BUSINESS STRATEGIES AT THE BOTTOM OF THE PYRAMID (BOP):
AN EXAMINATION OF MEXICO’S BOP AND INSIGHTS FROM SOME
OF THE INCLUSIVE STRATEGIES EMPLOYED THERE

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by
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ABSTRACT OF THE THESIS

Business Strategies at the Bottom of the Pyramid (BOP): An Examination of Mexico’s BOP and Insights from Some of the Inclusive Strategies Employed There

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This thesis examines the claims that there is market potential in poverty stricken BOPs and that inclusive business strategies provide the best chances for initial access and long-term success. The claims are examined using Mexico’s BOP the subject of the larger study. In this context, two main questions are addressed: Does Mexico’s BOP have market potential in terms of size, current spending, needs, and capabilities, and, if so, what consumer and environmental characteristics might be relevant to strategy formulation? Are inclusive strategies effective in Mexico’s BOP, if so, which elements, or combination of elements, of these inclusive strategies appear to be proving the most effective at helping the firm to reach its goals?

I compiled the research for this thesis using three main sources: an extensive review of the BOP and strategy literature, an analysis of informal sector data compiled by The Mexican National Statistics Institute (INEGI), and interviews conducted as part of a series of case studies on three firms targeting Mexico’s BOP consumers with some form of an inclusive strategy. The firms hailed from the industries of microinsurance, point-of-use water systems, and homebuilding. The review of literature suggests BOP environments demand strategies capable of achieving high volume, attending to diverse local demands, and functioning efficiently in a context where gaps in infrastructure, education, and market efficiencies are the norm. Characteristics of successful BOP ventures emerging in the literature are the use of co-creation, capacity building, and non-traditional partners (such as non-profit organizations and NGOs), and the overall ability to become “socially embedded” in the BOP.

The findings of my study revealed approximately half of Mexico’s 111 million people living at the BOP. This group comprises some 15 million households whose collective expenditures amounted to US $14 million in the quarter examined. I found that while extreme diversity demands localized solutions from firms in Mexico, the major challenges reported are common to many other BOPs as well. Additionally, I found that to incorporate the flexibility needed to address variety of local demands and the standardization necessary for replicating into numerous BOP communities, firms created platform solutions. Within these platform strategies, firms are incorporating elements similar to those found in the literature. By doing so, they have created sustainable business models and significant advantages toward addressing challenges, gaining consumer trust, creating new networks and channels, and developing more capable consumers. Overall, my findings support and at times
supplement the claims and findings in the literature regarding the existence of BOP market potential and the effectiveness of inclusive strategies. For example, although my findings showed that using non-traditional partners provided many benefits to firms, they also revealed that an over-reliance on these partners left firms out of touch with consumers.
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<td>ADA</td>
<td>Adobe Home Aid</td>
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<td>AGEB</td>
<td>Basic Geostatistical Areas</td>
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<td>BOP</td>
<td>Bottom of the Pyramid</td>
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<tr>
<td>CIA</td>
<td>Central Intelligence Agency</td>
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<tr>
<td>CONAPO</td>
<td>Consejo Nacional de Población (National Population Council)</td>
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<td>CONAVI</td>
<td>Comisión Nacional de Vivienda (National Housing Commission)</td>
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<td>CONEVAL</td>
<td>Consejo Nacional de Evaluación de la Política de Desarrollo Social (The National Council for Evaluation of Social Development Policy)</td>
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<td>CSR</td>
<td>Corporate Social Responsibility</td>
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<td>EMs</td>
<td>emerging markets</td>
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<td>ENIGH</td>
<td>La Encuesta Nacional De Ingresos y Gastos de los Hogares (the National Survey of Household Income and Expenditures)</td>
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<td>FDI</td>
<td>foreign direct investment</td>
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<td>GDP</td>
<td>gross domestic product</td>
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<tr>
<td>GNI</td>
<td>gross national income</td>
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<td>IB</td>
<td>international business</td>
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<td>IBLF</td>
<td>(The Prince of Wales) International Business Leader’s Forum</td>
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<td>IDB</td>
<td>Inter-American Development Bank</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>International Labour Organization</td>
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<td>Instituto Nacional de Estadística y Geografía (The National Statistics Institute)</td>
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<td>multinational corporation/ multinational enterprise (used interchangeably)</td>
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<td>The Water Initiative</td>
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<td>United Nations</td>
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<td>WHO</td>
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<td>WOCCU</td>
<td>World Council of Credit Unions</td>
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CHAPTER 1

INTRODUCTION

With established markets becoming saturated, multinational corporations (MNCs) have turned increasingly toward emerging markets (EMs) in the developing world especially as world markets have begun to open up to foreign investment. Now with globalization, innovations in technology and information and worldwide wealth are on the rise. On the surface this would appear to translate into vast new growth horizons for MNCs with the resources and persistence to enter and compete. Yet experience has shown that the lure of millions of additional “middle class” consumers who could afford and were clamoring for the products of multinationals was vastly oversold (Ricart, Enright, Ghemawat, Hart & Khanna, 2004). The reality is that the true nature of the vast majority of people living in developing countries is only beginning to be understood. The size of these markets is huge, as expected, but the potential consumers lie not in the ready numbers of the middle-class but rather within the figures representing the low-income populations (Collier, 2007; De Soto, 2000; Hammond & Prahalad, 2004). According to Mahajan and Banga (2006) and Prahalad (2006), these low-income markets, also referred to as the Bottom of the Pyramid (BOP), comprise nearly two-thirds of the world’s population and consist of people who live on individual incomes of less than US $1,500 per year or on household incomes of less than US $6,000 per year (Hammond & Prahalad, 2004), and collectively represent a market potential of approximately US $13 trillion.

Thus far most EM strategies by MNCs have targeted almost exclusively at the wealthy elite at the top of the pyramid [TOP] (London & Hart, 2004; Prahalad, 2006; World Business Council for Sustainable Development [WBCSD], 2004). Further, even the majority of national companies in EMs have traditionally focused their businesses on reaching the middle and upper classes (Prahalad, 2006). Recently however, a number of MNCs as well as large national companies, and international and local new ventures have launched new initiatives that are exploring the untapped market potential at the BOP (Preston, Libow, Bruno, Meade & Wells, 2007; Sharma, Mohan & Singh, 2003;
WBCSD, 2005). However, reaching these masses of people poses both tremendous opportunities and unique challenges (London & Hart, 2004; Prahalad, 2006; United Nations Human Settlements Programme [UN-HABITAT], 2008) and how companies can successfully enter these low-income markets has not been effectively addressed in the literatures on global and EM strategies.

Recently, a new group of international business (IB) researchers, hereafter referred to as BOP researchers, (i.e. Hammond & Prahalad, 2004; London & Hart, 2004; Prahalad, 2006) have begun trying to address these existing gaps in the strategy literature and have found that firms that attempt to use their traditional strategies and products, originally created in and for TOP market consumers and environments, by making minor modifications to them to better fit what they perceive as the needs and tastes of emerging-market customers have not succeeded in making products and services available to the mass markets (the BOP consumers) in the developing world. Though tailoring strategies in this way may be effective, in some scenarios, for reaching the smaller, more affluent markets in emerging economies, the people at the BOP, researchers are finding, have an entirely different and diverse set of needs, demands, capabilities, incomes, and environmental situations that require new mindsets and innovative, products and approaches. For example, BOP individuals are often found operating in their county’s informal sectors where formal rules and benefits may not apply, where social contracts replace formal ones, where infrastructure is fragmented or non-existent, where people live in shantytowns, slums, or hard to reach rural areas, where traditional value chain partners do not exist and numerous small and micro businesses dominate, and where incomes are low and unpredictable and consumer sophistication is low. Given that traditional strategies were designed assuming certain market and institutional efficiencies, it should come as little surprise that when placed in environments where such efficiencies do not exist, such strategies might become irrelevant.

In place of traditional strategies, BOP researchers suggest that a company’s ability to create small-scale “inclusive strategies” that incorporate the development of the poor directly into the business model, facilitate intimate market learning, and result in the creation of goods and services designed especially for the unique needs, demands, and environmental conditions of low-income sectors will ultimately given firms not only the most effective mode of entry but also the best chance of creating scalable business models capable of
addressing a variety of local demands and issues that are present from community to community, solidifying relationships, and obtaining intimate market insights crucial for developing the competitive and long-term advantages needed in such environments (Hammond & Prahalad, 2004; Hart, 2005; London & Hart, 2004; Prahalad, 2006; Simanis & Hart, 2009; WBCSD, 2005). Furthermore, researchers like Prahalad (2006), Viswanathan (2007), and Hart and Milstein (1999) assert that the unique environments and needs of BOPs together with the advances in today’s technology combine to offer firms a unique opportunity to design innovations that boast high functionality and efficiency at an affordable price that greatly benefits the BOP consumer and may ultimately transfer to TOPs as superior products. In other words, if firms learn to view the BOP needs and environments as an ideal test bed for new innovations instead of hazardous annoyances, there could be many exciting opportunities ahead.

Different from strategies some companies are employing under the social responsibility mantra, BOP advocates insist that true inclusive BOP strategies or business models, should go beyond the unsustainable philanthropic or token image enhancing Corporate Social Responsibility (CSR) efforts to create self-sustaining profitable businesses where both the company and the poor profit over the long term (Prahalad, 2006; Preston et al. 2007; Simanis & Hart, 2009). However, given the relatively new focus on BOP markets, currently exists very little in the literature on what elements and approaches combine to create the most effective inclusive strategies. As such, firms are largely involved with various trial and error experiments that range from arm’s length approaches to working with the poor to business models that intimately link the social development of the poor with the overall business and financial goals. Furthermore, most of the current BOP strategy literature has been broad based, addressing BOPs and strategies there as a whole.

Given that every country has its own unique variables, as well as characteristics common to BOPs worldwide that may influence strategy formulation, and the claims that the truly inclusive strategies offer the greatest long term advantages to both firms and BOP consumers, this thesis seeks to add to the current BOP literature first, by supplementing the broader BOP literature with an analysis of Mexico—whose country shares many similar characteristics with other Latin American countries—and it’s BOP market potential (in terms of numbers of households and their current income and expenditures, and the needs and
opportunities represented there) and characteristics; and second, with industry and strategy insights and comparisons from firms that are currently using some form of an inclusive strategy to do business in Mexico’s BOP.

The basic purpose of the study is to assess Mexico’s BOP for market potential, to determine any opportunities, challenges, capabilities, and limitations, and to gain insights into the effectiveness of inclusive strategies currently being employed there. At the same time, the thesis seeks to determine which elements, or combination of elements, of these inclusive strategies appear to be proving the most effective at helping the firm to reach its goals, and to uncover any emerging trends that are resulting from firm experiences in Mexico’s BOP. To accomplish this, the thesis addresses the following questions: Does Mexico’s BOP have market potential? If so, what are the BOP consumer and environmental characteristics there? Additionally, what types of strategies are most effective there? Several related questions ensue from these larger ones and are posed to and addressed by firms interviewed for this thesis: What BOP need does the firm address? What are the major challenges, as perceived by the company, to successful market entry and long-term success in regards to accessing and engaging potential BOP consumers? How are products and business models designed to exploit the opportunities identified and to successfully address the challenges at hand? What are the major advantages and disadvantages of, or limitations to, the company’s specific business model or mode of entry? What insights have come from the company’s experiences in and with the BOP?

The findings of this thesis contribute to a broader effort to understand the unique challenges, opportunities, capabilities and limitations existent in BOPs; how strategies can be formulated to enable firms to enter and compete in these markets successfully; and what strategies provide the most advantages to firms in a variety of local markets. Specifically, the thesis builds on findings by the London and Hart’s (2004) exploratory study highlighting specific factors that appeared to be contributing to successful BOP strategies, and adds to the BOP research effort as a whole with specific insights into Latin America’s second largest BOP market and into the inclusive strategies being formulated and employed there. The following sections will discuss in detail the basic plan and methodology of this thesis.

The thesis consists of six chapters with chapters. Chapter 1 introduces the thesis, details the plan of the thesis. Chapter 2 then begins the thesis’ review of literature by
providing a background on the BOP that includes a discussion of some of the distinctive characteristics of low-income sectors and consumers in developing countries and the basic theory of BOP markets. To address the thesis question regarding Mexico’s BOP potential and overall characteristics, Chapter 3 then uses aggregate statistical data compiled by The Mexican National Statistics Institute (Instituto Nacional de Estadística y Geografía [INEGI]) on the country’s informal sector; subsequent uses of the data resulting from INEGI surveys and INEGI’s most recent 2005 National Census by Mexico’s National Council of the Evaluation of Social Development (Consejo Nacional de Evaluación de La Política de Desarrollo Social [CONEVAL]) and the National Population Council (Consejo Nacional de Población [CONAPO]) in the form of Marginalization Indexes; and data gathered through INEGI’s 2008 National Survey of Household Income and Expenditures (La Encuesta Nacional De Ingresos y Gastos de los Hogares [ENIGH]) providing information about the level and structure of income and expenditure in Mexican households.

The original criteria used for determining low-income groups was based on Hammond and Prahalad’s (2004) classification and included those households that make less than US $6,000 per year, or in Mexico up to six times the minimum wage (6MW). However, throughout the research process, it became clear that Mexico’s low-income sector incorporates households whose incomes exceed the 6MW, potentially representing an even wider market than originally anticipated.

In regards to data compiled on the informal sector, it is important to clarify that Mexico uses the informal sector definition recommended by the fifteenth International Conference of Labour Statisticians, which is also the definition adopted by the International Labour Organization (ILO), and has prepared its national statistical accounting system to assume the modifications demanded by the 1993 SNA revision (Negrete, 2006). As a result, the terms Informal Sector and Shadow or Underground Economy are no longer synonymous within the system. According to Negrete (2006), the INEGI data for the informal sector is gathered using a mixed-household surveys strategy that combines micro-business, national urban employment and national employment (including both rural and urban samples) surveys that go from the household to the unit production and are designed to explore the sector’s double socio-demographic and economic dimension. In addition, the Marginalization Index put out by CONEVAL presents data for socioeconomic indicators on a state, municipal
and local level and CONEVAL supplements its Marginalization Index with maps that provide a visual understanding of the distribution of income-measured poverty throughout Mexico in terms of “food poverty,” “capability poverty,” and “asset poverty.” The marginalization index put out by CONAPO contains data on indicators similar to those found in CONEVAL’s marginalization index but are specific to Mexico’s urban Basic Geostatistical Areas (AGEB) and measure the ability or inability of a person to participate in or to enjoy the benefits and essential services for the development of basic capabilities. These urban areas are further measured in terms of the regions they belong to and their city size in terms of population.

Together, with indexes and information compiled by international organizations like the Heritage Foundation (Index of Economic Freedom), The World Bank (Ease of Doing Business and Country Profiles), Transparency International (Corruptions index), and the CIA (World Factbook), the INEGI data are analyzed to assess Mexico’s overall BOP potential and characteristics. By gaining a better picture and understanding of Mexico’s BOP situation, the thesis seeks to identify important characteristics of Mexico’s low-income sectors regarding both the environments and the people themselves that would help to inform business strategy formulation for firms considering doing business here.

Next, Chapter 4 examines the existing literature on emerging market and global business strategy and the recent research, findings, and proposals of BOP researchers in order to determine the availability of strategy literature appropriate for informing the development of strategies and models for BOP markets. In Chapter 4, it is revealed that recent research at the BOP suggests that companies that develop true understandings the BOP environments they enter and create more bottom-up, context-appropriate, inclusive models may be better positioned to deal with the challenges that have doomed other companies and to benefit from a new kind of competitive advantage. Chapter 5 discusses the methodology used during the research process for Chapter 6. To investigate these assertions and to gain insights into how models are being designed to incorporate these aspects and to what degree, as well as into the unique opportunities, challenges, capabilities and limitations that lie within Mexico’s BOPs, Chapter 6 uses semi-structured, open-ended interviews as part of a series the three case studies then developed within the chapter. The three companies represent three different industries and have each developed products and business models designed specifically for
Mexico’s BOP using some form of an inclusive approach. This chapter also incorporates the results and discussion part of the thesis. Finally, Chapter 7 concludes the entire thesis effort with a summary of the thesis’ limitations, conclusions, and final recommendations.
In the 1980s, as the Cold War came to an end, China, India, the former Soviet Union and its allies, and Latin America began to open to foreign investment. As governments began to implement, at various speeds, policies aimed at privatization and market liberalization, Prahalad and Lieberthal (1998) suggested that, in answer to their quests for new markets, MNCs should consider overcoming their imperialistic mindsets and see these highly populated, less developed countries not just for their cheap labor and resources but also for their market potential, which they claimed was represented by the large numbers of aspiring middle-classes and high income consumers who could afford and were clamoring for MNC products and services. As firms began to accept the challenge, the terminology began to shift from “developing countries” to “emerging markets” and academics began to excite firms with assurances that first movers could gain significant advantages that would open up a world of opportunities for market growth (Arnold & Quelch, 1998). However, although some firms found success in the TOP or upper income sector markets, many others met with significant setbacks. Early movers quickly found that not only were the markets in EMs structured very differently than those of more developed nations but the claims of millions of additional middle-class consumers had been vastly oversold (Seelos & Mair, 2007). The reality is that the true nature of the vast majority of people living in developing countries is only beginning to be understood.

This chapter provides some insights into EMs by discussing the nature and characteristics of their true majority markets--the BOPs. Further it will discuss the major claims regarding the potential in these low-income areas, and provide insights into the true character of the BOP and the people found there, and into the reasons most firms have traditionally avoided doing business there.
THE TRUE STATE OF THE WORLD, THE BOP, AND THE NEW MARKET HYPE

The size of these markets is huge, as expected, but the potential consumers appear to lie not in the ready numbers of the middle class but rather within the figures representing the low-income populations. For example, according to Hammond and Prahalad (2004), studies show that in poor countries, the distribution of households by income level is heavily skewed toward the bottom rungs of the economy. Reassessing the situation and seeing a different kind of potential, Prahalad and Hart (2002), redefined the target (or majority) groups in emerging market countries as low-income or BOP sector individuals with incomes of less than US $1,500 per year or annual household incomes of less than US $6,000 per year as noted by Hammond and Prahalad (2004).

Explaining the economic pyramid concept, Prahalad (2006) breaks down the income groups of the world using a pyramid diagram. Divided into four sections, he illustrates how, through a very small triangle at the top of the pyramid, those who make greater than US $20 thousand per year comprise a tiny percentage of the global population while the majority of the world’s population, some four billion people, make up the very large base (or bottom) of the pyramid and are found in the lowest income categories. According to Prahalad (2006) and Mahajan and Banga (2006) the BOP represents approximately two-thirds of the world’s population, with an estimated market potential of US $13 trillion (Prahalad, 2006).

THE BOP: BEYOND INCOME MEASURES

Traditionally, international organizations and more recently BOP researchers have measured the poor in terms of income levels and poverty in terms of material deprivation, or not having enough income to cover the basic needs of food, shelter and clothing (Karnani, 2007; Prahalad, 2006; Whitney & Kelkar, 2004). For instance, The World Bank (2000) discusses poverty as being either relative or absolute where relative poverty is defined as “a lack of the resources required to participate in activities and to enjoy living standards that are customary or widely accepted in the society in which poverty is measured” (p.23), while absolute poverty encompasses a more desperate situation and is defined as a lack of resources, such as food, clothing, or access to medications, needed to ensure physical
well-being and survival, is not country-specific, and is typically measured in terms of international poverty lines, such as the US $1 per day extreme poverty line or the US $2 per day poverty line.

However, the economic development literature suggests that poverty and well-being are actually multi-dimensional constructs for which measures of income alone miss out on important social dimensions of poverty and well-being such as education and health, and thus give incomplete and not altogether accurate scenarios of the needs, capabilities or limitations of the people being measured. For instance, a measure based on income alone would not differentiate between a person with access to free State-provided healthcare and education and a person on the same income who does not have access to these services, though clearly the person without these services would be worse off overall. According to Rufin (2009) there are at least five important and strongly interrelated dimensions to poverty that cannot be fully analyzed separately. These five categories are material deprivation, lack of education, ill health and lack of access to health services and medication, vulnerability (or high exposure to risk), and voicelessness (or a lack of influence on decisions in one’s life) and considers them to be strongly interrelated where one leads to or reinforces another (Rufin, 2009).

The reality is that how people experience poverty is determined by a variety of factors that often vary from region to region and even household to household as there are wide divergences in how equitably or inequitably income, physical assets, financial credit, social services and job opportunities are distributed. For instance, Rogaly, Castillo, and Romano Serrano (2004) found that in addition to income, households had many different kinds of assets and dynamic interactions among assets, including their own skills, which contributed to wealth disparities among households of the same income categories. In their work, Rogaly et al. (2004) divided households into four categories: secure households, regular households, insecure households, and most vulnerable households to show how present income flows and asset bases could either enable households the ability to benefit from micro-loans or put them at risk for falling into a debt they could not recover from. The authors found that the most secure households were those most likely to have wealth (in the form of physical assets, and/or human capital/assets such as education, self-esteem and good physical health) that allowed them to better access loans, use them productively, and even make loans to others,
placing them in a much better positioned to protect themselves from sudden shocks and the more predictable dips in income (Rogaly et al., 2004).

Currently there is no one internationally accepted standard for measuring the socioeconomic factors that play into a person’s well-being and the quantity and quality of information on the subject varies from country to country. However, there are a number of composite indexes that offer powerful alternatives to income as a summary of well-being. Though they are not without their limitations, they can provide useful entry points to an awareness understanding of the wide range of forces that influence human well-being. For instance, the United Nations Development Programme (2009) offers access to indexes such as the Human Development Index (HDI), The Human Poverty Index (HP-1 and HPI-2), the Gender Related Development Index (GDI) and the Gender Empowerment Measure (GEM). Additionally, individual countries may also have their own composite indexes that incorporate many of the same, and sometimes additional, indicators. Understanding the levels of poverty and the true state of the poor in various regions in regards to their efficiencies and deficiencies present in any given area can go a long way towards assisting firms in creating BOP strategies appropriate for the environments they are in, figuring out the best areas for initial investments, and deciding on initial target markets both in terms of geographical location and in terms of spending power, capabilities, and limitations.

