the region. The research results allow proposing the first and second generation innovation strategies as two identifiable categories of innovation that have demarcated business development in the BoP.

Key words: Innovation, Inclusive business, Base of the pyramid

1. Introduction

Since the inception of the Base of The Pyramid [BoP] concept in 2002, business initiatives within the BoP have been focused on addressing the needs and opportunities in the markets constituted by the group of people whose daily income lies below USD$ 8 (PPP) and who often face serious difficulties for covering their most basic needs (Hammond et al., 2007). Currently, the aggregate of this population represents a number close to two-thirds of humanity (i.e. 4 billion). Thus, creating innovative and sustainable business models that can concomitantly address these societal problems and deliver business profits, constitutes one of the major challenges faced today by contemporary enterprises. Given the relatively novel and unexplored character of this phenomenon in business-society relations, more research needs to be done to gain a clearer understanding of how business may best engage with the BoP.

Based on a qualitative multiple case study research approach, this study makes a contribution to management literature by developing theory for the understanding of inclusive business models at the BoP. The task is approached by first reviewing the available literature on innovation processes identifiable in BoP markets, and consecutively comparing it against the experiences illustrated in inclusive business case studies from Latin America that had been previously documented by recognized authors and organizations in the field. The research results allow proposing the first and second generation innovation strategies as two identifiable categories of innovation that have demarcated business development in the BoP.

After presenting a review of the literature on innovation in BoP markets, the article introduces the research methodology, and moves on to present the categorization of innovation strategies in the BoP in first generation and second generation strategies. The last section of the paper presents the main implications and conclusions.

2. Theoretical framework

From a business and management perspective, the study of the BoP has gained importance over the last decade, building upon the seminal works from professors CK Prahalad and Stuart Hart, whom gave birth to this dynamic and growing area of administrative research (see for example Prahalad & Hart, 2002; Prahalad & Hammond, 2002; Hart & Christensen, 2002). A thorough
review of the extant BoP literature allows for the identification of two main stages of conceptual evolution. At its inception, the BoP concept emerged from the core idea of an existing latent market to be exploited by business at the BoP, emphasizing its commercial potential and depicting low-income population solely from a consumer perspective. At a later stage the perspective of analysis was broadened, contemplating a wider set of roles for the participation of low-income population throughout the value chain. Thus, the possible engagement of the poor into business operations is not only framed by their consumption capacity, but also by their potential as employees, suppliers, distributors or business partners (Pineda-Escobar, 2013).

In this latter context the idea of inclusive business [IB] arises as a novel business model that, based on the logic of mutual benefit, aims at incorporating low-income communities into corporate value chains, with the dual objective of improving the quality of life for the population while simultaneously achieving business profit. IB therefore emerge as a way for corporations to evolve beyond philanthropy or classical corporate paternalism, turning towards a sustainable market-based approach to overcoming poverty.

Increasing evidence from BoP research has reflected upon the significant differences existing between traditional and more affluent top-of-the-pyramid markets on the one hand, and BoP markets on the other. In this sense, a fundamental mistake from firms trying to engage with BoP markets has found to be the intent to transfer their familiar –let alone successful- strategies and business models from top markets to be used at the BoP, without attention to major dissimilarities that call for innovative processes. London and Hart (2004) evaluated more than 20 case studies of firms trying to engage with the BoP and concluded that traditional and normally successful business strategies did not necessarily result in a successful outcome when transferred to BoP markets.

Therefore, scholars studying BoP market opportunities from the perspective of innovation, have retaken the concept of disruptive innovation, coined by Christensen (1997), and propose it as an essential feature of the entrepreneurial efforts aimed at the BoP. Disruptive innovation is claimed to provide companies with the necessary flexibility for handling emerging opportunities independently from their traditional organizational models and value systems, adapting to contexts where it will be necessary, for example, to compete against non-consumption (Hart and Christesen, 2002). Similarly, reverse innovation is recognized as having the potential to create disruptive innovations at the BOP with progressive scalability towards developed markets (Hang, Chen and Subramian, 2010).