**IS THERE REALLY A MARKET IN THE POVERTY STRICKEN AREAS OF THE BOP?**

Despite the presence of a handful of MNCs at the BOP, firms and IB scholars, most comfortable in the more familiar middle- and upper-income or TOP markets, remain skeptical as to whether or not any real market opportunities actually exist in the world’s poorest sectors (evidenced by the complete lack of attention to the region both in the literature and in the low number of MNCs attempting entry in the BOP). However, there are a small handful of IB scholars--the aforementioned BOP researchers--who maintain there is potential at the BOP and who are adamant and persistent in their efforts to provide firms with the convincing data they need. For instance, recently one of the first empirical studies was done on the BOP by Hammond, Kramer, Katz, Tran and Walker (2007) that resulted in aggregate data, derived from the surveys of 110 countries for which household survey data
were available, for four developing regions Africa, Asia, Eastern Europe and Latin America. In efforts to demonstrate the market potential at the BOP, Hammond et al. (2007) focused on analyzing market composition in terms of total annual income or expenditures by BOP income segments and household spending in terms of average annual household expenditures. Additionally, the authors break down the market composition by urban and rural locations and conclude that although the lowest BOP consumers’ incomes are low, there is still a sustainable amount of spending by these consumers and the huge numbers in these markets do add up to create a viable market.

**If There Is a Market at the BOP, Why Have Firms Traditionally Avoided It?**

An important fact to point out, as revealed by a recent study conducted by Preston et al. (2007) on firms operating in the BOPs of Latin America, is that there are firms, both national and international, that have been doing business at the BOP for decades and that view these markets as both important aspects of their growth strategies and as sources of stable income during times of economic instability. However, for those firms that have avoided BOPs, the justifications for why this has been the case has usually been in regards to the greater “psychic distance” they represent (Hitt, Dacin, Levitas, Arregle and Borza, 2000) and the belief that the poor resist new products, services and technologies and thus would not make good customers (Prahalad, 2006).

**Psychic Distance**

Although the general literature on the internationalization of the firm, including the works of Johanson and Vahlne (1977), Nordstrom and Vahlne (1994) and Vahlne and Wiedersheim-Paul (1977), has identified psychic distance a key explanatory factor in its theoretical framework (as cited in Evans & Mavondo, 2002), the definition of the term has changed considerably since its first use in Beckerman’s (1956) study on the distribution of international trade (as cited in Evans & Mavondo, 2002). For example, Vahlne and Wiedersheim-Paul (1973) defined psychic distance in terms of factors that prevent or disturb the flow of information between suppliers and customers (as cited in Evans & Mavondo, 2002), while Nordstrom and Vahlne (1994) redefined it as “factors preventing or disturbing firm’s learning about and understand a foreign environment” (as cited in Evans & Mavondo,
2002, p. 42), and O’Grady and Lane (1996) defined it as “...a firm’s degree of uncertainty about a foreign market resulting from cultural differences and other business difficulties that present barriers to learning about the market and operating there” (p. 330).

Considering these definitions, Evans and Mavondo (2002) proposed that while the continuous redefinition of psychic distance had resulted in a deeper understanding of the concept, the aforementioned definitions had all failed to address the two most important elements: psychic and distance. According to Evans and Mavondo, the psychic portion of the term indicates that it is not the simple presence of external environmental factors that determines the degree of psychic distance but rather the mind’s processing, in terms of perception, of cultural and business differences that formed the basis of the psychic distance. Further, in terms of the distance part of the term Evans and Mavondo (2002) asserted that although the idea of distance had sometimes been confused with uncertainty, or the lack of sureness about something, the term distance should, in fact, be understood as a separate notion entirely that refers to the similarity or difference in regard to the degree of separation between two points. A discussion of this concept of distance can be seen in detail in Lee’s (1998) definition of cultural distance that encompassed a marketer’s perception of socio-cultural distance in terms of language, business practices, legal and political systems. By way of a new definition, which the authors then went on to study and confirm in terms of its ability to explain a firm’s strategy effectiveness and financial performance in distant markets, Evans and Mavondo (2002) proposed that psychic distance was the distance between the home market and a foreign market, that results from the perception of both cultural and business differences where business differences include the legal and political environment, which were examined on the levels of interstate, state and local; the economic environment; market structure; differences in business practices, and barriers to learning and understanding such as language and communication differences.

Because the BOP sectors of most countries have been largely ignored by firms and because the poor have less to work with in terms of income, opportunities, infrastructure, and resources, the strategies for survival and doing business are often much different than those found in the more affluent TOP markets of both the developing and the developed countries of the world. In fact, these differences are so distinct that London and Hart (2004) and Schutte and Ciarlante (1998) suggested that the strategy literature should be expanded to
differentiate between groups within EMs beyond just those differences in the affluent sector as buyer behavior was likely to be markedly different between the wealthy elite and growing middle class consumers and the urban and rural poor BOP consumers there. Thus, while the distant TOP markets of developing nations each offer their own psychic distance challenges to firms, the even less well understood BOP markets can represent an even greater stretch for firms as the within country differences between the two markets can be immense. For instance, according to the UN-HABITAT (2008), the vast majority of those residing at the bottom of the economic pyramid live in rural villages and urban slums and shanty towns where educational levels are often low to non-existent and illiteracy tends to be high. This requires nontraditional marketing approaches. Further, BOP markets are hard to reach—from the point of view of distribution, credit, and communications; infrastructure in the developing world is often poor or nonexistent, creating the need for substantial upfront investment; tribal, racial, and religious tensions create security issues; rule of law is often weak; there is often rampant crime that can complicate hiring and business operations; governments—especially local and provincial authorities often do not function effectively or transparently; and corruption is widespread. In many cases the people that make up the BOP are denied access to proper services, energy, water, health, and above all the opportunities to improve their economic and social outlook.

In addition to the aforementioned realities, perhaps one of the most significant elements contributing to the psychic distance in BOPs, which firms may not even be aware of, is the presence of and roles played by informal sector and the hidden rules that govern them. As noted by London and Hart (2004) and Garcia-Verdu (2006), the informal sectors of developing countries play a much different and more substantial role than those found in the developed world. For instance, those found in the developing world are usually much larger and result not from the desire to hide illicit activities, but because the country lacks the dynamics to create enough formal opportunities to absorb the large numbers of the labor force, and complex regulatory environments make it too costly or complicated for many entrepreneurs to enter the formal economy.

The significance and differences of the informal sector in developing countries can be seen in the 15th International Conference of Labour Statisticians and ILO official definition of the term which ultimately distinguishes the informal sector as an entity entirely separate
from the “shadow” or “underground” economy. To address the many aspects in play, the ILO adopted three separate but related concepts to delineate the informal sector: informal sector, informal sector employment and informal employment (ILO, 2004). According to the ILO (2004) the *informal sector* consists of all legal, non-agricultural goods and services which are destined to market and are produced by private, unincorporated enterprises, which are part of the household sector where the key distinguishing characteristic between formal and informal private unincorporated enterprises or firms is that the former keep separate accounting records from their household activities, while the latter do not. *Informal sector employment* is then considered by ILO (2004) to be all work that is mobilized or employed by informal sector firms while *informal employment* (a more inclusive, job-based concept as opposed to the more firm-based concepts represented by the first two terms) was created to include all workers employed by an informal sector firm (i.e. informal sector employment) as well as own-account workers employed in their own informal sector enterprises; employers employed in their own informal sector enterprises; contributing family workers, irrespective of whether or not they work in formal or informal sector enterprises; members of informal producer’s cooperatives; employees holding informal jobs, defined as having an employment relationship not subject to national labor legislation, income taxation, social protection or entitlement to certain employment benefits; and own account workers engaged in production of goods for self-consumption.

One feature highly characteristic of developing countries with dynamics issues is the high percentages of micro, small and medium enterprises that often account for less than half of all formal employment and contributions to gross domestic product [GDP] (WBCSD & SNV [Netherlands Development Organization], 2007). For instance, Angelelli, Moudry and Listerri (2006) found that although large firms in Latin America made up less than one-half of 1% of total firms, they accounted for 23% of formal employment and generated more than half of the GDP while micro- Enterprises, over-represented in the informal sectors, made up approximately 94% of firms in the region, accounted for less than half of total formal employment and tended to display greatly diminished sales compared to large firms in terms of percent of total sales and average monthly sales. Additionally, WBCSD and SNV (2007) noted similar trends in Morocco where 93% of industrial firms are small and medium enterprises (SMEs) and account for
38% of production, 33% of investment, 30% of exports and 46% of employment; and in Bangladesh where enterprises of less than 100 employees account for 99% of firms and 58% of employment.

Although many micro, small, and medium enterprises have gained valuable local knowledge and skills surviving in hostile environments, the majority of these smaller sized firms face significant challenges and often lack adequate access to credit, training in basic skills such as management, book keeping, business planning, marketing, distribution, quality control and advanced technology (WBCSD & SNV, 2007), often creating obstacles for MNCs looking to use local suppliers or value chain partners. As a result of these challenges, micro, small, and medium enterprises in developing countries in particular and those found in the informal sector more specifically are often characterized by decreased wages, job-growth potential, skills-upgrading and job security (Angelelli et al., 2006).

A final characteristic common to BOPs that represents perhaps one of the greatest business differences for firms is the extreme importance of and reliance on social capital and social contracts by the people there. Excluded from the formal sector and the benefits associated with it, most of the people found at the BOP have become accustomed to more hostile environments where the name of the game is survival and trustworthy businesses and financial capital are difficult to come by. In the absence of such assurances, people at the BOP have learned to depend on their social networks as a source of capital (De Soto, 2000; London & Hart, 2004; Viswanathan, 2007) and even, as noted by Fletcher and Chikweche (2009), as a basis for how they relate amongst each other and to the environments outside their communities. For instance, Fafchamps (2000) observed that there was a great emphasis on relationships and on sharing information in BOP communities; Kuada and Sorenson (2000) found that trust, together with the creation and retention of long-term relationships were important parts of communities’ social fabric; and Michailova and Worm (2003), noted that in communities where individual members live and operate in a variety of formal and informal networks that cover different aspects of their social and business lives, family and kinship play a very important role in the creation and maintenance of trust.

As evidenced throughout this section, BOPs can certainly represent a significant amount of psychic distance to firms more familiar with developed and affluent markets.
However, it is important to point out that although it has often been assumed that psychic distance is negatively related to organizational performance, the truth is that the empirical research does not conclusively support either a positive or a negative relationship between the two (Evans and Mavondo, 2002). Furthermore, it has been argued that a firm’s perception of a greater level of psychic distance may actually lead to the realization of opportunities in and the creation of more successful business strategies for distant markets. According to Evans and Mavondo, when firms believe there are many differences between markets that could adversely affect business if undiscovered, they are more likely to proceed with caution, leave the assumptions at home, and take the necessary steps to learn about the new market environment. In contrast, O’Grady and Lane (1996) found that in numerous situations the biggest firm blunders came when firms perceived a low level of psychic distance between country markets (such as between the US and Canada), made incorrect assumptions, and failed to take into account some very important differences. Thus, if approached with an attitude of humility where learning becomes a key firm priority and assumptions are sidelined, a perceived high level of psychic distance could actually set firms up for success.

**Consumer Myths and Realities: Characteristics of the BOP Consumer**

A second major deterrence for firms, according to Prahalad (2006), has been the assumption that even if the company were to overcome the psychic distance represented by BOPs, it would be for naught because the poor resist new products, services, and technologies. However, numerous case studies, used to illustrate doing business at the BOP, have begun to reveal that the poor are often quite willing to consume but are rarely offered products designed for their lifestyles and circumstances (Prahalad, 2006) and are challenged by income constraints that limit their ability to pay for products and services (London & Hart, 2004; Prahalad, 2006; WBCSD, 2004). Additionally, most entrepreneurs and customers in the BOP are poorly served by low-quality vendors or are actively exploited by predatory suppliers and intermediaries, suggesting the possibility for firms to generate both profits and consumer surplus (Prahalad & Hammond, 2002).

Because the poor are generally cash-poor and with low levels of income, Prahalad (2006) suggested that companies must access them differently. For example, Prahalad noted,
firms can help to convert the BOP into a consumer market by designing strategies that help create the capacity to consume that include finding ways to not only create appropriate and affordable products and services, but also to create access to products (taking into account where the poor live, their work schedules, etc.) and to ensure their availability (or distribution efficiency). Additionally, firms should take into account the limitations of BOP consumers and understand the consequences of those in regards to the consumer/firm relationship. For example, a study by Viswanathan, Rosa and Harris (2005) determined that there were important differences between the capabilities of functionally illiterate—people lacking the language and numeracy competencies required to function adequately as adults in a day-to-day life—and literate BOP consumers that have should also be considered when formulating strategies. For instance, Viswanathan et al. (2005) found that functionally illiterate consumers had a strong preference for concrete reasoning and an overreliance on pictographic information, suggesting companies should reconsider how they highlight the added benefits of new products or the differentiating aspects of existing product offers across channels such as advertising, in-store displays, and positioning. According to Viswanathan et al. (2005), concrete reasoning has strong implications for the execution and presentation of price promotions through coupons and in-store discounts because many consumers are unable to process the information and avoid discounted products.

In regards to income, Banerjee and Duflo (2007) observed that the poor typically earn their money through informal employment in small and medium size firms or compensate for unemployment through self-employment. Additionally, to compensate for insufficient and most often unpredictable revenues and lack of access to credit, people at the BOP also tend to pursue multiple revenue generating activities (Banerjee & Duflo, 2007) and invest money in portable assets that can be sold quickly and easily for cash (such as small animals)--as ATMs and formal banking services have generally not been options for the poor.

In general, the typical low-income, low literate individual spends a high proportion of income on food, clothing and unexpected expenses such as those associated with serious illnesses, a punctured tire on a bicycle, or a birth, death, marriage, or even visits by guests (Viswanathan, 2007). The poor tend to make purchases only when they have cash and often buy only what is needed for the day and, as a result, BOP consumers are more likely to buy goods in smaller packages (like single-serve) and to shop more frequently than their bulk-
buying counterparts in TOP markets (Prahalad, 2006). Additionally, in BOP households, it is the women who are usually responsible for the household purchases and the distribution of the family budget. Men may weigh in on the bigger ticket items and assist the women in regard to transportation when it would be dangerous for her to travel alone but are otherwise out of touch with how the budget is allocated or how to assess the quality of generic products (Viswanathan, 2007).

Viswanathan (2007) found that individuals usually had a primary economic relationship with one local store that was often determined by geographic proximity to a person’s neighborhood or a larger retailer located farther away that sold to retailers as well as individuals. When choosing a retailer, Viswanathan (2007) found consumer decisions to be influenced by transportation factors (distance, cost, restrictive work schedules, forgone income in taking off work to travel, and just-in-time wages where wages earned by evening and the need to prepare a meal soon after) and the value offered by the retailer to the buyer. However, a person’s loyalty to a particular retailer was found to be greatly influenced by how responsive the store was to customer needs and whether or not they provided help and credit in times of need--an assurance highly valued by individuals whose unpredictable circumstances create high levels of uncertainty and anxiety (Viswanathan, Sridharan & Ritchie, 2008). For example, Viswanathan et al. (2005) observed that functionally illiterate consumers often displayed loyalty to companies that were sensitive to their literacy and numeracy deficiencies and suggested this tendency represented a potential for loyalty programs aimed at the population in some form other than price discounts.

Perhaps one of the most important factors to understand about BOP consumers, as noted by Viswanathan (2007), is that because of the severe constraints on traditional economic resources, these individuals have to deal with high levels of uncertainty and a lack of control over many aspects in their day-to-day lives, whether it is the quality or quantity of water or the availability of electricity. In addition, they must deal with significant amounts of complexity just in meeting basic necessities such as food preparation from generic ingredients, which in turn, are dependent on uncontrollable factors such as quantity and quality of water and the ingredients themselves (Viswanathan, 2007).

Due largely to this uncertainty, as well as to modest and unstable incomes, and low levels of literacy, individuals are often compelled to rely on others for help in times of need.
(Viswanathan, 2007). One important consequence of this interdependence among individuals is the resulting one-to-one relationships that have resulted among buyers and sellers and among individuals in general (Viswanathan et al., 2008). For instance, because buyers and sellers often come from similar economic strata and thus undergo similar adversities, and buyers may have at least some experience as a vendor, Viswanathan et al. (2008) noted that marketplace dealings between buyer and seller are often characterized by considerable empathy and offerings are regularly customized, with price, quality and quantity adjusted to account for the personal characteristics of both buyer and seller (Viswanathan et al., 2008).

Part of these one-to-relationships is the significance and frequency of the passing of information via word-of-mouth. This method of communication serves an important role in terms of obtaining information for the buyer and the seller alike. For example, according to Viswanathan et al. (2008) while word-of-mouth provides the seller with valuable consumer insights, it’s implications for a firm’s reputation also serves to limit unscrupulous practices and to condition individuals to be guarded about their transactions. This type of communication is also used by consumers to help reduce uncertainty when deciding whether or not to trust or try a new product or service. According to Prahalad (2006), because BOP consumers have to use their cash conservatively and are very value conscious by necessity, they will often pay more for a trusted brand than one they know. However, Viswanathan (2007) noted that consumers with a close relationship with a particular retailer that accepted product returns, allowed exchanges for bad products, adjusted supply based on customer complaints and generally tried to satisfy customers may resort to trial and error to try out new products and provide regular feedback to sellers about the products.

As seen in this section, the lives of BOP consumers are characterized by high levels of uncertainty, unpredictable income streams and life conditions, a shared experience of just trying to survive, and a diversity of skill sets, assets, and incomes. Further, people exist in the challenging environments of their countries’ informal sectors where they make their own informal rules to govern them and use their relationships to guide and protect them. One-to-one relationships become valuable market and social interactions and word-of-mouth the main channel for which to share information. In light of all the diversity in regards to need, circumstance, and capabilities, market offerings were found to be regularly customized
to the individual, indicating the need for new firms wishing to find a place at the BOP to be able to do the same.

**TRENDS, URBANIZATION AND URBAN POVERTY**

The urban populations in most developing countries have expanded more rapidly than total population over the years resulting partly from industrial activity and partly from biases in policy that have pulled people into cities with the enticement of greater job opportunities and access to better services (The World Bank, 1978). The UN-HABITAT (2008) reported that one effect of the mass migration from rural to urban areas and the consequent rapid urban growth experienced by many developing countries is that far more people have migrated to urban areas than could be absorbed, and despite large investments in urban infrastructure, the result has been a severe strain on urban services and labor markets with only small proportion of the increase in the work force able to find jobs in the formal sector. According to The World Bank (1978) the rest, who were absorbed mostly by the informal sector, earned meager incomes in service occupations which prevented purchasing power from rising as fast as the number of people.

In most developing countries, the inability of cities to absorb all the newcomers, results in highly dualistic urban systems, where islands of high income "modernity" coexist with shanty towns and slums (The World Bank, 1978). The urban poor face significant challenges in meeting their most basic everyday needs and in many cases, after factoring in the rural-urban trade-offs, may find themselves no less worse off than their rural cousins (UN HABITAT, 2006). In fact, the report noted, living in an overcrowded and unsanitary slum is actually more life threatening than living in a poor rural village. The UN-HABITAT (2006) report argued that part of these difficulties stem from the low levels of human capital that characterize the majority of urban poor, which, it noted, usually translate into low levels of income. Further, the urban poor generally lack proper access to basic infrastructure and public service, including drinking water, drainage, solid waste disposal, electricity, housing, telecommunications, roads, transportation, and education and health facilities (Garcia-Verdu, 2006; UN-HABITAT, 2008). Additionally, The World Bank (1978) asserted that the permanence of the new peripheral urban settlements had not been adequately recognized, and municipal financing and management had not received the attention they needed. As a result,
The World Bank (1978) noted, little had been done either to deal with the appalling inadequacy of essential services, such as sanitation, in these settlements, or to assist the large part of the urban economy that consisted of small-scale and informal production activities, which operated at low levels of productivity. However, when viewed in terms of the large collective needs and the more accessible natures of the urban poor (in relation to their more remote rural cousins), the urban poor may represent significant opportunities for firms looking to begin engaging BOP markets in the developing world.

**SUMMING UP AND MOVING FORWARD**

Hart and Milstein (2003) pointed out that the combination of a rising population and growing inequity was increasingly being recognized as a prescription for accelerating social decay, political chaos, and terrorism, suggesting that social development and wealth creation on a massive scale, especially among the world’s poorest, may be essential to sustainable development. In response to the skepticism of BOP researchers’ claims of market potential in regions rife with poverty, Fletcher and Chikweche (2009) maintain that, even in poverty-stricken BOPs, there are people who buy, consume, eke out an existence and are economic beings and though the individual purchasing power amongst this BOP group may be miniscule, collectively it is significant. Though BOPs may represent a significant psychic distance, require very different approaches and place new demands on firms, in light of the current global circumstances--two-thirds of the world living at the BOP, a widening gap between the rich and the poor, the aforementioned consequences of growing inequity which ultimately threaten all markets both BOP and TOP, and developed markets facing saturation, the serving the BOP may very well be crucial to the long-term survival of MNCs as well.

In light of the current gaps in the literature regarding insights for BOP consumers and environments, both in general and in terms of those inherent to a specific country, the following chapter examines Mexico for insights into its BOP market potential (in terms of numbers, needs and capabilities, and opportunities) and the environmental characteristics that work to shape and influence both the sector itself and the people within it. Through these insights, the thesis seeks to gain a better understanding of what opportunities and challenges may exist for firms seeking to do business in Mexico’s BOP, and what types of strategies are needed to be successful.
CHAPTER 3

MEXICO

Mexico was chosen as a country of interest for examining BOP potential and strategies for numerous reasons. First, with a population of 111,211,789 (Central Intelligence Agency [CIA], 2009), Mexico is the twelfth largest country in the world with the second largest market in Latin America. Second, despite its aggregate wealth, Mexico’s resources are heavily concentrated among a small percentage of individuals that are concentrated mostly in urban areas Garcia-Verdu (2006), resulting in a situation where household incomes span a wide spectrum from extremely wealthy to disturbingly poor. For example, according to findings by CONEVAL (2005b), approximately 47% of Mexico’s population is considered to be poor with 18.2% of this group classified as extremely poor. Additionally, The World Bank (2005) reported that although Mexico is a middle income country with a 2004 gross national income (GNI) of US $6,770, more than half its population can be considered informal (in terms of their lack of access to social security systems). In other words, Mexico’s BOP is composed of nearly half of Mexico’s 111 million people.

Third, in the last century, Mexico has experienced such rapid population and urban growth that the urban population now constitutes nearly 80% of Mexico’s total population (National Water Commission, 2008). Although the incidence of poverty is still relatively higher in Mexico’s rural areas where 57% of the population is reported to be moderately poor and 28% extremely poor, as compared to urban areas where 41.7% is moderately poor and 11.3% are extremely poor (The World Bank, 2005), given the fact that the country is so predominantly urban, in sheer numbers around half of the population living in moderate poverty and one-third of those living in extreme poverty are actually residing in urban areas. This urban concentration offers a potential opportunity for firms that do not have the capacity to overcome distribution and marketing challenges to reach remote, rural regions to achieve the initial scale needed in their new ventures.
A fourth reason for selecting Mexico for study is that it is one of the few developing
countries that actually has abundant and relatively high-quality data. For example, since 1993
INEGI has been publishing official statistics on the informal sector of the Mexican economy
as part of the System of National Accounts. As a result, better measurements of informal
economic activity may be obtained in the Mexican case than is possible from other
developing countries. Additionally, utilizing data from INEGI’s II Conteo de Población y
Vivienda 2005 (INEGI, 2005), CONEVAL publishes a Marginalization index that provides
socio-economic indicators that allow a more in depth analysis of the multidimensional
character of poverty in Mexico by state and by municipality. Finally, INEGI also publishes
statistics on household income and expenditures for various income levels in its 2008
ENIGH report (INEGI, 2008), allowing firms the ability to obtain some insight on income
levels and sources at the BOP as well as on what the poor currently spend their money on.
Insight into current spending patterns can help firms uncover not only what people value
most but can also shed light on what types of things are needed but either out of reach for the
poor or possess a value that is not yet understood by the poor, either of which can represent
opportunities for innovative firms.

This chapter will examine the aforementioned data and other resources in an attempt
to determine Mexico’s BOP potential and characteristics. To do so, this chapter includes an
overview of Mexico, an investigation of the major factors shaping its BOP and informal
sector, an examination of the characteristics of its BOP people and environment, an analysis
of the estimated quarterly income and expenditures of its BOP households, and ends with an
overall discussion of the chapter’s findings.

OVERVIEW OF MEXICO

Mexico is a federal republic meaning that its State governments are free and
sovereign entities (CIA, 2009). Mexico has 31 federations, or states, and one federal district
(D.F) where states are further divided into municipalities (2,429 throughout the country) and
the Federal District is divided into 16 independent delegations (CIA, 2009). The following
subsections will highlight the major insights regarding Mexico’s internal diversity,
demographics, major issues, economy, and labor force.
The Diversity Within

The World Bank (2009a) notes that Mexico is approximately 758,449 square miles, or slightly less than three times the size of Texas, and shares a 2000 mile border with US to the north and borders Guatemala and Belize to the south. Within these borders, Mexico’s terrain varies from high, rugged mountains and high plateaus to low coastal plains and formidable deserts (The World Bank, 2009a). Further, the climate varies from tropical to desert; the elevation ranges from its lowest point at Laguna Salada (10 m) to its highest point at Volcan Pico de Orizaba (5,700 m); and its natural hazards encompass everything from tsunamis along the Pacific coast to volcanoes and destructive earthquakes in the center and south, and hurricanes on the Pacific, Gulf of Mexico, and Caribbean coasts (The World Bank, 2009a). As will be evidenced in the next chapter of this thesis, all of these factors play an important role in shaping the needs, local cultures and ways of doing things as well as the capabilities and limitations of the people who live in the country’s various regions.

The people of Mexico are just as diverse as the land. They represent such diversity in fact, that it has been argued that except for living in the same country, there has been very little that has united all the people living within Mexico’s borders since the day it became a nation. Indeed, as argued by Simpson (1941), a more adequate description of the nation might be to say that there are actually many Mexicos within the national borders that contribute to the rich diversity of Mexico’s regions, states, localities, and communities. For instance, although the CIA (2009) lists the ethnic make-up in Mexico as 60% mestizo (or a mix of Spanish and Indian), 30% Amerindian, or predominantly so, 9% white and 1% other, the grouping of indigenous peoples into one “Amerindian” category masks the great diversity that exists among Mexico’s various indigenous groups that encompass different ethnic backgrounds, languages, cultures, political systems, community customs. Additionally, although Mexico’s 2000 census lists Roman Catholic is the most commonly practiced religion (76.5% of the population) and Protestants occupying the second largest percentage at 6.3% (as cited in CIA, 2009), it is important to note that among indigenous groups the religion practiced is often a mixture of Catholicism and older indigenous religious and superstitious practices.
Demographics

Mexico has a very young population, as seen in its estimated median age of 26.3 years (CIA, 2009). For instance, of the total population, 64.6% are between the ages of 15 and 64, and 29.1% are between the ages of zero and 14 (CIA, 2009). Further, by 2020, the 25-50 year-old demographic will be the largest age segment in the country (Ecoblock International, 2009a). Although The World Bank (2009a) estimates that 94% of males and 91% of females ages 15 and greater are considered to be literate, CONEVAL (2005b) findings show that 45.98% of the total population in Mexico has not completed basic education.

Resulting from a large growth in population (from 13,607,259 to 97,483,312) and a mass migration of people from rural to urban regions between the years of 1900 and 2000 (Garcia-Verdu, 2006), the percentage of Mexico’s people living in urban regions has changed dramatically in the last 100 years. According to Garcia-Verdu (2006), one of the results of the mass migration from rural to urban areas and rapid urban growth in Mexico has been the emergence of one megacity, or a small group of cities with populations above one million, and a large number of medium sized cities with populations above 100,000 people. In fact, citing findings for 2002 from the Statistical Division of the UN, Garcia-Verdu (2006) noted 69 cities proper in Mexico with populations of 100,000 people and nine urban agglomerations in Mexico with populations of one million people or more. According to Garcia-Verdu (2006), the largest urban agglomerations are the Mexico City Metropolitan Area, with 18,538,820 inhabitants, the Guadalajara Metropolitan Area with 3,863,855 and the Monterrey Metropolitan Area, with 3,426,078.

Taking these findings a step further, National Water Commission (2008), using information gathered in 2005, found and mapped out 30 population centers in Mexico with more than 500,000 inhabitants. Of these 30 centers, the National Water Commission report notes that 27 are said to correspond to metropolitan zones and the rest to individual municipals. The maps contribute to a visual understanding of the distribution and densities of the population centers throughout the country and reveal that 56% of the total population are concentrated in Mexico’s 56 metropolitan zones with 30.8%, or 31.8 million people, living in the five metropolitan zones (and the 148 municipalities and/or delegations of the Federal District within them) of Valle de Mexico, Guadalajara, Monterrey, Puebla-Tlaxcala, and
Toluca—all of which are located in Mexico’s Central region (National Water Commission, 2008). According to The World Bank (2009b), the urban areas of the Central region are also where approximately one quarter of the country’s extreme poor resides. The rest of the population centers reported by the National Water Commission are found scattered mostly throughout the North with a smattering of smaller ones in the South.

**Major Issues**

Ongoing economic and social concerns include recent spikes in violence, mainly from wars between rival drug cartels, low real wages, underemployment for a large segment of the population, inequitable income distribution, and few advancement opportunities for the largely Amerindian population in the impoverished southern states (The World Bank, 2009a). Further, in regard to environmental issues, Mexico has a scarcity of hazardous waste disposal facilities; a large incidence of rural to urban migration; a shortage of natural fresh water resources with pollution issues in the North, inaccessible and poor quality issues in the Center and extreme Southeast; raw sewage and industrial effluents polluting rivers in urban areas; deforestation; widespread erosion; desertification; deteriorating agricultural lands; serious air and water pollution in the national capital and urban centers along US-Mexico border; and land subsidence in Valley of Mexico caused by groundwater depletion (CIA, 2009)

**The Economy**

Mexico has a free market economy in the trillion dollar class (The World Bank, 2009a). The CIA (2009) reported US $1.483 trillion in 2009 purchasing power parity adjusted GDP estimate for Mexico. Although this figure is up from $1.494 in 2006, the GDP real growth rate has decreased from 5.1% in 2006 to 3.3% in 2007 and 1.3% in 2008 (CIA, 2009). Consumer price inflation was headed downward after peaking at 6.5% in December, 2008 (The World Bank, 2009a). Per capita income is roughly one-third that of the US and the purchasing power parity adjusted GDP per capita for 2008 was estimated at US $14,200, up from $13,900 in 2006 (CIA, 2009). Income distribution remains highly unequal as indicated by a 2006 Gini coefficient of 47.9 (CIA, 2009) with household income or consumption by percentage share figures showing the lowest 10% of households with a mere
1.8% while the highest 10% of households took 37.9% (CIA, 2009). According to The World Bank (2009b), the inequality in Mexico has tended to be counter-cyclical, it was reduced by the 1994-1995 crises, but increased with the 1996-2000 recovery and was then reduced again by the 2000-2003 stagnation. After having reached the already very high Latin American average, Mexico fell slightly under the average in 2002 (The World Bank, 2009b).

Although measuring GDP in terms of informal output is difficult, as the two sectors are often quite intertwined and informal activities are present in both formal sector and informal sector firms, according to estimates by Becker (2004), the informal economy in Latin American accounts for more than half of nonagricultural employment. Garcia-Verdu (2006) found that informal sector output in Mexico represented on average one eighth of GDP over the period 1993-2003 and in 2003, The World Bank and the International Finance Corporation [IFC] (2006) estimated that 30.1% of Mexico’s GNI was derived from the informal sector.

While total spending increased on average by 6.3% a year between 2000 and 2002, social development spending increased on average by 5.3% a year and poverty reduction spending increased by 14.2% annually (The World Bank, 2009b). According to The World Bank (2009b), spending on programs specifically targeted to the poor now represent 1.3% of GDP, compared with 0.7% in 1990. Further, programs involving transfers to the poor, spearheaded by OPORTUNIDADES (formerly PROGRESA) grew by 8.4 percent a year on average during the 1990’s and by 9.8% since 2000 (The World Bank, 2009b).

Mexico’s economy contains a mixture of modern and outmoded industry and agriculture, increasingly dominated by the private sector with recent administrations having expanded competition in seaports, railroads, telecommunications, electricity generation, natural gas distribution, and airports (The World Bank, 2009a). According to The World Bank (2009a), Mexico is dependent heavily on oil exports, trade with the United States and on money sent home by the millions of migrant workers in the US. As a result, the recent dramatic drop in international oil prices and the financial crisis in the US, which caused large declines in migrant remittances, significantly affected Mexico’s public finances. Economic growth decelerated in the first three quarters of 2008 and turned negative during the last quarter, bringing GDP growth for the year at a modest 1.3% (The World Bank, 2009a).
The Labor Force

In 2008, Mexico’s labor force was an estimated 45.32 million people with unemployment estimated at 4% and underemployment estimated at a conservative 25% (CIA, 2009). However, it is important to note that the unemployment rate appears low, not because of adequate formal employment opportunities but because the employment data include both those individuals employed by the formal economy and the large numbers of those employed within the informal sector. For example, Garcia-Verdu (2006) found that half the labor force in Mexico and in the Mexico City Metropolitan Area were employed informally and reported that this share had remained relatively constant over past years despite the fact that the economy had experienced episodes during which per capita GDP had grown above trend. Referencing IMSS (one of Mexico’s main social security providers) administrative records, Garcia-Verdu (2006) revealed that in fact, the average number of new formal jobs created during the 1996-2000 period of relatively high GDP growth rates of was only about 971,000 per year, hardly enough to satisfy the 1.14 million annual new entrants to the working-age population.

According to Garcia-Verdu (2006) this inability of the economy to create sufficient formal jobs to absorb the entrants to the labor force even in periods of high economic growth suggests that the causes of the informal economy may be more structural than cyclical in nature. As Wall (2007) noted, although the Mexican economy is stable at present and foreign direct investment (FDI) has continued to pour in, it continues to lack the dynamics needed to produce more jobs. Thus, Wall (2007) noted, economic growth alone, absent of the appropriate policy reforms is unlikely to decrease the prevalence of informality in the country, and with so many vested interests involved, implementing the needed reforms may be difficult to achieve.

FACTORS SHAPING MEXICO’S BOP AND INFORMAL SECTOR

An accommodating business environment is one that encourages firms to operate efficiently. Such conditions strengthen incentives for firms to innovate and to increase productivity—key factors for sustainable development. A more productive private sector, in turn, expands employment and contributes taxes necessary for public investment in health, education, and other services. In contrast, a poor business environment increases the obstacles to conducting
business activities and decreases a country’s prospects for reaching its potential in terms of employment, production and welfare (The World Bank & IFC, 2006, p. 3).

As measured by various dimensions of the Ease of Doing Business Index for 2010, Mexico, ranks 51st out of 183 countries, indicating that, at least in some areas, Mexico outperforms several of the world’s other economies (The World Bank, 2010). Further, it appears to be improving as it has jumped 24 places in its worldwide ranking for Ease of Starting a Business from 2009-2010 (The World Bank, 2010). According to The Heritage Foundation (2010), the overall freedom to conduct a business is protected under Mexico’s regulatory environment; starting a business takes an average of 13 days, compared to the world average of 35 days and costs an average of 11.7% of income per capita, compared to the Latin American average of 36.6%; obtaining a business license requires less than the world average of 18 procedures and 218 days; and bankruptcy procedure are reported to be relatively easy. However there are several issues that impede a productive business environment in Mexico and create obstacles and disincentives for many people and small businesses to participate in the formal sector.

For instance, the country’s regulatory framework is characterized by high levels of bureaucracy that can make starting a business quite burdensome and expensive; property is often difficult and costly to register; credit is still expensive and hard to obtain; and many aspects of the labor legislation are counter-productive, outdated and result in high incidences of firm non-compliance and in the denial of mandated benefits to workers (Garcia-Verdu, 2006). Additionally, the country’s overburdening regulatory framework appears to open the possibility for corruption and bribery as private agents attempt to sidestep the multiple procedures required and avoid the costs imposed by the regulations. Not surprisingly then, Mexico like many Latin American nations faces a high level of corruption, which adds to the uncertain business environment as noted by Transparency International (2008) which perceived corruption in Mexico to be significant and ranked the nation 72nd out of 179 countries. Further, The Heritage Foundation (2010) found the country’s judicial system to be slow to resolve cases and vulnerable to corruption. From a firm perspective, results of Enterprise Surveys conducted in Mexico, showed that 17.9% of all sized firms (small, medium and large) identified corruption as the main obstacle, and 48.1% of firms considered
it a major constraint to doing business with the largest percentages (61.7%) coming from large businesses (The World Bank & IFC, 2006). Ultimately these issues create significant challenges for formal sector firms in terms of dealing with in regards to anti-competitive or informal practices. For example, according to Enterprise Surveys from firms doing business in Mexico (small, medium and large), the presence of anti-competitive or informal practices were ranked as the top obstacles to doing business in the country (The World Bank & IFC, 2006).

Another important aspect to understand is that despite the aforementioned national averages reported by the Ease of Doing Business Index and the Heritage Foundation, the reality in the country is that such figures vary from state to state throughout the Federal Republic of Mexico as both the state and local municipal governments have the right and ability to pass legislation for their areas so long as it does not interfere with State or Federal regulations (CIA, 2009) and thus bear considerable influence over the regulatory environments in which their inhabitants must operate (Garcia-Verdu, 2006).

Further, because most of the efforts to streamline the regulatory process in Mexico have, thus far, been at the federal level, state and municipal processes are proceeding at uneven paces where some states have advanced their regulatory reform agenda significantly and others have lagged behind (Garcia-Verdu, 2006). Consequently, there are wide differences from state to state in levels of transparency, and in the number of procedures, time and cost to register property. For example, in Chiapas, three weeks are sufficient to complete the five procedures necessary that cost 1.6% of property value, the same property transfer requires eight procedures, takes almost three and one-half months and costs 4.3% of property value in Quintana Roo (The World Bank, 2008). Additionally, time to enforce a contract across cities was found to vary significantly despite identical federal legislation: 248 days in Zacatecas and 560 days in Quintana Roo. Various states were noted to be reducing backlog by creating specialized commercial courts—such as Zacatecas, the top performer on the ease of enforcing contracts (The World Bank, 2008). Other states were increasing using electronic platforms to share information and manage cases (Garcia-Verdu, 2006). The World Bank (2008) lists the 32 states according to their ease of doing business rankings. As of 2009 the top five easiest places to do business in Mexico are the central states
of Aguascalientes (1), Zacatecas (3), San Luis Potosí (4), the northern state of Sinaloa (5) and the southern state of Chiapas (2).

CHARACTERISTICS OF MEXICO’S BOP

As noted in Chapter 2, the character of poverty is multidimensional, involving all aspects in a person’s life, and often varies from region to region based on differing levels of income, equality or inequality, and ones access to or deprivation of opportunities and resources. In order to get a better idea of the state of the poor in Mexico, including their needs, limitations and capabilities, this section will draw from CONEVAL’s Marginalization Index, which was based on survey responses gathered by INEGI’s 2005 National Census and created to measure poverty in such a way that considers its multidimensional characteristics. The Marginalization Index covers Mexico’s 32 Federal entities and their municipalities, though for the purposes of this thesis, only the federal entities will be examined.

The Index presents three categorizations of income-measured poverty to include “pobreza alimentaria,” “pobreza de capacidades” and “pobreza patrimonial,” each explained in depth below, and uses 13 indicators to measure the various levels of social deprivation experienced in each state. Together, these 13 indicators allow a deeper understanding of how poverty is experienced by people from region to region through an assessment of the abilities, or inabilities, reported by low-income households to access basic services and benefit from others essential to the development of basic household capabilities.

Describing the three levels of poverty in greater depth, CONEVAL (2009) explains that pobreza alimentaria, hereafter referred to as “food poverty,” is the most extreme of the poverty categorizations and is comprised of those households whose disposable income is not enough to acquire even the minimum acceptable level of nutrition or “basic food basket” for every member of the household, even if all the household income was used to obtain it. The second category, CONEVAL (2009) notes, is pobreza de capacidades, hereafter called “capability poverty,” and refers to those households whose disposable income is insufficient to purchase the basic food basket and make the necessary expenditures on health and education even when devoting the entire household income to these purchases. Finally, CONEVAL (2009) explains that pobreza patrimonial, hereafter referred to as “asset
poverty,” is the portion of the population whose disposable household income is insufficient to acquire the basic food basket and to make the necessary expenditures on health, clothing, housing, transportation and education needed for all members of the household, even if all household income was used exclusively for the purchase these goods and services. Thus the food poverty category includes only those households considered to be in extreme poverty, unable to purchase even the basic food basket, while the asset poverty category casts a wider net to include both the households represented in the food poverty and capability poverty categories and an additional group of households, better off than the first two category members but still unable to cover all the aforementioned expenses in its category.

According to CONEVAL’s (2005b) Marginalization Index, the average number of the total population in Mexico that fall into the food poverty, capability poverty and asset poverty categories are 18.2%, 24.7%, and 47.9% respectively. Because the households represented by all three categories all consist of those individuals found in Mexico’s BOP, the thesis will focus largely on the final, all-inclusive category, asset poverty.

**Poverty: Income, Social Deprivation and Regional Differences**

Although 47.9% is a high figure in and of itself, it is important to note that in 16 out of Mexico’s 32 federal entities, asset poverty is reported to be greater than 50% of the population and reaches as high as 75% in federal entities like Chiapas, Mexico’s poorest state (CONEVAL, 2005b). Further, in addition to these 16 states, eight others report asset poverty above the national average, ranging from 40-49.9% of the population. In fact, only three of Mexico’s states, Nuevo Leon, Baja California Sur, and Baja California report asset poverty numbers consisting of less than 30% of the population.

To illustrate the geographical distribution of poverty throughout Mexico, CONEVAL (2005a) created several maps dividing the country’s federal entities into seven sections according to their levels income. The maps show that those states that reported asset poverty between the ranges of 35.8% and 75.7% are found spanning the entire country, indiscriminately from north to south and east to west. However, a second map presented by CONEVAL (2005a) plotting the incidences of food, capability and asset poverty separately, reveals that the highest levels of all three poverty levels can be seen clustered in the southern
and central states while the lowest levels are spread out in the northern states bordering the
US, in those states along the west coast and in the states of Baja California North and South.

In regards to social deprivation, CONEVAL (2005b) found Mexico’s highest scoring
marginalization categories, representing the presence of higher amounts of social deprivation,
to be “the percentage of the population 15 years or older that have not completed basic
education” (primary and secondary) (45.98 %); “the percentage of homes with household
members between 15 and 29 years with some resident who has less than nine years of
education” (36.12 %); “the percentage of the population that are without health services”
(49.78 %); “the percent of occupied, private dwellings that did not have a washing machine”
(39.94 %); and “the percent of occupied, private dwellings that did not have a refrigerator”
(23.22 %). The next highest scoring groups were those occupied, private dwellings that did
not have access to “drainage” (11.67%), “water from the public network” (11.05%), “a
private toilet or sanitary” (9.9%), and finally, those “homes with dirt floors” (9.93%). With a
population of over 103 million at the time the surveys were done in 2005, even this last
category with only 9.93% of the population, still represents some 10 million Mexicans.