Anderson and others have also argued that innovation at the BoP is not intended for securing new customers or developing new products and services. On the contrary, it should focus on responding to issues of acceptability –willingness to purchase-, affordability -capacity to purchase-, availability -possibility to purchase-; and awareness –consciousness about the product or service. What they call "The four A's framework for strategic innovation" (Anderson and Billou, 2007, Anderson and Markides, 2007). On a different line of thought, Bill Gates proposes an evolution in the interpretation of innovation in business activity, arguing the need to reach another level of innovation that goes beyond technological innovation and incorporates systemic innovation. In this way, capitalism will allow market forces to serve the public interest and help solve global inequities, what he labels as "creative capitalism" (Hemphill, 2010).

Such understanding of creative capitalism goes in line with the proposal developed by Simanis and Hart (2009) in their 'BOP Protocol', which is based on the embedded innovation paradigm. Embedded innovation, they argue, responds to the challenge of innovation in business models, enabling the co-creation of business between the community and companies through the development, by the latter, of native-capabilities that are sensitive to the local culture and context and are based on building trust and social capital. All these are found to be essential characteristics that frame the innovation processes of any company seeking to operate

3. Research method

Following Yin (2009) and Eisenhardt (1989), this study applied an inductive case study qualitative research approach, as a suitable methodology for developing theory. The research was designed based on an in-depth analysis of multiple cases from Latin-American companies with documented inclusive business experiences, and was grounded on the concurrent comparison of the theory and the data obtained. This type of methodology has been recognized to be of particular use in the early stages of research on relatively new and unexplored fields (Brown and Eisendhardt, 1997); which corresponds to the purpose of the study presented herein. In addition, theory building from case studies is becoming increasingly relevant as a research strategy that can provide a proper link from "qualitative evidence to mainstream deductive research" (Eisenhardt and Graebner, 2007).

As depicted on Table No. 1, a total of 30 inclusive business cases from Latin America were analysed, allowing for the production of contrasting and comparable results. Secondary sources were used for data collection, building mainly from the information gained through case study reports previously published by renowned international organizations working in the field of inclusive business in the region. Analysed reports came from CECODES and SNV (2008), SNV and WBCSD (2008), SNV and WBCSD (2010), UNDP (2010); and the IFC (2012). Complementary information was also sourced from company websites, public reports, specialized media articles and companies’ presentations given at the II BASE Forum organized by IDB in June 2013.

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<thead>
<tr>
<th>Country</th>
<th>Inclusive business case(s)</th>
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Source: Own construction

4. Results and findings

By comparing the literature on BoP innovation with the processes illustrated in the case studies explored, the following categorization of inclusive business innovations in Latin America, as summarized on Table No. 2 and elaborated in detail in the following sections, is proposed: i) first generation innovation strategies, corresponding to the initial stages of innovation for the BoP; and ii) second generation innovation strategies, with more relevance for an effective implementation of inclusive business with the BoP.
Table No. 2: categorization of BoP innovation strategies

<table>
<thead>
<tr>
<th>First generation innovation</th>
<th>Second generation innovation</th>
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<td>- Focused on consumer potential of the BoP</td>
<td>- Pluralistic conception of BoP potential</td>
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<tr>
<td>- Adaptation of existing products to BoP markets</td>
<td>- Co-creation of new business models</td>
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<tr>
<td>- Focused on traditional management styles</td>
<td>- Flexibility and local sensitivity</td>
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<tr>
<td>- Exogenous and imposed on the local context</td>
<td>- Native capabilities</td>
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<tr>
<td>- Market access vision above inclusive market</td>
<td>- “embedded innovation” (Simanis &amp; Hart, 2009)</td>
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Source: Own construction

4.1. First generation innovation strategies

Initial innovation strategies aimed at BoP markets show a particular interest in the consumer potential of the population living in poverty, quite possibly encouraged by the early understanding of the concept of the BoP which, as discussed in the theoretical framework, was born from a vision limited to a commercial interpretation of the poor as quiescent consumers.