Table 1 shows the performance of Mexico’s 32 states based on their levels of reported
asset poverty and social deprivation as found in CONEVAL (2005b). As illustrated by the
table, 17 states reported poverty levels greater than the national average. Further 11 of those
17 also scored social deprivation scores of “high” and “very high” indicating the extreme
levels of social deprivation found in those states. The states that reported the lowest levels of
poverty were Baja California, Baja California Sur, Nuevo Leon, Distrito Federal, and
Chihuahua. Notably, all of these states also received “low” to “very-low” social deprivation
scores. Though it may be the case in some areas that the severity of a state’s asset poverty
directly influences its performance in regards to social equity or vice versa, the performance
of the rest of Mexico’s states in these two categories appear to suggest that this is not always
the case. In fact, as seen in Table 1, some states, despite their high incidence of income level
poverty appear to have successfully managed to create more equitable access to public
services as measured by the marginalization index. For example although 51.1% of the
population in Aguascalientes was found to be in asset poverty, the state still managed to
create enough social equity for its residents to be ranked fourth in the nation among its peers.
Table 1. Asset Poverty and Social Deprivation Performance in Mexico’s 32 Federal Entities

<table>
<thead>
<tr>
<th>Rank</th>
<th>State</th>
<th>Population in Asset Poverty</th>
<th>Social Deprivation</th>
<th>Rank</th>
<th>State</th>
<th>Population in Asset Poverty</th>
<th>Social Deprivation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Chiapas</td>
<td>76% 3.2 million</td>
<td>Very High</td>
<td>17</td>
<td>Morelos</td>
<td>41% 668 thousand</td>
<td>Medium</td>
</tr>
<tr>
<td>2</td>
<td>Guerrero</td>
<td>70% 2.2 million</td>
<td>Very High</td>
<td>18</td>
<td>Durango</td>
<td>59% 897 thousand</td>
<td>Medium</td>
</tr>
<tr>
<td>3</td>
<td>Oaxaca</td>
<td>68% 2.4 million</td>
<td>Very High</td>
<td>19</td>
<td>Mexico</td>
<td>50% 7 million</td>
<td>Low</td>
</tr>
<tr>
<td>4</td>
<td>Puebla</td>
<td>59% 2.4 million</td>
<td>Very High</td>
<td>20</td>
<td>Nayarit</td>
<td>44% 415 thousand</td>
<td>Low</td>
</tr>
<tr>
<td>5</td>
<td>Veracruz</td>
<td>59% 4.2 million</td>
<td>High</td>
<td>21</td>
<td>Sinaloa</td>
<td>44% 1.2 million</td>
<td>Low</td>
</tr>
<tr>
<td>6</td>
<td>Michoacán</td>
<td>55% 2.2 million</td>
<td>High</td>
<td>22</td>
<td>Baja CA Sur</td>
<td>24% 120 thousand</td>
<td>Low</td>
</tr>
<tr>
<td>7</td>
<td>Hidalgo</td>
<td>54% 1.3 million</td>
<td>High</td>
<td>23</td>
<td>Jalisco</td>
<td>42% 2.9 million</td>
<td>Low</td>
</tr>
<tr>
<td>8</td>
<td>Yucatan</td>
<td>52% 940 thousand</td>
<td>High</td>
<td>24</td>
<td>Chihuahua</td>
<td>34% 1.1 million</td>
<td>Low</td>
</tr>
<tr>
<td>9</td>
<td>Campeche</td>
<td>51% 388 thousand</td>
<td>High</td>
<td>25</td>
<td>Baja CA</td>
<td>9% 261 thousand</td>
<td>Very Low</td>
</tr>
<tr>
<td>10</td>
<td>San Luis Potosi</td>
<td>56% 1.3 million</td>
<td>High</td>
<td>26</td>
<td>Tamaulipas</td>
<td>45% 1.4 million</td>
<td>Very Low</td>
</tr>
<tr>
<td>11</td>
<td>Guanajuato</td>
<td>52% 2.5 million</td>
<td>High</td>
<td>27</td>
<td>Colima</td>
<td>39% 218 thousand</td>
<td>Very Low</td>
</tr>
<tr>
<td>12</td>
<td>Queretaro</td>
<td>37% 415 thousand</td>
<td>Medium</td>
<td>28</td>
<td>Sonora</td>
<td>40% 967 thousand</td>
<td>Very Low</td>
</tr>
<tr>
<td>13</td>
<td>Tlaxcala</td>
<td>51% 549 thousand</td>
<td>Medium</td>
<td>29</td>
<td>Aguascalientes</td>
<td>51% 544 thousand</td>
<td>Very Low</td>
</tr>
<tr>
<td>14</td>
<td>Tabasco</td>
<td>59% 1.2 million</td>
<td>Medium</td>
<td>30</td>
<td>Coahuila</td>
<td>41% 1 million</td>
<td>Very Low</td>
</tr>
<tr>
<td>15</td>
<td>Queretaro</td>
<td>38% 603 thousand</td>
<td>Medium</td>
<td>31</td>
<td>Distrito Federal</td>
<td>32% 2.8 million</td>
<td>Very Low</td>
</tr>
<tr>
<td>16</td>
<td>Zacatecas</td>
<td>54% 733 thousand</td>
<td>Medium</td>
<td>32</td>
<td>Nuevo Leon</td>
<td>28% 1.2 million</td>
<td>Very Low</td>
</tr>
</tbody>
</table>

Measuring Urban Poverty and Social Deprivation Performance in Mexico

Like CONEVAL, CONAPO (2005) also created a marginalization index based on data derived from INEGI’s 2005 national census. However, in CONAPO’s version, the index focuses on measuring the incidence and depth of poverty in Mexico’s AGEBs and is thus called the Urban Marginalization Index for 2005. This index uses many of the same indicators as the CONEVAL (2005b) index and covers 29,564 urban AGEB’s with a total population of 69.8 million people. Interestingly, 49.3% of urban AGEB show low-very low levels of social deprivation while 10.2%, 18.7% and 21.7% of urban AGEB respectively report very high, high, and medium levels. The greatest deprivation found in these urban regions, overall, were found in the percentages of people over 15 years that have not completed secondary school (36%), the percentages of people not accessing health services (43.3%), the percentages of households without water piped into their homes (17.2%), the percentages of households without a private toilet with a connection to water (22%), the percentages of households without a refrigerator (11.4%), and finally, the percentage of households reporting over crowdedness (18.3%).

Compared to the national figures reported by CONEVAL (2005b) mentioned previously, AEGB urban regions appear to perform 10 and 12 percentage points better in regards to those completing secondary school and those households in possession of a refrigerator, respectively. However, according to the two indexes, urban areas actually perform six percentage points worse than the overall average in regards to those households with access to water piped in from a public network. Still, it is important to point out that in some of the urban AGEBs with high to very high levels of social deprivation reported, the percentages of the indicators showing the highest levels of social deprivation can be as high as 40 to 80%.

According to The World Bank (2005), location is a key element for understanding the structure and trends in deprivation not only in regard to differences between urban and rural locations but also in regard to city size and even more significantly to the particular larger regions they are associated with. Illustrating the role city size plays on marginalization levels, CONAPO (2005) compiles Mexico’s cities into three groups: the 9 metropolitan zones with populations of greater than a million inhabitants; the 80 medium sized cities with populations
of 100,000-999,000; and the 269 small cities with populations of 15,000-99,000 people. The report found that as city size increased, the levels of social deprivation decreased from approximately 40% in small cities to 19.5 and 17.2% in medium and large cities respectively (CONAPO, 2005).

Although the size of the city certainly appears to influence the severity of the social deprivation found there, CONAPO (2005) find that regional affects also play a big role. For example, when urban AEGBs are examined by region, it becomes clear that some regions have significantly higher percentages. For example, when comparing the Monterrey region to the Puebla-Tlaxcala region, Monterrey was found to have less than 5% of its population in AGEB urban areas with high and very high levels of social deprivation while Puebla-Tlaxcala showed up to 38.7% of its population in such areas. Of the urban AGEBs reporting high and very-high levels of social deprivation, 38.6% can be found concentrated in just four entities of the country’s central and southern regions. These entities are the states of Mexico, Veracruz, Puebla, and Guerrero. On the other end of the spectrum, Aguascalientes, Baja California Sur, Tabasco and Nayarit have the highest percentages of urban areas with low and very low social deprivation scores in the country.

The Marginalization Indexes provide helpful tools for better understanding the experiences, levels, extent and diversity of poverty from region to region and may provide some insight into the location of more socially equitable areas where poor households may be able to make their money go a little further than households of equal income in areas with higher levels social deprivation. Additionally, it can also highlight where gaps in access to goods and services may represent opportunities for visionary businesses willing to engage households at the BOP.

However, it is important to be aware that these indexes are not without their limitations and firms should avoid making any major assumptions based on them. For instance, although the percentages given provide information on the quantity of people with access, they do not report on the quality of services actually received. As noted by The World Bank (2005), although public services are usually more available in cities, they are often known to fail for the poor due to low quality and reliability. According to The World Bank (2005) evidence of this reality can be seen in the figures showing that infectious diseases such as diarrhea and acute respiratory infections have been found to be equally common
among both urban and rural poor children, suggesting that, regardless of increased claims to access, urban water and sanitation systems have remarkably poor quality. Thus, although the indexes can allow a good jumping off point, in situations where accurate figures are needed, relying on indexes as a sole measurement tool to determining the extent of access and social deprivation will most likely lead to misleading conclusions about well-being (or needs and opportunities) in urban areas. Instead, organizations that require more accurate insights will most likely need to find ways of conducting their own on the ground assessments of the communities or areas they are interested in.

BOP Households Earnings and Expenditures

The goal of this section is to gain insight into the actual income earned, the spending power, and the current purchasing priorities of Mexico’s BOP consumers. To do so, an analysis of quarterly data gathered and presented by INEGI (2008) is done, looking specifically at those income and expenditure data for households earning between one and six times the MW in Mexico for the year 2008. It is important to note that Mexico determines its minimum wage figures by day and not by hour as done in the US. As a frame of reference, Mexico’s minimum wage amounts are divided into three geographic zones (A, B and C). Using the exchange rate at the time this section was written in 2009 of 12.7 pesos to the dollar (Currency Calculator, 2009), the corresponding daily minimum wages for each category are: A, 54.8 pesos (US $4.31); B, 53.26 pesos (US $ 4.19); and C, 51.95 pesos (US $4.09; Black, 2008).

BOP researchers refer to the BOP in terms of households that make less than US $6,000 per year or individuals who make less than $1500/year. Because there is no specification given on which minimum wage zones are represented and household income here is reported for only one quarter and income streams are known to vary from quarter to quarter, determining how many people in Mexico fall into this $6,000/year category, will not be an exact science nor will the resulting figure be without its inaccuracies. However, for this thesis, by taking the INEGI (2008) data from the minimum highest income multiple measure of six times the minimum salary for the quarterly average monetary income per household ($18,895 pesos), dividing that by the aforementioned 12.7 exchange rate, and then multiplying that figure by 4 (quarters), a figure of US $5,951 per year, per household is
obtained, which is just under the $6,000/yr figure listed above. Thus, this section will refer
the income and expenditures of those households represented in the minimum wage multiples
(MW) of 1-6.

INEGI (2008) provides a report of the quarterly income and expenditures experienced
by households in each minimum salary multiple for one quarter in Mexico. According to the
results of the Household Budget Survey 2008 associated with the reported data, Mexico had
approximately 26,732,594 households in the country with an average of four people per
household. The average quarterly income reported for MW 1-6 was US $934. Multiplied by
the 14,015,108 households placed in these six income categories, this per household figure
represented a collective monetary current income total of over US$ 13 million dollars.
Further, in regard to current spending money, total expenditures per household for the
MW1-6 groups was calculated to be approximately US $968, representing a collective
US $14.9 million dollars when multiplied by the categories’ 14,859,831 households with an
average 24% increase in overall expenditures was observed with each increase in income
level.

INEGI (2008) surveys, which examined the expenditure patterns for one quarter,
identified and reported data for nine main expenditure categories. Table 2 lists each of these
categories for the MW multiples of 1-6 and provides the total average amount spend per the
quarter, per multiple, per MW multiple. Additionally, the percentages in Table 2 provide
insight into the amount of money spent in each category as a percentage of total expenditures
and how these change when moving up MW levels. For example, of the nine categories
noted in Table 2, food, beverage, and snuff (tobacco); clothing and footwear; housing and
fuels, articles and services for cleaning, care of the house and household items; health care,
transport and communications; education and recreation, personal care, and transfer
spending, showed the main components of current spending money of the members of MW
1-6 households were food, beverages and snuff (46%); transport and communications (17%),
education and recreation (14%) and housing and fuels (12%) while personal care and
clothing and footwear each accounted for 7%. The top four expenditure categories noted by
the MW 1-6 households were also reported by the overall average of households from all
income groups represented in the INEGI (2008). Of all the main categories measured by
INEGI (2008) noted in Table 2, in terms of percentage of total expenditures, the food,
<table>
<thead>
<tr>
<th>Category</th>
<th>1MW</th>
<th>1.5MW</th>
<th>2MW</th>
<th>3MW</th>
<th>4MW</th>
<th>5MW</th>
<th>6MW</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Food, Beverage &amp; Snuff</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$223</td>
<td>$268</td>
<td>$318</td>
<td>$364</td>
<td>$433</td>
<td>$499</td>
<td>$557</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>53%</td>
<td>51%</td>
<td>47%</td>
<td>43%</td>
<td>41%</td>
<td>40%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>20%</td>
<td>19%</td>
<td>14%</td>
<td>19%</td>
<td>15%</td>
<td>11%</td>
</tr>
<tr>
<td><strong>Clothing &amp; Footwear</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$26</td>
<td>$39</td>
<td>$41</td>
<td>$48</td>
<td>$64</td>
<td>$75</td>
<td>$86</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>8%</td>
<td>7%</td>
<td>6%</td>
<td>6%</td>
<td>6%</td>
<td>6%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>46%</td>
<td>6%</td>
<td>18%</td>
<td>31%</td>
<td>19%</td>
<td>14%</td>
</tr>
<tr>
<td><strong>Housing &amp; Fuels</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$55</td>
<td>$63</td>
<td>$80</td>
<td>$103</td>
<td>$127</td>
<td>$145</td>
<td>$160</td>
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<td>Percent of total expenditures</td>
<td>--</td>
<td>13%</td>
<td>13%</td>
<td>13%</td>
<td>13%</td>
<td>12%</td>
<td>11%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>15%</td>
<td>27%</td>
<td>29%</td>
<td>23%</td>
<td>15%</td>
<td>10%</td>
</tr>
<tr>
<td><strong>Household &amp; Cleaning Articles</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$26</td>
<td>$33</td>
<td>$36</td>
<td>$44</td>
<td>$53</td>
<td>$65</td>
<td>$74</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>7%</td>
<td>6%</td>
<td>6%</td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>30%</td>
<td>9%</td>
<td>23%</td>
<td>19%</td>
<td>24%</td>
<td>14%</td>
</tr>
<tr>
<td><strong>Health Care</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$25</td>
<td>$30</td>
<td>$32</td>
<td>$40</td>
<td>$49</td>
<td>$48</td>
<td>$58</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>6%</td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
<td>4%</td>
<td>4%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>23%</td>
<td>5%</td>
<td>27%</td>
<td>22%</td>
<td>-2%</td>
<td>20%</td>
</tr>
<tr>
<td><strong>Transport &amp; Communications</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$62</td>
<td>$84</td>
<td>$99</td>
<td>$121</td>
<td>$162</td>
<td>$201</td>
<td>$258</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>17%</td>
<td>16%</td>
<td>15%</td>
<td>16%</td>
<td>17%</td>
<td>18%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>35%</td>
<td>18%</td>
<td>22%</td>
<td>34%</td>
<td>24%</td>
<td>29%</td>
</tr>
<tr>
<td><strong>Education &amp; Recreation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$56</td>
<td>$58</td>
<td>$92</td>
<td>$107</td>
<td>$141</td>
<td>$174</td>
<td>$194</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>12%</td>
<td>15%</td>
<td>14%</td>
<td>14%</td>
<td>14%</td>
<td>14%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>5%</td>
<td>58%</td>
<td>17%</td>
<td>31%</td>
<td>23%</td>
<td>12%</td>
</tr>
<tr>
<td><strong>Personal Care</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$28</td>
<td>$37</td>
<td>$43</td>
<td>$57</td>
<td>$72</td>
<td>$85</td>
<td>$95</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
<td>7%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>30%</td>
<td>17%</td>
<td>32%</td>
<td>26%</td>
<td>18%</td>
<td>12%</td>
</tr>
<tr>
<td><strong>Transfer spending</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average expenditures in USD</td>
<td>$13</td>
<td>$25</td>
<td>$31</td>
<td>$32</td>
<td>$47</td>
<td>$71</td>
<td>$76</td>
</tr>
<tr>
<td>Percent of total expenditures</td>
<td>--</td>
<td>5%</td>
<td>5%</td>
<td>4%</td>
<td>5%</td>
<td>6%</td>
<td>5%</td>
</tr>
<tr>
<td>Percent change to next MW</td>
<td>--</td>
<td>98%</td>
<td>22%</td>
<td>4%</td>
<td>47%</td>
<td>50%</td>
<td>7%</td>
</tr>
</tbody>
</table>

beverage, and snuff category decreased the most as income levels increased. However, in terms of overall spending, expenditures per category increased, on average, around 21%.

Table 3 supplements Table 2 with some additional expenditure insights by listing the performance of some of the subcategories of the major expenditure categories measured by INEGI (2008) according to the MW 1-6 group. As seen in Table 3, under the food, beverage and snuff category, food and beverages consumed in the household accounted for approximately 90% of expenditures while snuff is responsible for only 1%. Under the transport and communication category, public transportation makes up 53% of all expenditures with this figure appearing to decrease as income levels increase. Also under this category, communications comprises 21% of expenses and appears to increase when moving up MW multiples.

Table 3. Subcategory Expenditures

<table>
<thead>
<tr>
<th>Category</th>
<th>1MW</th>
<th>1.5MW</th>
<th>2MW</th>
<th>3MW</th>
<th>4MW</th>
<th>5MW</th>
<th>6MW</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Food, Beverage &amp; Snuff</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Food &amp; Beverages Consumed in Household</td>
<td>95%</td>
<td>94%</td>
<td>91%</td>
<td>90%</td>
<td>88%</td>
<td>86%</td>
<td>86%</td>
</tr>
<tr>
<td>Snuff</td>
<td>1%</td>
<td>0%</td>
<td>1%</td>
<td>0%</td>
<td>1%</td>
<td>1%</td>
<td>1%</td>
</tr>
<tr>
<td><strong>Transport &amp; Communications</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Transportation</td>
<td>62%</td>
<td>56%</td>
<td>58%</td>
<td>56%</td>
<td>50%</td>
<td>45%</td>
<td>41%</td>
</tr>
<tr>
<td>Communications</td>
<td>18%</td>
<td>16%</td>
<td>19%</td>
<td>20%</td>
<td>23%</td>
<td>24%</td>
<td>25%</td>
</tr>
<tr>
<td><strong>Education &amp; Recreation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>83%</td>
<td>90%</td>
<td>90%</td>
<td>84%</td>
<td>83%</td>
<td>82%</td>
<td>76%</td>
</tr>
<tr>
<td><strong>Household &amp; Cleaning Articles</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electricity &amp; Fuels</td>
<td>69%</td>
<td>67%</td>
<td>68%</td>
<td>58%</td>
<td>58%</td>
<td>59%</td>
<td>59%</td>
</tr>
<tr>
<td>Gross Rent</td>
<td>22%</td>
<td>23%</td>
<td>22%</td>
<td>31%</td>
<td>31%</td>
<td>29%</td>
<td>28%</td>
</tr>
<tr>
<td>Water</td>
<td>9%</td>
<td>8%</td>
<td>8%</td>
<td>9%</td>
<td>10%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td><strong>Health Care</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prescriptions</td>
<td>38%</td>
<td>37%</td>
<td>35%</td>
<td>33%</td>
<td>29%</td>
<td>35%</td>
<td>32%</td>
</tr>
<tr>
<td>Health Insurance</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>2%</td>
<td>1%</td>
<td>1%</td>
</tr>
</tbody>
</table>

The third highest expenditure category, recreation and education (as noted in table 3), is comprised largely of expenditures going toward education (84%). Additional subcategories of interest fall under INEGI’s main categories of household and cleaning articles and health care. Under household and cleaning articles, electricity and fuels appear to make up 63% of all expenditures and decrease with an increase in MW multiple. Further, under this category are gross rent accounting for 27% of expenditures and water, comprising 9%. Finally, under health care, 34% of expenditures are towards prescription drugs and only 1% toward health insurance with the MW multiples 1-3 showing health insurance expenditures of closer to 0%. This is not surprising given that most insurance products are out of reach for many low income households, an issue the following chapter will discuss in greater depth.

**DISCUSSION OF FINDINGS**

The findings of this chapter indicate that Mexico and its BOP share many of the same characteristics as those present in other developing countries and their BOPs throughout the globe. In the country overall, these include aspects like high incidences of urbanization, over burdensome regulatory environments, high levels of inequality and poverty and large informal economies, gaps in infrastructure, especially in the areas where many of the poor tend to reside widespread corruption, and lack of transparency with government officials. Further, at the BOP, the poor are often characterized by low levels education, unpredictable income streams, and limited access to credit and basic services. Although it is true that the country’s economy has been growing and improving per capita income levels for all income segments throughout the years (INEGI, 2008), the high levels of inequality have contributed to keeping nearly half the population at the BOP.

The informal sector, marginalization factors, and the wide diversity characterizing the country’s BOP in terms of geography, climate, people, communities, cultures, customs, and poverty experiences all work together to influence the specific needs, limitations and capabilities that differ from region to region and even neighborhood to neighborhood throughout Mexico. Though poverty is widespread throughout Mexico, there are regions that seem to struggle worse than others in regard to income distribution and/or in the achievement of greater levels of social equity. For example, according to the findings in this chapter, Mexico’s central and southern regions tend to experience the greatest levels and
concentrations of poor people and social deprivation. In regards to urban poverty and social deprivation, it was found that, in terms of percentage of the population, social deprivation levels appear to increase as city sizes decrease. Further, regional affects seem to play a significant role in terms of how many urban areas per region are likely to experience high or low levels of social deprivation.

Finally, the expenditure figures from Mexico’s BOP segment appear to contribute to the recent claims that even the poor are economic beings and that there are both money and spending strategies in play at the BOP. However, there are various levels of income, experiences of poverty and thus capabilities within Mexico’s BOP. Although Mexico has a greater quantity and quality of information available for gleaning insights from BOPs as potential target markets, the data is imperfect and can serve, at best as a jumping off point for firms interested in identifying markets, needs, opportunities and challenges. Further, all the traditional deterrents for companies regarding EMs and BOPs apply and though there certainly seems to be for potential firms to find new markets in Mexico’s BOP, the extreme diversity in regards to the people and the places they reside; the subtleties of their informal environments; and their harder to reach aspects in terms of distribution, communications, and credit will absolutely require committed, creative, efficient and innovative solutions from firms that wish to access them successfully and survive into the long-term.

Given the fact that BOPs appear to represent fundamentally different and very sensitive markets with different needs and demands and very little in the way of market research, academics have begun to argue that MNCs may need to rethink business models fundamentally to develop small-scale, locally-driven, scalable strategies (Hart & Milstein, 2003; London & Hart, 2004; Prahalad, 2006; WBCSD, 2004). For instance, because informal markets are regulated by informal rules, social contracts, and shared use of assets (De Soto, 2000), Autio, Sapienza and Almeida (2000) believe entry strategies may require greater inclusiveness and less reliance on protecting knowledge and technology, strategies that may be counterintuitive to subsidiary managers. Furthermore, given the low-income levels of this consumer group, according to Prahalad (2006), firms will need strategies capable of leveraging low margins by achieving high volume. The following chapter will review the strategy literature to see what kinds of insights are available for informing firms on how to best proceed into BOPs.
CHAPTER 4
THE EVOLUTION OF STRATEGY FOR BOP MARKETS

The modern multinational enterprise (MNE), hailing largely from the relatively rich and technologically advanced developed countries of Britain, North America, continental Europe, though diverse in the variations of their strategies and MNE structures (Stopford & Wells, 1972), have been found to frequently share a core set of features that include technological, marketing and managerial strengths (Guillen & Garcia-Canal, 2009). Over time as experience in international markets grew and strategies were refined, much of the work on global strategy, as seen in Prahalad and Doz (1987) and Bartlett and Ghoshal (1989), found that most MNE strategies could be classified based on the their responses to the needs for local responsiveness and globalization.

Defined by Hodgetts, Luthans and Doh (2005) national responsiveness is “the need to understand different consumer tastes in segmented regional markets and to respond to different national standards and regulations imposed by autonomous governments and agencies” (p. 242). According to Hodgetts et al. (2005), the term also relates to the need for firms to adapt tools and techniques for managing the local workforce, as sometimes what works well in one country does not in another. Globalization, on the other hand, is described by Hodgetts et al. (2005) as “the production and distribution of products and services of a homogenous type and quality on a worldwide basis” (p. 242), and is used by MNCs in an attempt to exploit economic efficiencies through economies of scale (Doz, 1980).

Bartlett and Ghoshal (1989) found that MNEs were clustering around four distinct patterns with regard to strategy, structure, and managerial processes that seemed to be responding, at different levels, to these demands for globalization and local responsiveness. Operating from this conceptualization stream, the global literature includes topics such as the control and coordination of national subsidiaries, the level of integration across national subsidiaries, and the balance between global headquarters control and autonomy of national subsidiaries (Gates & Egelhoff, 1986; Martinez & Jarillo, 1989; Paterson & Brock, 2002).
Bartlett and Ghoshal (1989, 1998), whose findings have since been confirmed by more empirical studies (Harzing, 2000; Leong & Tan, 1993), suggested firms fell into one of the following four categories: global, multi-domestic, international, and transnational, with the appropriateness of each strategy depending on pressures on the firm for cost reduction and local responsiveness in each country served.

For instance, as observed by Hodgetts et al. (2005), the global strategy is a low-cost strategy used by firms that experience high cost pressures and low demand for localized product offerings and usually involves mergers and acquisitions. Further, due to the high emphasis on the cost advantages of integration, all strategic functions are centralized at a worldwide headquarters (Arthaud-Day, 2005). The strategy is based on the assumption of the presence of a global market segment with a high degree of common interest, whose consumers the firm attempts to satisfy by offering a standardized product worldwide while leveraging its experience to create aggressive pricing schemes and benefit from scale economies in production, distribution and marketing (Hodgetts et al., 2005).

The opposite scenario is represented by the multi-domestic strategy, where the need for differentiation is high but the concern for integration is low (Bartlett & Ghoshal 1989, 1998). Here, Hodgetts et al. (2005) note, niche companies, especially those of the consumer packaged goods type, adapt products to satisfy the high demands of differentiation and ignore economies of scale because integration is not very important. Because margins are high enough that scale is not an issue, companies are able to develop an extreme sensitivity to the local environment, allowing them to modify their products, marketing, and managerial practices accordingly (Arthaud-Day, 2005). Although such an approach is a little more expensive than the global strategy, it often results in a high degree of localized knowledge and decision-making power that increases the likelihood that its products and services will be responsive to local needs and will therefore be successful.

In the case of the international firm, neither the potential to obtain economies of scale nor the benefits of being sensitive to differentiation are of great value (Bartlett & Ghoshal, 1989, 1998). Firms that pursue an international strategy have valuable core competencies that host-country competitors do not possess and face minimal pressures for local responsiveness.

In the 1980’s a new trend started to emerge. Although industries varied significantly with regard to which balance of globalization and local integration they chose, according to
Ricart et al. (2004), technological change was bringing convergence in tastes, customs, and products but implementation was still requiring some degree of localization to respond to local needs and cultures, as well as to benefit from local advantages. As MNC reach increased into new countries, traditionally global companies were being forced to diversify while typically multi-domestic firms were increasingly discovering the advantages of standard brands and common promotional campaigns (Bartlett & Ghoshal, 1998).

Responding to this seeming convergence, Bartlett and Ghoshal (1989, 1998) argued that complexities in the current international environment coupled with MNCs continuing need for scale demanded a new “transnational” mentality that could simultaneously address the strong needs for both globalization and national responsiveness. Although globalization and national responsiveness represent two fundamentally opposing approaches, Bartlett and Ghoshal (1998) maintained the strategy was feasible because customer needs were growing more homogeneous throughout the world and, as a result, efforts for duplicating firm manufacturing and product development in each national market were no longer necessary. Instead, firms could leverage their capabilities across borders in order to achieve global economies, respond to local markets, and transfer best practices (Quelch & Bloom, 1996).

The transnational strategy appealed to many firms as means of both rationalizing costs and increasing control over far-flung overseas subsidiaries, according to Quelch and Bloom (1996). Firms that adopted the transnational strategy began rooting out entrenched country managers whose local autonomy often resulted in blocking headquarters’ efforts toward standardization, regional consolidation, and the like (Quelch & Bloom, 1996). Geographic power began to give way to worldwide strategic business units or product directors operating from central headquarters and the transnational model, though the most complex and expensive to implement, became the preferred model among many MNCs, at least, claim Quelch and Bloom (1996), until the 1990’s when emerging markets began to reveal some serious weaknesses in the strategy.

EMERGING MARKETS AND THE LIMITATIONS OF GLOBAL STRATEGY

With the fall of communism in the late 1980’s, transition economies began to open their markets to foreign investment (Hoskisson, Eden, Lua & Wright, 2000). For the first time, MNCs began to view developing countries anew, seeing beyond the cheap labor to the
potential new markets for goods and services, and academic work on emerging market
strategy began to experience rapid growth as firms looked for the best ways to proceed
(Ricart et al., 2004). London and Hart (2004) noted that initially scholars assured firms that
when pursuing the more affluent TOP markets in EMs, MNCs could rely on the proven
global capabilities they had honed in the developed markets of the United States and Europe
to incrementally adapt their existing business models and familiar subsidiary strategies based
on controlling resources, extracting knowledge and leveraging economies of scale and scope.
Other authors like Buckley and Casson (1991) insisted that modifying (national
responsiveness), leveraging (global efficiency), or sharing (worldwide learning) existing
products or resources within firm boundaries would allow MNCs to overcome liabilities of
foreignness in serving the wealthy TOP as had always been the case in the past.

However, as firms expanded into EMs, they were met with mixed success and new
realizations about the markets they had entered, especially in regard to the fewer than
anticipated middle-class consumers (Ricart et al., 2004), the unfamiliarity of the markets, and
consumer tastes. So challenging were the new markets that the one study done assessing the
first-mover advantage in EMs (Marketing Science Institute, 1995), found that the conditions
present in EMs actually served to negate any potential advantages that might be gained from
being a first mover and strongly suggested that companies should instead assume a wait and
see approach. For instance, according to Quelch and Bloom (1996), even the transnational
strategy, which had promised the perfect balance, seldom worked well in expanding or
emerging markets. Quelch and Bloom claim the difficulties of the strategy were a result of its
emphasis on HQ-oriented product managers in a market where local insights and cultural
sensitivities were desperately needed. In practice, the author noted, people in the field were
told to be creative about satisfying local customers’ needs with increasingly standardized
products, over whose design and marketing they had little influence. Further, the motives for
organizational realignment, which were supposed to be based on improving customer value,
were increasingly replaced by pressures for cost reduction and tightening central control
(Quelch & Bloom, 1996).

Although the study and the general sentiment of many firms and academics has been
that the impossible environments of EMs were to blame for firm failures, the recent
emergence of the New MNE--corporations that originated in and learned to thrive first in
emerging and transition economies and were then able to expand into developing and developed markets simultaneously, gaining huge advantages over traditional firms, whose experiences, limited to developed markets, put them on a more simple expansion path (Guillen & Garcia-Canal, 2009)--and new findings by BOP researchers suggest that the real fault may lie more with the incorrect assumptions made about EM markets and consumers and the flawed strategies that followed. Additionally, researchers like Arnold and Quelch (1998) asserted that and that those companies that get strategies right in EMs stand to gain significant first-mover advantages in terms of valuable learning and reputational benefits.

Two major assumptions that have greatly impacted the literature on EM and Global strategy are (a) that TOP markets in EMs are large and the only ones with market potential, and (b) that developing countries are simply in an earlier phase of development than developed nations and will thus follow predictable phases and behaviors as they eventually evolved into a setting more familiar to Western managers. The following sections explore the consequences of these assumptions and how they inform strategies for the BOP.

Rethinking Market Evolution Assumptions

Peng and Luo (2001) found that most of the research by management scholars on firm strategies in EMs suffers from a pre-occupation with strategies that seek to overcome the lack of a Western-style business environment. As a result, firms have often based demand predictions on such assumptions and looked to create short-term strategies to overcome limitations while waiting for the economic setting to evolve (London & Hart, 2004). For instance, London and Hart (2004) noted, to address the concerns of MNCs accustomed to creating competitive advantage through patents, brands, and contracts in regards to entering markets where their proprietary technology and knowledge cannot be protected through enforceable legal mechanisms, researchers have explored how MNC managers can successfully implement strategies that help to overcome the lack of legal boundaries and difficulties in property rights. As noted by Dunning (1988) and Khanna and Rivkin (2001), firms design boundaries to protect internal resources and capabilities from unintended spillover, and look for partner organizations that wield substantial capability to fill voids in the business environment (as cited in London & Hart, 2004). As evidence, London and Hart (2004) discussed various suggestions found in the literature regarding how firms can address
gaps in the business environment, including Beamish (1987) and Hitt et al. (2000) who study forming alliances; Khanna and Rivkin (2001) who emphasize forming networks; Peng and Luo (2001) who recommend using interpersonal ties; Delios and Henisz (2000) who discuss the importance of managing firm boundaries; and Hoskisson et al. (2000) who stress the need for institutional capacity building to address the lack of well defined property rights.

The problem with the Westernization assumption, as noted by De Soto (2000), is that although it may be argued that the wealthiest fraction of the population in emerging economies is evolving toward a more Western-style (or modern) business environment, the vast majority of the people continue to be on the outside looking in. The reality, as discussed earlier in the thesis, is that developing countries are generally characterized by dual economies and thus, as noted by London and Hart (2004), firms must understand that there are at least two different and important patterns of economic development occurring in most EMs that may or may not evolve into an economic setting where legal contracts supersede social ones and where competitive advantage is grounded in the ability to protect resources and knowledge from unintended leakage outside firm boundaries.

**Misguided Market Understandings**

According to London and Hart (2004), one of the biggest challenges for firms is to find differences and similarities in locations that can be leveraged across multiple countries while adapting to local differences as needed. Strategies in the literature that have attempted to address this are geographic clustering (Moskowitz & Rabino, 1994; Oyewole, 1998); and looking for segments that transcend national and cultural boundaries (Hassan & Kaynak, 1994); as well as the more integrated approaches such as the CAGE framework (Ghemawat, 2007), which measures the cultural, administrative, political, institutional, geographic, and economic dimensions of differences across countries. However, although these strategies provide valuable tools for MNCs in regards to between-country differences, London and Hart (2004) pointed out that they fail to account for within-country variations, especially with regard to distinctions between BOPs and TOPs. For example, Hassan and Kaynak (1994) start to offer insights in this area but limit their segmenting to TOP consumers only, such as the global teenager. London and Hart assert that MNCs should consider that there are at least two distinct market environments (the aforementioned TOP and the BOP markets) worthy of
firm consideration for which very different strategies may be necessary and note that firms that design strategies that seek to overcome limitations in the short-term may find themselves at a great disadvantage over the long-run.

Such gaps in the literature reveal an important limitation present for firms seeking advice for how to proceed into BOPs and although the literature on strategies for EMs is growing, except for a small group of BOP focused IB researchers like Prahalad (2006), Mahajan and Banga (2006), and Prahalad and Hart (2002), most academics have yet to be convinced of the need for bothering with strategies that recognize in-country differences and are specifically designed to address the markets found at the BOP. As noted by Prahalad and Hart (2002), there is little in the way of theory or research in the area of IB that provides clear guidance on how to pursue EMs and an even more serious gap when it comes to global capabilities and business strategy at the BOP, which, London and Hart (2004) say, “highlights an important and increasingly untenable discontinuity between MNC practices and academic research” (p. 7).

RETHINKING IB STRATEGY: GLOBALIZATION, ANTI-GLOBALIZATION, SOCIAL RESPONSIBILITY AND SPILOVERS

According to Ricart et al. (2004), in recent years many forces have combined to change the face of international business and resulted in a rethinking of IB strategy. To illustrate their point, the authors listed several of the contributing factors to include the expansion of global finance and financial markets, the spread of knowledge facilitated by improved communication, the widespread availability and use of technology, the active expansion of MNCs, the decoupling and decentralization of economic activities within and between firms, the blurring of the nationality of multinationals, the reductions of barriers to trade and investment, the emergence of regions and regional identities that transcend borders, and more recently the rise of electronic communities over the internet, not to mention the fact that nations accounting for nearly one-half of the world’s population have either entered or have dramatically changed their relationship to the world economy. However, in the midst of all this, noted by Wright (1984) is the persistence of neocolonialism sensitivities in EMs, best described as the perceived penetration of a third-world country by a multinational corporation that, according to Berger (1974), “results in a distortion of the economy in the
sense that it develops not in terms of international economic and social forces, but in the interest of the foreign metropolis” (as cited in Wright, 1984, p.231).

Prahalad and Lieberthal (1998) added to the observations by Wright (1984) noting that MNC strategies aimed at tailoring existing products to fit the needs of the elites and rising middle classes in the developing world have inadvertently resulted in a form of “corporate imperialism” as the incremental design changes and cost reductions associated with this strategy have not succeeded in making products and services available to the mass markets in the developing world. The stark reality, noted by Ricart et al. (2004) is that currently about four to five billion people living around the world have been largely bypassed or even damaged by globalization and given the current sensitivities and often legitimate mistrust of big businesses, if corporate expansion is seen to come at the expense of the poor and the environment, it will encounter vigorous resistance. In support of these claims, WBCSD and The Prince of Wales International Business Leader’s Forum [IBLF] (2004) found two interesting trends facing firms today. First, in the wake of corporate governance scandals and public concern over accounting failures, conflicts of interest, and inadequate market oversight, there is a massive pressure on businesses to rebuild public trust and to restore confidence in the private sector; and second, in the face of high levels of international insecurity and poverty, the backlash against globalization, and mistrust of big business, companies are being asked to deliver wider societal value and to show that globalization is inclusive and that markets can work for all (WBCSD & IBLF, 2004).

Unfortunately, due largely to the fact that most of the research and therefore the resulting dominant business logic has been on how to run businesses better-in terms of profits, not as socially responsible citizens (Meyer, 2004), strategies for firms on how to deliver wider societal value are sparse. Although arguably the prime experts on MNEs, Meyer (2004) lamented that IB scholars have contributed relatively little to explaining and evaluating the role of MNEs in society and noted that FDI impact literature had paid scant attention to the diversity of business strategies that influence the type and extent of spillovers. This becomes even more of an issue when considering Rodrik (1999) and Meyer’s (2004) review of the empirical literature that found that despite the extravagant claims in the policy literature on positive spillovers from FDI, firms did not have strong track records in this area. Currently, few studies on the impact of FDI consider more recent developments in
strategic management research, such as the resource-based view, organizational learning
theories, and institutional perspectives (Meyer, 2004). The United Nations Educational,
Scientific and Cultural Organization [UNESCO] (2000) added that assessments of the
variations of long-term impact from different modes of entry lacked strong empirical
evidence (as cited in Meyer, 2004) and Meyer asserted that the literature on the long-term
implications of different methods of privatization in emerging economies lacked such
empirical strengths as well.

Such gaps in the literature could prove costly for firms as recent EM and BOP
research seem to suggest that insights into the potential positive and negative spillovers of
firms and how they impact communities are crucial insights for firms seeking to create
competitive advantages and successful strategies. For instance, Meyer (2004) asserted that
positive spillovers help build a company’s reputation as an actor concerned for its
stakeholders while Brugman and Prahalad (2007) demonstrated how negative spillovers risk
triggering adverse reactions from stakeholders such as local politicians concerned about
employment, and consumers and non-governmental organizations (NGOs) concerned about
ethics. Recognizing both complementary and conflicting interest can go a long way to help
firms during the negotiation process to identify strategies that benefit both MNEs and
stakeholders in host economies. Further, because developing country economies often have
less sophisticated market supporting institutions and fewer locational advantages based on
created assets, such as infrastructure and human capital (Hoskisson et al., 2000; Narula &
Dunning, 2000), knowing how MNEs may contribute to development is useful for policy
makers and managers alike (Meyer, 2004).

Brugman and Prahalad (2007) confirm that early MNE entrants in the BOP faced
numerous challenges from NGOs. According to the authors, though the relationship between
the two organizations began with the two fighting each other on every point, it had recently
begun to evolve as the two recognized the need to and the benefits of learning to co-exist.
According to Brugman and Prahalad (2007), smart firms at the BOP began to realize that
proactive strategies toward the incorporation of social responsibility would be much less
expensive than the millions they might lose in future defensive measures against NGO
lawsuits and bad publicity effects and decided to take their cases directly to consumers
through implementation initiatives like CSR, voluntary self-regulation schemes, cause-based marketing and more recently, public-interest-cum-advertising campaigns.

Lacking useful advice from the strategy literature on how to create effective CSR initiatives, firms compensated by hiring people from the social sector who had networks, credibility, and an understanding of NGOs that they could bring into corporations (Brugman & Prahalad, 2007). Discussing CSR initiatives, Brugman and Prahalad (2007) noted that what began as a way for companies to gather intelligence about NGOs and manage their reputations became a catchall phrase for the ways by which businesses managed reputations and struck relationships with the social sector. However, an important drawback is that although CSR initiatives usually use their resources to work on socially relevant issues, as they are defined by NGOs, most of these efforts are unrelated to the companies’ core business activities and have been argued to be unsustainable (see White, 2005 for pros and cons of CSR). The major argument is that CSR strategies do not necessarily create sustainable opportunities for the poor to rise out of poverty that would lead to sustainable market development and because they are unrelated to core business activities, they are unsustainable for the firm as well. In short, CSR initiatives act as short-term strategies that may boost a firm’s reputation and prevent community push-back in the short-run, but are incapable of being sustained, distract from the firm’s core activities, and do not contribute to developing markets that firms could benefit from in the long-run.

**RECENT BOP RESEARCH**

Some of the greatest challenges firms face in BOP markets deal with obtaining reliable market data; creating strategies that incorporate income restraints and demands for low cost, high quality products; creating value chain solutions for distribution, marketing, and sales; finding appropriate and capable partners; achieving scale while also dealing with social responsibility pressures in the various communities they work in; dealing with a lack of familiar markets, new market challenges, and rule-of-law issues; and creating and leveraging competitive advantages, entry-strategies and long-term strategies. To succeed in BOP settings, firms need solutions that allow them the flexibility and insights to address local conditions at the community level (Arnold & Quelch, 1998), such as accommodating different local ways of doing business (Rangaan & Rajan, 2005), and are capable of
achieving a certain level of standardization to facilitate scale over local, national and (ideally) global markets (Prahalad, 2006). The following sections discuss insights from the literature specifically geared toward addressing these challenges and include some actionable strategies, proposed approaches to the BOP, characteristics common to successful BOP ventures, and newly emerging BOP business models.

**Some Actionable Strategies**

In the absence of reliable market information, accessing context-specific information is crucial to entry and to long-term success in ever changing BOP environments. Without a broad understanding of the lives and needs of individuals living in BOP environments, product and market development on a sustainable basis is not likely to be successful (Viswanathan, 2007). Thus, Viswanathan et al. (2008) asserted, at the very least, firms should begin their approach to the BOP by developing a deep understanding of the lives of the individuals living in BOP subsistence conditions. By approaching the BOP in this manner firms would pave the way for a bottom-up, grounded understanding of the potential for businesses to contribute to economic and social development among the poor (Viswanathan et al., 2008) and give firms the best chance of creating viable and sustainable products and business models.

According to Viswanathan et al. (2008), firms seeking to better understand BOP consumers must learn to see them as both producers and consumers. Further, to develop appropriate business strategies, firms must seek to understand the interplay and complex trade-offs between needs, products, markets, and finances at the BOP (Viswanathan, 2007). For example, Viswanathan et al. (2008) explained, the relationship between buyers and sellers in subsistence economies extends well beyond the marketplace roles to the point that economic exchange becomes an extension of everyday personal interaction, rather than being divorced from it. Social relationships should then be understood as a community-owned resource that might be harnessed to add value for the community through market exchanges (Viswanathan et al., 2008).

Suggestions for how reliable market research data can be obtained can be found in works by authors like Fletcher and Chikweche (2009), who offered compelling evidence that the consumer decision models currently used by firms in TOP markets may need to be
replaced by a model better suited for the realities of the BOP, and provided some useful insights and starting points for doing so. Additionally, insights can be found in Viswanathan et al. (2008) who suggested that to conduct effective market research and design successful products, firms would need to treat subsistence environments not just as markets, but as individuals and communities from which to learn. Further, Arnold and Quelch (1998) encouraged firms to come up with creative, customized approaches, citing examples like those used by Citi-Bank and Mary Kay that found ways of obtaining important and relevant information indirectly when direct sources were unavailable or unreliable. Finally, Prahalad (2006) and London and Hart (2004), findings suggested that co-creation of products and/or processes with NGO partners or BOP consumers provided the right set of characteristics for obtaining intimate market insights directly.

According to Mahajan and Banga (2006) and Prahalad (2006), to seize opportunities at the BOP, firms need different mindsets and market strategies. The BOP, these authors assert, need managers who can envision creating a business of selling sachets of shampoo for pennies, distributing products in stores the size of phone booths, or offering credit cards to people whose idea of banking is storing rolls of coins in a money belt. Currently firms at the BOP are experimenting with a variety of strategies for product development and design, pricing, packaging, distribution, and marketing as can be seen in the numerous case studies presented in the works of Prahalad (2006), Mahajan and Banga (2006), and WBCSD (2004). For example, one firm dealing in construction materials, discussed in WBCSD (2004), began offering mobile sales where two trucks stocked with over 50 items were sent into poor neighborhoods to visit the smallest plumbing and home repair storefront shops to give them the opportunity to buy, invoice, ship and deliver all in one single transaction. By cutting out the middleman, the small customer was able to avoid keeping large inventories, replenish only what was needed, and pay cash at a fair price to the retailer that also returns a profit to the supplier. Other firms have realized the value of the women in communities and have recruited and trained individuals from local self-help groups to act as spokeswomen, saleswomen, distributers, and even microloan administrators (Prahalad, 2006; WBCSD, 2004). Though several major MNCs such as Procter & Gamble, Johnson & Johnson, Hewlett-Packard, and Dupont have become members of the WBCSD in an effort to glean
insights on the BOP toward the development of more effective strategies, as of yet there does not appear to be any particular strategy being preferred by these firms over another.