Consequently, it was possible to identify amongst Latin American companies a tendency towards the adaptation of existing products, to make them marketable in the BoP markets. Such adaptation can occur through innovations involving technological simplifications, changes in the presentation of the products (eg sachets) or in its functionality, with the dual objective to achieve, on the one hand, a reduction in costs that suits the unpredictability and irregularity of income flows typical of BoP population and, on the other, particular product characteristics that may meet these unfamiliar contexts.

By focusing attention on specific innovations at the level of products and services offered to the BoP, first generation innovation strategies disregard the relevance of system innovations for implementing inclusive business. In this way, companies tend to start operating in poverty contexts by implementing business systems and methodologies that are alien to the local context; with the risk of failure that such lack of adaptation entails (Hart and London, 2005).

An example of the implementation of first generation innovation strategies is seen in the case of Bancolombia, an important banking institution in Colombia. Although it is true that financial inclusion is a key component for improving quality of life for the poor, Bancolombia is failing to evolve in its BoP strategy, and is mainly focusing on expanding market access by creating new banking channels that can reach vulnerable population. By opening new banking channels in remote rural and urban areas in the country, Bancolombia is implementing incremental innovation in its service offer, expanding its customer base.

4.2. Second generation innovation strategies

Second generation innovation strategies occur when companies adopt a holistic interpretation of the BoP potential, recognizing the feasibility of engaging the poor all along their value chain, with a view to establishing a mutually beneficial company-community relationship. Thus it corresponds with an understanding of innovation in line with what Simanis and Hart (2009) refer to as embedded innovation, allowing communities and businesses to build together a new shared identity based on proximity and mutual commitment, becoming a source of value creation.

Second generation innovation strategies are based, therefore, on great flexibility and local sensitivity that allows for the co-creation of new business models, grounded in deep dialogue and joint action. Second generation innovation requires that the company is open to new ways of
learning, with acceptance of exploration and experimentation processes and without reluctance to uncertainty and risk.

The implementation of second generation innovation strategies is best illustrated in the case of the Colombian company Promigas with its inclusive business model called 'Brilla'. Brilla corresponds to an inclusive business model that departs from the traditional lines of business operation of the company, which is dedicated to the distribution of residential natural gas in Colombian Atlantic coast. While Promigas has been offering access to natural gas service for the BoP families through a funding mechanism specifically designed for that market, its inclusive business model goes beyond ensuring affordability of their service, surpassing first generation strategies. Thus, having sufficient organizational flexibility to design and implement context-sensitive business schemes with the BoP, Brilla emerges as a microcredit solution that offers financing to BoP families against monthly payments that are allocated together with their gas bill. A key feature of Brilla program is its recognition of the importance of local understanding for BoP success, which meant embarking on a preliminary process of dialogue with the community with the purpose of understanding their particular needs and interests. As a result, Brilla is tailored to facilitate access to those goods that are actually mostly needed by the population in order to improve their quality of life (SNV-CECODES, 2008:62-69; SNV and WBCSD, 2010:86-91; IFC, 2012).

5. Implications and conclusion

The comparative analysis of the literature on innovation in BoP business models against the failures and successes found in the inclusive business cases from Latin America, make it possible to identify key innovating strategies that have shaped business development in the BoP in the region. The analysis of research findings allows for the proposition of the categorization into first and second generation innovation strategies.

Second generation innovation strategies, being based on the embedded innovation paradigm, and recognizing the potential of BoP population to perform a variety of roles along the value chain; exhibit greater relevance for BoP markets. Second generation strategies appear therefore to be more desirable for an effective implementation of inclusive business with the poor, allowing to find synergies between business performance and social development.

The analysis presented herein is not intended to be exhaustive, nor to provide a unique model for the interpretation of innovation in inclusive business with the BoP. On the contrary, it seeks to make an initial contribution to the limited literature on the subject, providing a basis to spur the development of future research on the same line.

List of references


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1 Due to space limitations, a description of each case and its main features can not be included, but may be available from the author upon request.