According to Viswanathan (2007), BOP markets are characterized by a unique mix of the old (with products and markets that individuals interact with) and the new (with products like cell phones that leap frog the need for landlines in infrastructure poor regions). Viswanathan further stated that the BOP was not the realm of one size fits all and warned that it was important to understand the interplay and complex trade-offs between needs, products, markets, and finances that influence consumer’s purchase, product, and choice of retailer decisions. For example, Viswanathan (2007) suggested that distribution strategies should be designed taking into account the local dynamics in a variety of urban neighborhoods and rural areas, each with its own characteristics; product design should take into consideration how a number of variables interact with one another in settings characterized for the customer by uncertainty and lack of control (see The Annapura Salt Story case study in Prahalad, 2006, p. 213, for additional insights); promotional efforts should understand the significance of word of mouth and the one-to-one interactions that characterized the BOP marketplace and be designed with the full understanding of the nuances of subsistence contexts in terms of the knowledge that customers possess; and pricing should be guided by what BOP consumers could afford to pay as well as a willingness to pay more for acceptable quality, particularly for such core products as staple food.

**Approaching the BOP Inclusively, the Strategy Potential beyond CSR**

In 2004 C.K. Prahalad, in his book *The Fortune at the Bottom of the Pyramid* (now in its 5th edition) began to argue that firms that wanted to access the BOP should create inclusive, co-created solutions with non-traditional partners and focus on entire ecosystems, or the symbiotic nature of the relationships, rather than only one aspect of them (like SMEs or individual entrepreneurs) for wealth creation and social development at the BOP. Prahalad (2006) and other BOP researchers believed there was much to be gained by working together with multiple partners from various private sector, civil society organizations, governments, international aid organizations and local civil servants towards poverty alleviation and market development and emphasizes the need for MNEs to radically change their approach
and to fundamentally rethink every step in their supply chain to create BOP appropriate products/services and models that are affordable and accessible to BOP market consumers. Commenting on the limitations of CSR initiatives used by many MNEs and the findings of the report, SNV and the Inter-American Development Bank [IDB] (2008) suggest that CSR policies should instead be leveraged to motivate firms to upgrade their business models so that they are strategic and sustainable. In this sense, the report noted, there was an opportunity “to disseminate inclusive business models with a medium- to long-term perspective for generating benefits and to demonstrate that the initial marginal costs associated with working with BOPs represent an investment that generates returns in the medium and/or long term” (p. 20).

It is this end goal that motivates the assertions of Prahalad (2006), Simanis and Hart (2009), and WBCSD (2005) who all promote sustainable, long-term focused models that not only create solutions for BOP consumers but also incorporates the poor into actual business models so that CSR becomes a part of the business itself. As explained by WBCSD (2005), the recommended model is a blended values approach (blending social and financial values to create mutually beneficial solutions that are distinct from charity or philanthropy). These inclusive businesses—“also termed bottom of the pyramid (BOP), pro-poor, or sustainable livelihoods business—refer to doing business with the poor in ways that simultaneously benefit low-income communities and also benefit the company engaged in this initiative” (WBCSD, 2005, p.14). It is strictly business, new business and new markets, business that benefits the poor and benefits the company. “These innovative business models focus on fostering economic development and helping low-income families build more secure livelihoods, while creating new markets for companies and are about ‘doing well by doing good’” (WBCSD, 2005, p.14).

**Characteristics of Successful BOP Ventures**

Up to 2004, in the absence of any BOP specific empirical studies, most BOP suggestions and theories had been based largely on learning from numerous case studies. In an attempt to address this gap, London and Hart (2004) conducted a qualitative empirical study examining twenty-four companies that were or had been attempting to reach the BOP. From the study, the authors discovered several important emerging factors that were present
in successful initiatives and missing in those that failed or performed poorly in BOP markets. According to the study, companies that found the most success relied heavily on the use of non-traditional partners; co-creation (or the co-invention of solutions with BOP partners or consumers); and the building of local capacity into their business models, while those businesses that had failed or performed poorly had focused on using traditional models and approaches to pricing, value propositions etc, and failed to incorporate the three aforementioned characteristics seen in successful models. For example, London and Hart (2004) noted that failed or poorly performing firms often had a heavy reliance on the expertise of local subsidiaries or familiar TOP partners, had limited or no contact with non-profit or other non-traditional partners, preferred to sell their products as is and tried to limit modifications by distributers and users, made substantial efforts to protect property rights (e.g., patents, brand names), tended to view value proposition in terms of the product, not functionality, tended to view the environment in terms of the institutions that were missing (instead of see the value of the existing ones), and limited contact with local entrepreneurs and local institutions.

London and Hart’s (2004) findings support Meyer’s (2004) emphasis on the importance of understanding spillovers, noting that successful MNEs appeared to encompass an additional capability of “social embeddedness,” or, as the authors explain it, “the ability to create competitive advantage based on a deep understanding of and integration with the local environment. Regarding the social embeddedness capability, London and Hart (2004) observed that “ rather than looking to overcome weakness this capability is based on the ability to craft a strategy that relies on resources and knowledge in the external environment as sources of competitive advantage” (p. 15). Further, London and Hart (2004) added, “it involves the ability to create a web of trusted connections with a diversity of organizations and institutions, generate bottom-up development, and understand, leverage, and build on the existing social infrastructure” (p. 15). The following sections examine some of the existing literature on the three elements found by London and Hart to be key characteristics of successful business models: the use of non-traditional partners, co-creation, and capacity building.
NON-TRADITIONAL PARTNERS

According to Prahalad (2006), London and Hart (2004), and the experiences of several firms currently in the BOP (WBCSD, 2004), partners normally chosen for the TOP markets of EMs may be inappropriate for BOPs, as many have little experience or networks in lower-income sectors. Though the BOP literature emphasizes the importance of building relationships with multiple partners and sectors, the main focus in the literature is in reference to those of the MNE-NGO. For instance, to help facilitate MNEs with finding adequate NGO or non-profit partners at the BOP, WBCSD and IBLF (2004) put out a Business Guide to Development Actors that introduces the different types of development organizations (multilaterals, bilaterals, and NGOs) and provides information on various organizations under each category for firm reference. In addition, Brugman and Prahalad (2007) and WBCSD (2004) contributed works with guidance to firms on finding common ground and managing these partnerships.

The literature on non-traditional partners, also known as public-private partnerships (PPPs), covers a diverse range of topics including how firms and organizations work to sustain the partnerships, which processes and mechanisms they establish to plan, implement, and monitor collaborative action, how they can effectively create a shared vision between two very different organizations, how to identify appropriate partners, promote accountability etc (Bazzoli et al., 1997). Additionally, because the research and the understanding of how to form, manage, and protect the interests of the organizations as well as the communities they work with is still underdeveloped, there is also a significant amount of discourse on the subject both from those in favor and those opposed to the marrying of the public with the private.

The main argument in the BOP literature in support of NGO partnerships says that while firms are realizing their need for insights, relationships and new business models for proceeding into BOPs, are seeing the value of working with local organizations, NGOs, facing declines in worldwide spending on social programs, are beginning to see the value of entrepreneurship for poverty alleviation in addition to charity and aid, creating fertile ground for firms and NGOs to begin working together in a mutually beneficial manner (Brugman & Prahalad, 2007). BOP authors like Brugman and Prahalad (2007) argue that MNEs have the financial, technical and experiential know-how that NGOs need to grow and increase their
reach while NGOs often possess the knowledge, local infrastructure, and relationships firms need. For instance, the authors point out that there are NGOs that have already created large distribution networks capable of furnishing food, medicine, and credit, especially in remote areas. Additionally, many NGOs have developed a deep understanding of local cultures, established credibility and earned people’s trust by repeatedly assisting disadvantaged communities in the face of poverty, natural disasters and conflicts (Brugman & Prahalad, 2007). For many of these same reasons, a smattering of authors such as Budinich, Manno-Reott, and Schmidt (2007) and Seelos and Mair (2007) suggest that social entrepreneurs at the BOP may also make natural partners for MNEs (see Seelos & Mair, 2005, for additional insights on social entrepreneurs).

On the flipside, those in opposition to PPPs argue that by allying themselves with private sector firms, that represent opposing interests, NGOs may face institutional capture by its more powerful partners and jeopardize its control over guidelines and procedures and derail its mission to help all those in need in favor of reaching those easier to reach thus further displacing the marginalized and endangering the reputation of the organization itself (World Health Organization [WHO], 2001). The one thing the literature on PPPs appears to agree on is that there is still much that is not understood about these relationships and how they are managed, governed, united, or kept accountable and balanced. Thus, there is much research that still needs to be done and most likely a lot of trial and error that will occur as organizations try to get it all figured out.

While some critics of PPPs argue over the appropriate role of the state and public institutions in society as a basis for how they feel about PPPs, such as those discussed by Wettenhall (2003), others like Bovaird (2004) are more concerned with making sure the necessary precautions in terms of good governance are taken to ensure a smoother working relationship, accountability, and protection for all involved. As noted by Haque (1996a, 1996b, 1998), for the dangers involved with PPPs to be overcome, designers of such partnerships must ensure that regardless of whether public sectors are big or small, issues of public policy and public interest are not altogether submerged by the demands of the market (as cited in Wettenhall, 2003). Public service legitimacy, public ethics, and public service motivation, Wettenhall (2003) noted, must all be defended and strengthened, so that the public sector can hold its own in all its new intersections with the private sector.
**Capacity Building**

London and Hart (2004) contrast their findings to the perspective emphasized by the transnational model and find that unlike the transnational strategy, which, according to Buckley and Casson (1991), focuses on sharing resources internally and maximizing the economic benefits to the firm, London and Hart’s findings suggest that firms at the BOP must also consider both societal performance and the sharing of resources outside firm boundaries or “local capacity building” to be successful. London and Hart (2004) found that many firms were accounting for societal performance by incorporating local capacity building directly into their business models rather than using the conventional approach of corporate philanthropy which treats capacity building as an activity separate from the business. Through this strategy, firms were able to develop both individuals and existing institutions in a mutually beneficial way.

The WBCSD and SNV (2007) report noted that the limitations of many local SMEs often precluded them from joining MNE value chains. Yet, despite their limitations, the report argued, established SMEs may have valuable insights and capabilities that warrant a little MNE investment to bring them up to speed. For instance, the report noted, many established SMEs often have extensive knowledge of resources, supply patterns and purchasing trends, as well as competitive strategies and insights developed while learning to work in BOP environments, flat management structures that allow them to be more flexible and less vulnerable to economic downturns, insights into how to re-engineer products or services to meet market demands, innovative distribution and/or sales techniques, a vested interest in community development, experience drawing from the community for their workforce, and skills in providing needed products and services at prices consumers can afford.

Given the potential gains and the significance of societal performance by firms in BOPs, researchers argue that efforts to develop local SMEs should be seen as investment strategies both for market development in general and for creating viable business partners who, in return, can provide the needed local insights and social networks. WBCSD and SNV (2007) emphasizes the differences a little investment in basic skills training in areas such as management, bookkeeping, business planning, marketing, distribution, and quality control, as
well as assistance through technology transfers, direct investment in infrastructure, and the sharing of knowledge, can make in creating more competitive reliable value chain partners.

**CO-CREATION**

Chambers (1997) noted that assessing context-specific information appeared to require a more participatory approach in which all parties needed to be willing to share information. London and Hart (2004) asserted that such an approach extends far beyond the guidance of national responsiveness which suggests companies can succeed by adapting pre-existing solutions to local conditions. Brugman and Prahalad (2007) assert that “co-creation involves the development of an integrated business model in which the company becomes a key part of the NGO’s capacity to deliver value and vice versa” (p. 89).

Such ventures offer three opportunities, to deliver products at low prices to low-income consumers or to provide niche products to consumers in mature markets; to create hybrid business models involving corporations, NGOs and entrepreneurs at the BOP and to impact the corporation’s social legitimacy while expanding NGO impact (Brugman & Prahalad, 2007, p. 89).

However, co-creation extends beyond the NGO and MNE relationship to include other partners at the BOP as well. For example, London and Hart (2004) noted instances of co-creation in cases that varied from firms allowing local distributors flexibility in how the final product was marketed or delivered, to firms working with non-traditional partners to determine appropriate price points first--forgoing the traditional pricing model of cost plus margin and implementing reverse engineering, while maximizing local knowledge and entrepreneurship to jointly design a product and business model that provided the functionality required and offered the profit margins acceptable for a high-volume business. Another example is the co-creation that resulted from collaboration between Muhammad Yunus, a highly trained economics professor, and Bangladeshi farmers, that lived in the village adjacent Yunus’ home and university. Yunus and the farmers came together and combined their knowledge, experiences and insights with one another until an obstacle was made known (the need for affordable credit), a context was understood (the local BOP) and an innovative solution was born--the Grameen Bank and, the now world-wide, micro-credit movement (Yunus, 1999).

Simanis and Hart (2009) offered additional insights for why co-creation is beneficial in BOP contexts. The authors note that BOP environments and the need for MNEs to achieve
scale mean firms must have a long-term strategy focus yet currently MNEs at the BOP continue to design their strategies under the same “structural innovation paradigm” they use in developed markets. The problem with using the structural innovation paradigm, which was designed to solve customer problems and needs “better, faster and cheaper” than competitors through structural changes to a company’s business system, is that although it may be appropriate for developed economies, the mentality behind it appears to create obstacles to long-term growth in BOPs (Simanis & Hart, 2009). The reason, note Simanis and Hart, is that the structural innovation paradigm motivated strategies, push companies into short-term value capturing strategies and ultimately foster rational, value-maximizing behavior in both consumers and employees that actually serves to undermine commitment to the company and its products.

In environments where rule of law and protection of intellectual property are weak and traditional competitive advantages found in brands, contracts and patents are put at risk, firms must either find new sources of competitive advantage or create ways to protect the original ones. By comparing and contrasting two different companies, Simanis and Hart (2009) demonstrated how the structural innovation paradigm approach created distribution limitations and high employee turnover that created obstacles to growth, while using the co-creation approach allowed the creation of a shared vision among partners where the self-interests of the company, its partners, employees and consumers could all be leveraged to create commitment to a common goal and to a process that was mutually beneficial for all involved.

**Business Models for the BOP**

Currently MNEs are experimenting with a variety of approaches at the BOP. Studies like SNV and IDB (2008) indicated that most firms are still approaching the BOP with CSR policies. However a review of the BOP literature reveals that some recent initiatives have begun to embrace different approaches that are embody many of the findings and key characteristics put forth by BOP researchers. The following are some of these initiatives.

**THE BASE OF THE PYRAMID PROTOCOL**

In efforts to incorporate the learning of Prahalad (2006), London and Hart (2004), and other BOP researchers into a more simplified plan of attack, Simanis and Hart (2008), in
collaboration with colleagues and four corporations, launched the second edition of the Base of the Pyramid Protocol, or simply “The Protocol”. The goal of The Protocol, according to Simanis and Hart, is to bring a company together with a community to conceive, launch and co-evolve a new business and a new market in that community. Ultimately, The Protocol combines a social and economic goal with the BOP as the end consumer and as a part of the business model itself. Divided into “pre-field” and “in-field” stages, The Protocol attempts to give firms pursuing BOP ventures a set of guidelines for how to proceed and includes steps for becoming immersed in the community, building trust, finding partners, creating an ecosystem, cocreating a business model, developing local management and becoming both embedded and independently stable (Simanis & Hart, 2008).

For example, within the pre-field process, The Protocol advises that firms begin by selecting appropriate BOP project sites, forming and training a multi-disciplinary corporate “field” team, selecting local community partners, and creating, within the corporation, an enabling environment that supports experimentation outside of the current business model and business development process. On the subject of partners, Simanis and Hart (2008) recommended two firms look for organizations that are (a) open to learning new capabilities and using enterprise as a way to advance their missions and (b) socially embedded in the community. According to Simanis and Hart (2008), firms can usually determine the level of an organization’s social embeddedness by noting whether or not its offices are located in the community and whether or not its staff is drawn from and/or live in the community. Because most organizations that are socially embedded are small in size and operate intensely within a narrow geographical range, Simanis and Hart (2008) warn that they are not always easy to find but add that in some cases, they can be located through large, well-known funding agencies like Oxfam, CARE or the IDB. Ultimately, Simanis and Hart (2008) observed that depending on a firm’s BOP experience and the extent of its social networks, the pre-field process can take between two and four months to complete.

Once the pre-field processes are complete, The Protocol calls for the initiation of the in-field process, which consists of three phases of activity (opening up, building the ecosystem, and enterprise creation) that Simanis and Hart (2008) maintained build a new, locally-embedded business and catalyze the local market in a progressive, evolutionary manner. For example, in the opening up stage, the company is to immerse itself in the
community, using homestays to build rapport and a base of trust. The next move is for the firm to then recruit a community team that is representative of the community’s diversity and committed to working together with the corporation to develop new business ideas that can benefit all parties (Simanis & Hart, 2008). Afterwards, the firm is to conduct a series of workshops designed to build understanding and a shared business language between the two groups and lead into co-creation workshops that converge the group on a single, actionable business concept (Simanis & Hart, 2008). The second stage, building the ecosystem, involves establishing the project team, participating in actionable learning activities and reaching out to the larger community (Simanis & Hart, 2008). Finally, the firm reaches the third phase, enterprise creation, in which it creates the business model using small-scale tests and continued action learning, jump starts local demand through the engagement of the wider community, deepens the management skills of the community team with the goal of having them eventually manage and lead the new business independently, and creates a platform to support the replication of the new business into other geographies (Simanis & Hart, 2008).

An important focal point of this model is that it emphasizes finding an appropriate NGO in the community of choice from which to gain local insights, leverage the NGOs existing relationships, networks, and trust and then to develop mutual value for all involved in the partnership and work together to co-discover and co-create new business opportunities and models embedded in the local cultural infrastructure, and finally to co-design and launch a business that generates mutual value for all partners (Simanis & Hart, 2008).

**AN EXTENSION OF TRADITIONAL BOP THINKING WITH AN INDIRECT APPROACH**

Arguing that there may be room at the BOP for more than one approach, Seelos and Mair (2007) pointed out that BOP strategies, like those promoted in The Protocol, require MNEs to not only rethink their resource and activity configurations but also to develop and acquire new resources and capabilities and forge a multitude of relationships and alliances with local nontraditional BOP partners, all of which, the authors claim, may present significant challenges and hurdles to MNEs. For example, Seelos and Mair argued that the literature on international strategic alliances alone indicated there was a substantial failure rate among partnerships and a general lack of knowledge about success factors for partner selection. For example Hitt et al. (2000) and Das and Teng (2001) pointed out that alliance
performance was dependent on mechanisms to lower uncertainty around partner intentions and partner abilities and on mechanisms to control for partner behavior that would limit the probability of undesired outcomes (as cited in Seelos & Mair, 2007). Thus, Seelos and Mair argued that it was important to consider that the nonaligned private benefits of partners and the differences in their competencies and organizational characteristics, especially when considering MNE and NGO partnerships, may create the potential for conflict and challenges in building and maintaining trust in partner good will and competence.

Contrary to the assertions of BOP researchers like London and Hart (2004), Seelos and Mair (2007) claimed fundamental insights from business strategy, especially in regards to the replication or redeploying of capabilities such as those discussed by Helfat and Peteraf (2003) and Winter and Szulanski (2001), can apply at the BOP and encouraged firms to see the potential of leveraging existing BOP models in use by social entrepreneurs and form mutually beneficial strategic alliances with them. As an alternative to The Protocol or other inclusive style models, Seelos and Mair saw an opportunity for companies to assemble existing building blocks into a new overall business model that was able to serve the poor, increase their incomes, and create profits but in such a way that MNEs do not serve the poor directly but indirectly by employing company capabilities to provide scale to an already existing BOP business model. In this way, the authors claimed, companies could leverage the relationship to build their own business models, serving higher income customers with whom their capabilities were better aligned, and in some cases derive revenue streams from BOPs as well.

**Micro-Franchising**

A third strategy that makes an appearance in the BOP literature is the Micro-Franchise model (Magleby & Pratt, 2007; Coronado, Krettecos & Lu, 2007). Smaller versions of the original franchise model, micro-franchises are more affordable to own, and, based on a mutually profitable contractual relationship of shared ownership, embody the inclusive, democratic capitalism BOP researchers argue is so important (Magleby & Pratt, 2007). At the same time, Magleby and Pratt (2007) added, the franchise’s proven method of replicating successful, small enterprises on a local, national, regional or global scale makes franchising an attractive way to leverage core capabilities to achieve scale while allowing
franchise owners the flexibility to co-create with the firm to address local BOP needs, effectively giving franchisors and franchisees a way to keep eyes and ears to the ground to keep abreast of markets changes, needs, demands, and opportunities.

Magleby and Pratt (2007) noted that the franchise model is all about brand protection and the way this is achieved is through the development of an operating system between franchisor and franchisee whereby a shared vision is created that is in the self-interest of all parties to uphold. Magleby and Pratt noted that despite diverse cultural mores, numerous franchise operating systems offered advantages in developing countries as they can serve many of the same functions as a rule of law, and even act as a surrogate rule of law able to stand in the gap when a country’s rule of law cannot be depended on. At the same time, noted Magleby and Pratt, these franchise networks can also counter as wonderfully supportive social institutions to franchise owners and employees, all depending of course on the way they are run.

There is one important limitation to this model in regards accessing the required start-up financing. As noted by Coronado et al. (2007) and WBCSD (2004), in developing countries, many people, especially those at the BOP, find it hard to get bank loans. Credit limitations represent potential obstacles to scale but are opportunities for firms to influence change. For example, one initiative in this direction is Mi Farmacita’s (A Mexican pharmaceutical microfranchise) current efforts at developing relationships with banks to establish agreements whereby the company can act as guarantee of the loans (Coronado et al., 2007).

**A LOOK AT FIRMS CURRENTLY AT THE BOP IN LATIN AMERICA**

Preston et al. (2007) reviewed 20 MNCs and 55 national firms in the Latin American Region and found that MNCs and national corporations approached the issues of the BOP from different perspectives. According to the report, some MNCs (i.e. Unilever and Procter & Gamble) are now employing ESG (environmental, social and governance) risk mitigation strategies because data are indicating that investing in such strategies results in opportunities to “do well and do good.” Within this scope, the report noted, more MNCs than nationals employed BOP type strategies to capture this double bottom line. However, national firms did not necessarily look at involvement with BOPs as a new strategy and found it
questionable as to whether these firms considered involvement with the BOP as a strategy or simply part of their overall governance/business plan (Preston et al., 2007). Either way national firms seemed to approach BOPs in a much more natural way—as this was their target market—and seemed to be more intrinsically aware that reaching the BOP had to be done by understanding the population and demonstrating that understanding through in their products and services, business models and interactions with BOP consumers (Preston et al., 2007).

SNV and IDB (2008) interviewed corporations in Latin America as well and found that when including BOP individuals or businesses as part of the production process, firms frequently concentrated on developing the capabilities of the agents involved as well as in strengthening their organizational abilities to effectively respond to firm demands. Additionally the report found that firms also concentrated on strengthening links with the BOP by promoting vertical integration, creating mechanisms to incorporate agents involved in the production chain into the formal economy, and facilitating financing for them. When working with the BOP as final consumers, SNV and IDB (2008) found the most popular strategies used by firms were those involving the design of specific products and services, the development of appropriate distribution channels, pricing, and market analysis, and the use of differentiated presentation of products and services, along with technology development and other marketing strategies to reduce costs or develop products target to the BOP.

In regards to the perceived obstacles by firms to working with BOPs, SNV and IDB (2008), found the initial marginal costs as the most frequently cited barrier to developing strategies for working with BOP individuals or businesses as part of the production chain, while obstacles to working with the BOP as consumers were noted to be the lack of appropriate distribution channels and the absence of technology for cost reduction to enter this market. To overcome these obstacles and better tap into BOPs, the report noted that companies needed superior market research, information, and innovation within their organizational structures.

Despite the obstacles, SNV and IDB (2008) found that firms still seemed to appreciate the economic benefits of incorporating these markets. For example the three most commonly reported benefits of incorporating BOPs as part of the firms’ production process were noted by firms to be increased income/sales, increased production chain productivity
and decreased risks (SNV & IDB, 2008). Additionally, the report found that a significant majority of firms that incorporated BOPs as their final consumers indicated that their consumers benefited by an increased access to new services and products designed specifically for them and two-thirds of firms reported that consumers encountered lower prices and thus real income increases (SNV & IDB, 2008).

**SUMMARY**

As seen throughout this chapter, old strategies designed for more familiar developed markets, when employed in EMs and BOPs are proving to be highly inappropriate. EMs and especially BOPs contain very different capabilities and limitations whose challenges and hazards have humbled many firms that have dared to enter. Although some look at the mismatch of traditional strategies and EMs and place all the fault with the EM, advising firms to “wait and see,” others insist there is great value to be found in taking a different approach both in attitude and in strategy. Researchers believe firms have the opportunity to gain great learning and reputation advantages (Arnold & Quelch, 1998; Brugman & Prahalad, 2007) as well as to design strategies that allow them to do well by doing good (Prahalad, 2006; WBCSD, 2004).

The BOP profit strategy is said to call for a low margins and high volume with an important overall challenge of finding similarities that can be leveraged across BOPs throughout the world. Additionally, recent research suggests the need for local (at a community level versus a national level) intimacy and sensitivity and small-scale ventures with a long-term scaling-up focus (London & Hart, 2004; WBCSD, 2004). For example, Raymond (1999) suggested that competitive advantage in BOPs may be premised less upon the protection of pre-existing proprietary technology and intellectual property, and more on the development of trust, social capital, and permeable boundaries. In support of Raymond, Ricart et al. (2004) noted recent BOP findings that suggest that building relationships directly and at the local level contributes to the social capital necessary to overcome the lack of formal institutions such as intellectual property rights and the rule of law and Chambers (1997) and Sen (1999) asserted that firms without a capacity to appreciate and create social value or to become locally embedded in the social infrastructure that dominates low-income markets may struggle to overcome their liability of foreignness. Ricart et al. (2004) asserted
that “companies apparently need to transform their understanding of scale from “bigger is better” to a strategy of distributed small-scale operations married to world-scale capabilities such as R&D and learning transfer” (p. 194-195). However, as seen by the various models currently in the BOP, it seems there may be room to address these issues in a direct or an indirect fashion.

Either way, as evidenced in this chapter, the strategy literature reveals serious gaps when it comes to global capabilities and business strategy at the BOP. Further, there is little written on how firms create and manage positive spillovers, the degree to which business strategies should be tailored when entering BOPs, or on the most effective types and/or levels of inclusiveness firms should seek to incorporate into their models. Preceded first by the methodology used for the research effort within, Chapter 6 attempts to address this gap by expanding of the findings from Chapter 3 with some specific insights taken from case studies examining the experiences of three firms currently doing business in Mexico’s BOP using some form of an inclusive-style business strategy. The chapter reveals and discusses some of the specific environmental and consumer opportunities and challenges for firms found at Mexico’s BOP as well as the advantages and disadvantages that were derived from the implementation of the various strategies.
CHAPTER 5

METHODOLOGY

The methodology discussed in this chapter applies specifically to the research conducted for and discussed in Chapter 6. It includes a discussion of how the sample was identified and selected, characteristics of the final sample, and finally, a discussion of how data were collected, recorded, and analyzed.

POPULATION OR SAMPLE

The firms chosen for this thesis were identified through a series of referrals. Initially, I spoke with the Inter-American Development Bank, I told them I was looking for businesses in Mexico that were employing some sort of inclusive strategy targeting the country’s lower-income groups and asked if they knew of any firms matching the description. They responded with a referral to a non-profit organization in Mexico City called New Ventures, Mexico that they believed would be able to identify such ventures. I then contacted New Ventures, Mexico and was referred to handful of organizations in the area to look into. The search was eventually narrowed to two companies that met the criteria needed for the thesis—for-profit businesses using inclusive strategies to reach low-income markets.

The third company, I learned about after contacting and speaking with Richard Wells, one of the researchers and authors of the Opportunities for the Majority Index: Analysis of Corporate Performance in Latin America and the Caribbean 2007 final report (Preston et al., 2007) written for the IDB. Though I had contacted him initially for insights regarding the reported he had participated in, through the course of the conversation I learned that Mr. Wells was also involved directly with an international new venture in Mexico that met the criteria of companies I was interested in learning about. Upon request, he agreed to let me interview him. All three companies, then, are for-profit ventures that have designed their products specifically for BOP markets and see as their target market Mexico’s low-income groups. Two are domestic firms and one is an international new venture. Finally, the firms hail from three different industries, represent three very different products, and have three
different inclusive approaches to BOP markets, but have all achieved sustainability and are continuing to grow.

**Data Collection and Analysis**

The interview questions were drawn up after an extensive review of the literature. The literature revealed five primary areas of research I then determined to be necessary to address in the interviews in order to address the current research questions regarding Mexico’s BOP potential and characteristics, key characteristics of successful models and the advantages, if any, of using inclusive models. These five areas are (a) the BOP need/opportunity addressed; (b) the major challenges as perceived by the company to successful market entry and long-term success in terms of accessing and engaging potential BOP consumers; (c) the products and business models designed to exploit the opportunities identified and to successfully address the challenges at hand; (d) the major advantages and disadvantages of, or limitations to, the company’s specific business model/mode of entry; and (e) the insights that have come from the company’s experiences in and with the BOP. These five topics served as the foundation for an interview guide (see Table 4), which provided the basic structure for the interviews conducted. Within these boundaries, however, respondents were encouraged to digress, and interrupt, as they deemed appropriate. Further, although the five areas developed during the literature review provided the starting point for the research presented in Chapter 6, these themes were continuously modified and adjusted as the research developed and lessons from previous interviews informed subsequent interviews.

The interviews were carried out by the researcher between July 2009 and February 2010 (see Table 5). Two interviews took place in person, one by telephone and the subsequent follow-ups via emails and telephone. Two of the respondents agreed that the interview could be recorded (the other respondent was not asked and the interview was not recorded). Thus, two interviews were recorded using a digital recorder, the third through note taking during the interview. No interviewee was compensated for participating in an interview. All files were subsequently transcribed by the researcher as Microsoft word files and analyzed for repeating themes and findings capable of informing the thesis questions.
Table 4. Interview Questions

Describe your business model to include the following:

- How you conduct market research to identify opportunities, challenges, changing wants and needs, moves of competitors etc

- The need/s or opportunity/s your business model addresses and how you balance The needs of the poor (i.e. affordability and quality products and/or services designed specifically for them) with creating a profitable business

- The business model process start to finish or from production to end user (including any partnerships you may have and how you approach distribution, marketing, advertising, sales etc)

- How you manage your partner relationships and the advantages and the challenges of working with these partners

- The unique aspects of the environment your business operates in including the challenges and opportunities present in this environment and the unique way your business model is designed to use these to its advantage in developing a workable business model in Mexico’s BOP

- How Mexican culture and mindsets at the BOP affect or affected your model

- Is your business model scalable

- What you have learned from your experiences

Table 5. Interviews

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<th>Method of Interview</th>
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<tr>
<td>Richard Wells</td>
<td>Principal</td>
<td>The Water Initiative</td>
<td>7/1/2009</td>
<td>Phone</td>
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<td><a href="mailto:Richard.Wells@LexGrp.com">Richard.Wells@LexGrp.com</a></td>
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<td>1/13/2010</td>
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<td>Francesco Piazzesi</td>
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<td>Échale a Tu Casa</td>
<td>9/10/2009</td>
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CHAPTER 6
INDUSTRY PERSPECTIVES

The objective of this chapter is to understand how business models and strategies are being formulated to accommodate both the general and the specific characteristics to successfully reach Mexico’s BOP populations and to become profitable. Additionally, this study will seek to determine whether or not the inclusive business models have provided the companies with any strategic advantages as well as to uncover trends, insights, obstacles, opportunities, and limitations noted by the companies that they perceive as arising from the use of their various business models.

The findings of this chapter are divided into four categories: Microinsurance, Point-of-Use (POU) Water Technologies, Homebuilding, and Discussion of Findings. The first three categories correspond to the individual industries of the three companies interviewed for the thesis as part of a series of case studies while the final category provides a discussion of the overall findings of the case studies. The firms represented in the case studies are Seguros Argos, a leading Mexican insurance company that has recently began serving the BOP with new life microinsurance products; The Water Initiative (TWI), an international (for-profit) new venture specifically created to provide appropriate and locally relevant solutions to BOP needs for quality drinking water, beginning in Mexico; and ¡Échale! a Tu Casa, a Mexican for-profit organization created to provide a better housing solution for Mexico’s poor. In order to answer the thesis questions, the layout of this chapter will be designed in such a way as to identify and discuss (a) the particular need the company is serving (b) the industry the company operates in (c) the product designed specifically for BOP consumers (d) the business model and how it is designed to address the specific challenges, capabilities and limitations presented by Mexico’s BOP and (e) the advantages and disadvantages of the business model as perceived by the company employing it. The final section in this chapter is a discussion of the overall findings of the case studies, and a look at how they inform the thesis questions.
MICROINSURANCE

The Geneva Association (2007) demonstrates that although there are a number of people whose situations make them uninsurable through market mechanisms, there are actually a large number of people that are insurable but simply lack access to products and services adapted to meet their needs and capabilities. Characteristics of these insurable BOP households include irregular cash flows, little disposable income, and very small amounts of savings and other reserves that leave them with few risk management options and make them much more vulnerable than middle-income or wealthy households to unexpected events or disasters (Goldberg & Ramanathan, 2008).

In fact, the resources of the poor are often so limited that low-income households are subject to great financial disruption when unanticipated events occur (Roth, McCord & Liber, 2007). For example, if the breadwinner is injured or falls ill, Goldberg and Ramanathan (2008) observe, a poor household will often lose not only in terms of forgone income and labor, but also in the sense that without cash in advance, they are unable to access the medical care needed to get the afflicted party well again. If a breadwinner dies, the family is faced with monetary needs for covering funeral expenses (short-term needs) and expenses associated with meeting the household’s daily expenses [long-term needs] (Goldberg & Ramanathan, 2008).

Often the vulnerability of the poor is so extreme that one financial upset can threaten their very ability to survive. Thus, the need for insurance protection is perhaps most crucial for this income level over any other. However, their lack of relationship with formal financial institutions and the lack of insurance products designed for their needs and capabilities have consistently denied the poor the ability to benefit from any such protection options. In Mexico, despite the growth of the economy and expansion of the financial sector, many Mexicans still struggle to find access to affordable financial services (World Council of Credit Unions [WOCCU], 2009). In fact, recent estimates report that Mexico’s formal financial sector is currently serving a mere 32% of the population (compared to the 80% observed in most developed countries; WOCCU, 2009). Although the problem is particularly acute for the 17 million inhabitants of rural communities where only about 5% of the population has access (WOCCU, 2009), because of the lack of relationships with formal
financial institutions, the ability of the urban poor to access these services is not much better, even when the physical financial institutions are within closer proximity (Brink, 2007).

When it comes to insurance coverage, even fewer Mexicans have access to appropriate products. According to Goldberg and Ramanathan (2008), in Latin America, the overall insurance penetration rate is only 2.5% for all income levels (compared to 4.3% in Africa and 3.1% in Asia) while in Mexico, due in part to the inequality of income distribution and in part to competition from within the US, the percentage is only 1.7% (Business Monitor International, 2009).

**An Industry Background**

In the absence of access to BOP appropriate formal insurance products, the poor usually adopt expensive risk management options. Seeing this gap as an opportunity, a handful of insurers in countries throughout the world have begun seeking ways to provide insurance to the BOP and are proving that it can be profitable to sell, at least some forms of, microinsurance to the majority markets of the developing world (or the working poor and lower-middle class). Microinsurance, as defined in the Draft Donor Guidelines of the Consultative Group to Assist the Poor (CGAP) Working Group (2003), is “the protection of low-income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of risk involved” (as cited in The Geneva Association, 2007).

Microinsurance can be provided by a variety of entities and should be run in accordance with generally accepted insurance practice (Goldberg & Ramanathan, 2008) but differs from regular insurance in many ways in regards to products and processes. For example, The Geneva Association (2007) notes that it is important to understand that microinsurance is not merely a specific product or line, like savings, credit, or risk provision, nor is it simply a small insurance company, just another product offered by microfinance institutions (MFIs), or simply regular insurance products with smaller sums insured and premiums. Instead, microinsurance is designed with the specific needs and capabilities of the poor in mind to create products that are within their reach and appropriate to their circumstances while microinsurance processes, like risk assessment, are designed to use very different types of information sources that are used for TOP insurance products.
In regards to risk assessment, microinsurers develop different processes for the BOP partly because BOP consumers are incapable of affording high risk-high costing insurance policies and partly because there exist very few countries that possess databases with statistical information on the rates of mortality, illness, accidents, and asset losses of poor households and microbusinesses that would allow insurance companies the data needed to calculate the risks of a BOP individual, household, or microbusiness as the basis of the premium and the level of benefits as well as the potential profits for the insurer (Goldberg & Ramanathan, 2008). To bridge the gap, most microinsurance players incorporate an institutional provider with experience in risk management, product development, and efficient information management systems--making the institutional options similar to those of microcredit which range from Cooperatives and NGOs to private firms (Goldberg & Ramanathan, 2008).

According to Roth et al. (2007), similar to the supply chains of traditional insurance, the microinsurance supply chain main players consist of a reinsurer, an insurer, delivery channel/s, a policy holder, and a beneficiary or beneficiaries. However, in the microinsurance supply chain, the reinsurer, which normally provides insurance to the insurer for catastrophic events, does not yet play a big role and thus, the insurer often carries the insurance risk while the delivery channels sell the insurance policies and provide basic servicing (Roth et al., 2007). Microinsurance insurers can range from multinational or domestic commercial insurers to member-owned mutuals, NGOs, community based organizations or even informal groups, though it is important to note that of the four main types of insurers: commercial, NGO, mutual, and community based organizations, only commercial insurers and mutuals are professionally managed and regulated under insurance regulations, meaning they maintain reserves and have access to reinsurance and are thus able to provide a greater level of protection to their already vulnerable BOP customers (Roth et al., 2007).

In regards to microinsurance delivery channels, because they are traditionally the ones in contact with the policy holder, they tend to work best when they are organizations that have close contact to the poor (Roth et al., 2007). Because currently there are very few traditional delivery channels that reach the poor, firm heads who think beyond the traditional modes of delivery tend to create advantages over those who do not in terms of getting their products to market. For example, some non-traditional outlets microinsurance organizations
have used are credit unions, retailers, MFIs, NGOs, employers, banks, smart cards, utility companies, cell phones, on-line set-ups and ATMs, self-help groups, cooperatives, and computer kiosks (The Geneva Association, 2007). Although it is possible for one organization to be both an insurer and a delivery channel, Roth et al. (2007) warn that some may be better suited for one role over the other. For instance, NGOs, which can include development organizations, trade unions, federations of groups, and microfinance institutions, are close to poor people and thus often very effective delivery channels, but because they are often unregulated and less professionally skilled than commercial insurers, as insurers, they automatically put their consumers at a greater risk.

**Taking Stock of Potential Delivery Channels:**

**Mexico’s Retail Financial Service Providers**

Klaehn, Helms and Deshpande (2006) country level savings assessment briefly discusses Mexico’s main retail financial service providers and through an analysis of Mexico’s deposit taking institutions, attempts to determine which of these are most likely to have existing relationships and channels in the BOP and thus be best positioned to reach the poor. According to authors’ assessment, Mexico has 32 commercial financial banks with 7,793 bank branches, more than three and a half times the number of service outlets of the entire popular finance sector and the government development bank combined. However, these branches are primarily located in urban areas and serve only 25% of the total urban population (Klaehn et al., 2006). Further, because there is still a large market to be gained among middle class consumers, Klaehn et al. (2006) observe that it is unlikely that commercial banks have much incentive to engage the BOP.

According to Klaehn et al. (2006), financial cooperatives, represented by approximately 300 cajas populares and more than 300 cajas solidarias, are the major players in Mexico’s popular finance sector with nearly 1,800 branches serving more than 2.5 million members. Of these two, Klaehn et al. found that the majority of members are in cajas populares, which function as credit unions or, as they are known in Latin America, “cooperativas de ahorro y crédito,” to provide savings, credit and other financial services to their members. Perhaps the reason for the popularity of cooperatives lies in the nature of the organization, as Roth et al. (2007) points out, credit union membership is based on a common bond, a linkage shared by savers and borrowers who belong to a specific community,
organization, religion, or place of employment. Whatever the reason, these financial cooperatives have managed to mobilize more than US $2 billion in savings, for an average of US $782 per member (Klaehn et al., 2006). However, despite having perhaps the deepest outreach into rural, marginalized, and underserved areas, the cajas solidarias, in particular, still suffer from a lack of public confidence, are still largely dependent on traditional credit-focused operating models, and will need to confront persistent governance problems and management deficiencies before attempting to increase their outreach (Klaehn et al., 2006).

On a positive note, in October of 2004, one financial cooperative, Caja Libertad, began issuing debit cards to its BOP members--a service previously offered only by commercial banks--and by February 2005, nearly 67,000 debit cards had been issued with average withdrawal amounts of US $93. Further, at the time of the article, the organization was negotiating with a national network to enable its cards to function in ATMs owned by other financial institutions (Klaehn et al., 2006). Such results offer evidence of technology reaching and being successfully used by BOP markets.

A third group included in the Klaehn et al. (2006) assessment is Credit Unions. According to Klaehn et al., Credit Unions are another diverse group in Mexico with 132 institutions, nearly 2.7 million members representing a 3.7% penetration rate, nearly US$ 2 billion in savings as of 2008--up nearly $1 billion from the authors’ estimates for 2004, and $1.7 billion in loans (WOCCU, 2008). Though credit unions have a mixed rural/urban presence with some offices located inside Mexico City, most branches are found in the more rural regions of the country (Klaehn et al., 2006). After examining the strengths and weaknesses of this group, Klaehn et al. (2006) concluded that in order to mobilize deposits and the like on a large scale, many credit unions will need to abandon traditional operating models and strengthen their financial management capacities.

Finally according to the Directory of Development Organizations (2010), there are approximately 116 MFIs operating throughout Mexico that collectively provide services to more than 375,000 low-income and poor clients. Though overall the microfinance sector is characterized by weak outreach and high levels of fragmentation, especially in acute rural areas, a small number of MFIs supported by the government are emerging as market leaders
and have recently begun to take the lead in creating a microinsurance sector (Goldberg & Ramanathan, 2008).

Thus although there do appear to be several existing channels through which microinsurance companies can begin to distribute their products, these organizations are not without their limitations. As seen above, commercial banks lack incentive to engage BOP markets, and financial cooperatives and credit unions lack significant reach to the urban poor, have weak financial management and operating models that need rethinking, struggle with governance issues and, as a result, suffer from a lack of public confidence. Finally, MFIs are characterized by weak outreach and high levels of fragmentation. All of these represent real needs among existing channels that will eventually require attention before they can become the reliable and trustworthy distributors and promoters capable of achieving the type of scale needed by industries attempting to reach and engage BOP markets.

Seguros Argos: Delivering Microinsurance to Mexico’s BOP

According to E. Rivera, an insurance agent with Seguros Argos--one of Mexico’s leading life insurance companies, right now there are only about five companies working in microinsurance in Mexico and of them, Argos is the largest (personal communication, September 11, 2009). Seguros Argos, or simply “Argos,” was founded in 2002, serves only middle to low-income consumers, and due in part to a partnership in 2006 with Aegon--one of the world’s largest insurance groups--has over 1.7 million clients, more than 300,000 of which are beneficiaries of microinsurance (ILO, 2009).

Inspired by the claims of authors like C.K. Prahalad that the BOP represents untapped market opportunities, Seguros did a little on the ground market research of its own in Mexico in order to determine what, if any, types of products were in need and might be appropriate for BOP consumers. On the ground, the company learned that many of the Mexico’s insurable poor earned less than $2,000-$3,000 a year and often experienced immediate financial difficulties resulting from funeral costs when someone in the household died (E. Rivera, personal communication, September 11, 2009). Realizing funeral costs could often be as high as a year’s worth of earnings, Argos designed life microinsurance policies in the amounts of US $2,000-$3,000 that required people to pay only US $10-$20 per year, depending on the policy chosen (E. Rivera, personal communication, September 11, 2009).
After deciding on an appropriate policy, Argos had to create a method of distribution that factored in the lack of its target market’s consumer sophistication with formal financial institutions and products, challenges in regards to access, and its general skepticism of new products. Because most low-income Mexicans do not have a checking or savings account with or any kind of relationship with commercial financial banks and would thus have great difficulty in cashing a check, Argos arranged for microinsurance beneficiaries to be paid in cash. When the policy holder dies, the beneficiary simply calls the company by phone and a representative goes out to the beneficiary and delivers the cash lump sum. Getting the cash to BOP beneficiaries is important, observed E. Rivera, because families incur immediate expenses upon the death of a family member and, as a cash society, they have few other ways of paying for things (personal communication, September 11, 2009). An additional benefit Rivera noted to distributing payouts in cash and in a direct and timely manner is that with each payment, BOP consumers become more confident and trusting toward Argos and start to spread the word of the company to others.

The Business Model

Currently Argos uses two different approaches to distributing its products. The first, E. Rivera explained, uses existing networks and institutions serving the BOP through a “partner-agent” model, whereby the company works closely with the existing networks of MFIs, credit unions, and cooperatives both to distribute goods and to leverage pre-existing reputations, credibility and local expertise at the BOP (personal communication, September 11, 2009). Ultimately, Rivera noted, Argos sells its microinsurance products to these organizations that then sell and deliver them directly to BOP consumers. In turn, the distributors receive a commission for sales from Argos.

The second approach Argos takes toward distributing its products is through its “Mutuals of people from the low income population in Mexico” or “Mutual” model. According to E. Rivera (personal communication, September 11, 2009), this model resulted from Argos’ desire to create more BOP appropriate products and to take their BOP approach beyond just selling to the poor. Ultimately, the Mutual model targets low-income Mexicans who do not have access to risk management mechanisms that are adapted to their needs, provides needed services to the BOP, and is designed to help empower BOP communities
with opportunities to learn about and to become more familiar with financial products and processes by participating in the microinsurance process themselves. The project has received partial funding from a new partnership between the ILO and the Bill & Melinda Gates Foundation that seeks to develop or improve insurance products to promote decent work for tens of millions of low-income people in the developing world (ILO, 2009).

The goal of the Mutual model, according to Argos’ project profile (ILO, 2009), is to reach 500,000 clients, mainly vulnerable women, in three years by creating ten mutual insurance schemes offering term life insurance that will be implemented through organizations already working in the target areas. An important service offered by these schemes, upon the death of a policy holder, is the provision of a doctor who will go into a community to record the death and deliver the death certificate and a lawyer who will help with administrative matters to ensure prompt payment of the covered unit (ILO, 2009), services previously unavailable to the poor. According to E. Rivera (personal communication, September 11, 2009), with this project, Argos works with existing cooperatives and credit unions to help them build their own regulated insurance companies (the mutuals).

Argos provides the professional and financial support to establish the mutuals and the necessary training and in return obtains its own close-to-market, BOP intimate channels. For example, E. Rivera explained, with a financial grant provided by the ILO, Argos is able to provide the newly formed mutual with everything it needs to get started--for free, including training (personal communication, September 11, 2009). The idea, Rivera explained, is for the mutuals to be managed by the people already in the BOP. These people, Rivera noted, are given the opportunity to learn and to become familiar with how the insurance business works from doing it hands on under Argos’ supervision. Thus, during the process of creating the mutual, a creative partnership between Argos and the mutuals is forged and creates an opportunity for a close-to-market mutual to keep a close eye on changing needs and circumstances and to co-create new products and modes of delivery with Argos while allowing Argos to become the mutual’s supplier both for financial products and for ongoing support. Ultimately, Rivera explained, Argos becomes the insurance company of the people’s newly created BOP insurance companies.
Advantages and Disadvantages

According to E. Rivera (personal communication, September 11, 2009), there have been many advantages to using the partner-agent model. First, the microinsurance model affords Argos the ability to access risk and insurability for its low-income consumers through alternative and more BOP appropriate methods. Second, by taking advantage of Mexico’s many existing channels, Argos has been able to begin immediate distribution of its newly created life microinsurance products, indirectly educate BOP consumers on the advantages of the product, and leverage the trust of its non-traditional distribution partners for quicker acceptance by BOP consumers. In fact, the major benefit of using these particular nontraditional partners as distribution channels, Rivera expressed, is that often they are already addressing the issues that stem from the poor’s lack of access to formal financial institutions, such as the skepticism and lack of knowledge or understanding of financial products that could be of benefit to them. Thus, through its association with its non-traditional partners, Argos has been able to obtain some immediate credibility in the BOP, allowing it to save time, money, and effort on overcoming skeptics and building its own trust before it was able to access consumers. Finally, Argos’ strategy of distributing cash payouts to beneficiaries quickly has worked to further BOP trust in the company by building credibility with BOP consumers.

The disadvantages found with using this model in Mexico appear to be related to the limitations of the existing channels or non-traditional partners used in the partner-agent model. For instance, as previously noted by Klaehn et al. (2006), the channels with the greatest BOP reach in Mexico are largely unregulated organizations that need great improvements in terms of management and efficiency. As a result, public confidence in these channels is low and the ability for the non-traditional partners to increase scale and quality of service is strained. Further, the existing channels lack any kind of significant presence in urban areas, thus limiting the ability for Argos to reach the potentially large markets represented by the urban poor. Finally, the reliance on non-traditional partners seems to have left Argos with only a vague understanding of the needs and realities of its BOP consumers, an issue the company appears to be trying to address through its Mutual model.

Although E. Rivera felt it was too early in the process to speculate on any disadvantages with the top-down, inclusive Mutual model, other than the fact that it appears
to remains limited in its ability to access to the urban poor, he was enthusiastic about the advantages the new model was creating (personal communication, September 11, 2009). For example, the new model attempts to address many of the disadvantages experienced by the Partner-Agent model, such as enabling Argos to (a) get closer to the poor to co-create ideas, and to stay in tune with changing needs and wants, and thus to gain access to local insights; (b) capacity build to contribute to consumer and distribution channel sophistication, bring informal participants into the formal system, advance formal financial products and systems, and develop markets for long-term demand generation; (c) gain access to grants like the ILO/Gates grant as a result of the model’s social and financial focus that then enables Argos to offer capacity building and training free of charge to new mutuals; (d) address the country’s existing channels’ weaknesses to enable them to become more effective providers while also creating channels for which Argos becomes the trusted and reputable suppliers of insurance products; (e) create regulated channels that will help ensure customer protection, company reputation, and long-term scaling up; and (f) provide consumers with a product that allows them to achieve a Mexican core value of leaving something behind when they go.

In other words, the Mutual model allows Argos to simultaneously address many of the existing weaknesses in Mexico’s existing channels to help them to become more viable entities while simultaneously creating regulated channels of its own that will help the company develop its own understanding of and reputation with its BOP markets, capacity build to contribute to the increasing the consumer sophistication of its target market, and co-create products to maximize benefits to both the consumer and the company, and ultimately expand its reach long-term throughout Mexico.

**Point-of-Use Water Technologies**

Discussing findings from the United Nations (UN) World Water Report 2, UNESCO (2006) noted that despite the fact that the world has plenty of freshwater, mismanagement, limited resources, environmental changes, corruption, lack of appropriate institutions, bureaucratic inertia and a shortage of new investments in building human capacity and physical infrastructure have led to a global situation where almost one-fifth of the planet’s population (some 1.1 billion people) lack access to quality drinking water. Poor water quality has been found to be a key cause of poor livelihood and health, and a major contributor to the
spread of the potentially crippling and fatal ailments associated with diarrheal diseases (1.8 million), malaria (1.3 million deaths/year), schistosomiasis (causing tens of thousands of deaths/year), trachoma (which often leads to blindness), intestinal helminths, hepatitis A, arsenic poisoning, and fluorosis (WHO, 2004). Further, UNESCO (2006) noted, in 2002, diarrheal diseases and malaria alone were found to be responsible for the deaths of 3.1 million, of which, 90% were children under the age of five.

Although approximately 1.6 million lives could be saved annually by providing access to safe drinking water, the UN Water Report 2 found that rather than seeing improvement, water quality is actually declining around the world. This is due in part to already failing systems and in part to the increasing demands for water from a growing world population that is further stressing a water infrastructure already unable to support the demand (UNESCO, 2006). Further, UNESCO reported, in many regions, financial resources for water are stagnating—just when they are needed most. For example, UN Water Report 2 found private sector investment in water services has declined as many big multinational water companies had withdrawn from or downsized their operations in the developing world because of the high political and financial risks (UNESCO, 2006). Additionally, UNESCO reported that although total Official Development Assistance to the water sector in recent years has averaged approximately US $3 billion per year with an additional US $1.5 billion allocated to the sector in non-concessional lending, mainly by The World Bank, only a small proportion (approximately 12%), is actually reaching those most in need and only 10% is being directed to support the development of water policy, planning and programs (UNESCO, 2006).

Although the UN Water Report 2 estimates just over a billion people worldwide in need of quality water, the difficulties and challenges of obtaining accurate, up-to-date data in developing countries, as mentioned in Chapter 3 of the thesis, make it impossible to obtain a fully accurate estimation of the number of people in need worldwide. However, because some idea of the need, even a conservative one, is better than none at all WHO (2006) has attempted to measure the number of people without access to quality water through two indicators: (a) the percentage of the population with access to improved drinking water sources and (b) the percentage of the population with access to improved sanitation facilities (see Table 6).
Table 6. Core Health Indicators for Mexico

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value (Year)</th>
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<tbody>
<tr>
<td>Population with sustainable access to improved drinking water sources (rural)</td>
<td>85% (2006)</td>
</tr>
<tr>
<td>Population with sustainable access to improved drinking water sources (urban)</td>
<td>98% (2006)</td>
</tr>
<tr>
<td>Population with sustainable access to improved sanitation (rural)</td>
<td>48% (2006)</td>
</tr>
<tr>
<td>Population with sustainable access to improved sanitation (urban)</td>
<td>91% (2006)</td>
</tr>
</tbody>
</table>


According to the percentages for rural Mexico in Table 6, rural residents appear to have significantly lower levels of access to quality drinking water than do urban residents. According to Tortajada (2001), this may be a direct result of the challenges currently being experienced by many rural regions throughout the country resulting from the recent decentralization of the water industry under the National Waters Law (Ley de Aguas Nacionales—LAN). Tortajada explains that the result of this decentralization has been the devolution of authority from the National Water Commission to municipalities without the other essential changes necessary for decentralization to work. For instance, one major issue Tortajada points out has been the failure of the transition to empower the local authorities that are expected to take on the recently decentralized responsibilities. According to Tortajada, these authorities often do not have the financial or human resources necessary to meet the water needs of rural Mexicans. Further, the people in these rural communities are, in most cases, generally unprepared to take on the burden of building and maintaining their own centralized water treatment systems (Tortajada, 2001). Thus, in addition to the current inability to get quality water to many rural residents, the outlook for the resolution of the problem anytime in the near future is not optimistic.

Taken alone, the figures in Table 6 appear to indicate that Mexico’s urban areas have relatively high levels of water quality while rural areas have a much lower level. However,
although it may be true that there is a disparity of access to water piped from the public system between the country’s urban and rural regions, the findings of recent studies like UN-HABITAT (2006) suggest that the extent of this disparity in terms of the number of households actually receiving uncontaminated water may not be as wide as the WHO figures suggest. For example, the UN-HABITAT (2006) found that although some cities had made notably large investments to extend services to its rapidly increasing inhabitants, in many cases they had failed to or been ill-equipped to provide the financial and human resources needed to maintain them. As a result, The World Bank (2005) noted that although public services in Mexico were found to be more available in cities, they often tended to fail for the poor due to low quality and reliability, indicating that the numbers of people in Mexico in need of quality water may be much higher than current estimations suggest. In addition, given WHO (2004) estimates that by 2030 two-thirds of humanity will be living in urban areas, with nearly two billion people in urban squatter settlement and slums taxing an already strained water system, the lack of access to quality drinking water is only expected to intensify.

The urgency of the water supply challenge facing lower income consumers presents the need for real, implementable, scalable, sustainable, high-impact interventions that can be rolled out in the near term and for the reasons discussed above, the construction and maintenance of large centralized water treatment plants are often inappropriate for the immediate needs of the BOP in developing countries. In addition, as pointed out by TWI (2010), large water treatment plants are known to consume enormous amounts of energy, produce tremendous wastewater issues and waste up to 40% of their output from plants through leakage from the water distribution infrastructure. Further, much of the remaining water becomes re-contaminated during distribution or storage (TWI, 2010).

Recently, TWI and other POU water technology companies, along with the WHO, have begun to advocate that the most effective and efficient solution to the immediate need for safe drinking water in the developing world is the widespread adoption of POU water technology solutions, whether in the home or at the community level. According to these groups, POU solutions offer affordable alternatives that treat water at the point of use or just before it is actually consumed, thereby reducing the risk of contamination. The following subsections will include insights gathered from a background on the POU industry, a
discussion of TWI and its unique product offering and BOP approach, and the advantages and disadvantages that result from its specific BOP strategy.

**An Industry Background**

Although POU water treatment technologies represent a low-cost, scalable, and potentially effective solution to the significant challenge of providing potable drinking water in low income areas, studies like Harris (2005), suggest that, so far, achieving widespread BOP acceptance of the POU industry and commercial viability without the dependence on a subsidy has proved challenging for firms. According to Harris’s findings, the most formidable challenges to firms have been in regards to creating demand, ensuring access and usage of products, recovering costs, overcoming business impediments, and overcoming political and administrative obstacles.

Most of the challenges discussed by Harris (2005) seemed to share characteristics to the struggling firms discussed by London and Hart (2004) that failed to create strategies appropriate for BOP conditions and consumer characteristics. For instance, the strategies mentioned by Harris (2005) all appear to use a top down approach, where the companies, independent of the communities they were targeting, were designing a product and business model, attempting to create demand, and using existing metrics to design cost allocation and recovery models. Perhaps the most expensive and time consuming of the challenges reported by Harris were those encountered in company efforts to generate health awareness and product promotion and to create product access and consistent usage. For example, through trial and error, POU firms have learned that in many BOP areas, particularly in rural locations, awareness campaigns are necessary to educate people on the presence of contaminated water in their communities and the dangers it represents before companies can even hope to create a demand for POU products (Harris, 2005).

However, convincing people to change behaviors in any market is no small task and trying to do so in BOPs where traditional media is not effective, local diversity prevents standardized campaigns, and mistrust for corporations is high can be expensive, tricky and, at times, precarious. For instance, Harris (2005) and WBCSD (2004) discuss one major issue POU firms encountered was that after pouring significant amounts of money into awareness campaigns that ultimately offered their firm’s products as solutions in an effort to create
demand, BOP communities simply distrusted them even further, writing the campaigns off as just another corporate scam. Finally, Harris found that for those people that were willing to try the product, income restraints and a lack of understanding of the product and its usage were common challenges to making purchases and using the product properly and consistently.

Harris (2005) ended his study by saying that although he went in search of obstacles, he found more along the lines of opportunities. His final analysis discusses six areas that are assisting POU projects in approaching viability that may represent emerging best practices against which POU projects seeking commercial viability in the future may consider when building their own models. These six areas are (a) refine and improve product positioning; (b) leverage existing health awareness in an area; (c) offer a smorgasbord of product options when doing promotional campaigns that allows companies that offer different types of POU technologies to share marketing expenses while creating widespread awareness and demand and eliminating the appearance of a salesman peddling his wares; (d) adapt business practices (to become more BOP business environment appropriate); (e) find alternative models of viability; and (f) focus on key product improvements.

**The Water Initiative: A Bottom-Up POU Solution in Mexico’s BOP**

One recent international new venture taking a slightly different approach than the firms studied by Harris (2005), both in terms of its type of POU product and its strategy for engaging the BOP and achieving commercial viability, is TWI. Comprised of an international network of technologists, entrepreneurs and leading global business professionals, TWI began its venture into the BOP first by creating an innovative product that was capable of responding to local needs and replicating into multiple BOP communities. As noted by Morrison (2008), instead of designing a POU technology capable of addressing only one or two water contaminants and then attempting to sell it in all BOP markets—regardless of whether or not the product actually fit the water need specific to the market, as most POU companies have done, TWI takes the opposite approach.

Understanding that the world presents a diversity of water problems ranging from local pathogens and in-transit fouling of water to high levels of chemicals like arsenic and fluoride, TWI’s product lines and services were designed to be dynamic and capable of
leveraging a broad base of technologies from different industries while also fitting into a broad schema (TWI, 2010). For example, comprising the broad schemata is a macro-filter that removes large particles, a micro-filter that strains out the local impurities (whether it’s pathogens or unsafe levels of inorganic materials like arsenic), a tester that ensures the water’s safety, and finally, a power source (type dependent on the community) that drives the process (TWI, 2010).

Further, the company’s business model is designed to work with communities to co-create water solutions appropriate to their needs and to work together with them to educate promote and distribute TWI solutions to households throughout the various communities. According to TWI (2010), to the best of their knowledge, TWI is the only enterprise with an integrated global business strategy that has the capacity to deliver appropriate POU water platform solutions that are distributed globally through co-created partnerships. Though many companies in the POU industry have impressive technologies, TWI (2010) notes, aside from TWI, no one else integrates all of the necessary system elements, i.e. macro and micro removal technologies together with sensors and energy sources, necessary for a fully integrated POU system capable of addressing a variety of local water conditions.

The Business Model

Well aware of the obstacles presented by the BOP, TWI chose to move forward using The BoP Protocol as its guide for entering Mexico’s low income areas. In addition to Richard Wells, a TWI Principle and one of the initial creators of The Protocol, TWI brought on individuals with experience using The Protocol to act as consultants to the endeavor. However, once on the ground, the company encountered an unexpected challenge that ultimately resulted in the slightly altered Protocol approach TWI now uses as its preferred mode of entry.

R. Wells noted that once TWI narrowed down the initial region that met the demographic it was looking for, i.e. peri-urban communities with arsenic and fluoride issues, the next step in The Protocol’s was for the firm to find a local NGO that would make an appropriate partner to help assimilate TWI and its products into the local communities (personal communication, July 1, 2009).
The problem was that there was no such company. TWI’s consultants then tried to insist that the company could not move forward, so I stepped in and said, ‘this kind of inflexibility is ridiculous, we will just go into the community and form our own networks and relationships,’ and we did (R. Wells, personal communication, July 1, 2009).

According to Wells, the decision for TWI to bypass NGOs and form its own relationships created a highly advantageous situation for the company because it gave the firm a real experience and understanding of the BOP community that it would not have otherwise obtained. Through the development of its own relationships, now TWI’s preferred mode of entry, the company researches local water issues and works with the community to co-design effective and affordable entry level products that the firm is then able to market and deploy through community-based local entrepreneurs, allowing it to penetrate and expand channels of distribution that were previously undeveloped (TWI, 2010). Where many other companies sell at the community level, R. Wells explained, TWI sells its products at the household level and uses its community partnerships to tackle the challenges of educating consumers on the health need and the product’s benefit and use (personal communication, January 13, 2010).

Specifically, the company uses a “go to market” sales implementation which is primarily the responsibility of its Community Site Leaders (TWI, 2010). Here, Site Leaders help organize socio partners--small groups usually comprised of entrepreneurial women that are known and respected in the community, who serve as educators, promoters and distributors--to organize social gatherings that are informative, fun and lead into sales opportunities (R. Wells, personal communication, July 1, 2009). Wells further noted that because products are priced lower than bottled water, TWI actually gives consumers the opportunity to save money by switching to POU systems. Finally, to address the income restraints experienced by some consumers, the TWI model gives people the option of paying a one-time fee for the hardware and disposables or financing it via a partner (usually a microfinance organization) into monthly payments (TWI, 2010). Table 7 sums up TWI’s business model into eight basic steps as noted in TWI (2010).
### Table 7. TWI Business Model

<table>
<thead>
<tr>
<th>Step</th>
<th>Description</th>
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<tbody>
<tr>
<td>1.</td>
<td>Perform a strategic regional assessment: Identify key water problems in a country or region (such as arsenic or fluoride in north-central Mexico).</td>
</tr>
<tr>
<td>2.</td>
<td>Define a target market: Conduct market analyses to identify best target markets (ex: peri-urban communities in rapidly growing countries).</td>
</tr>
<tr>
<td>3.</td>
<td>Community immersion: Immerse the initiative in a carefully selected representative community to understand its functioning and unmet needs.</td>
</tr>
<tr>
<td>4.</td>
<td>Technology development: Work in the community to develop tailored, integrated solutions to address its key water issues.</td>
</tr>
<tr>
<td>5.</td>
<td>Business co-creation: Co-create a business concept with local community leaders and entrepreneurs using the BoP Protocol.</td>
</tr>
<tr>
<td>6.</td>
<td>Organic growth: Use social networks to grow organically from initial host community.</td>
</tr>
<tr>
<td>7.</td>
<td>Replication: Apply an abbreviated BOP process to extend the model to new growth nodes beyond initial social networks.</td>
</tr>
<tr>
<td>8.</td>
<td>Expansion: Extend the model to new regions and new water quality problems.</td>
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According to R. Wells (personal communication, January 13, 2010), TWI is based on a profitable, self-sustaining business model and the company is confident it is on to something viable. So far, the company has received several million dollars in seed funding and is on the lookout for US $5-$10 million more (Morrison, 2008). In addition to investor funding, R. Wells (personal communication, July 1, 2009) noted, the company has received grants from the municipal water supply system for Gomez Palacio (SIDEAPA) for US $75 thousand and from the Mexican Business Coordinating Council for US $200,000.
Currently, R. Wells emphasized, the company is fully self-sustaining without the grant money but its availability represents local support, is non-dilutive to shareholders and permits the more rapid deployment of the TWI business concept (personal communication, July 1, 2009). Although the initial monies used at the front end of TWI’s business may sound like a lot to recover in low-income areas, it is important to keep in mind that TWI is targeting an estimated 550 million underserved middle and lower income households that represent US $125 billion (TWI, 2010).

**Advantages and Disadvantages**

TWI’s experience using The Protocol revealed both weaknesses and strengths in the approach. For instance, commenting on his recent experiences with the Protocol, R. Wells noted that in many ways The Protocol was an academic creation that had not accounted for many of the actual on-the-ground realities—such as the fact that there are not always NGOs available to partner with (personal communication, January 13, 2010). Basically, Wells explained, The Protocol becomes problematic when people view it as the bible of BOP entry, because that’s when the necessary flexibility gets lost. However, he added, when seen more as a set of guidelines, The Protocol can still be a very useful tool for navigating BOP entry. By forging its own relationships, TWI discovered that a slightly altered version of The Protocol resulted in a huge advantage over other POU companies competing for the BOP consumer.

TWI found that getting on the ground and getting to know the communities, getting co-creation and community owned projects was huge in gaining trust and positive reputational benefits in addition to creating invested spokespeople and salespeople within the community. Had we skipped this piece and just come in offering a product that gets rid of arsenic and fluoride, people would not have taken us very seriously. They would have said, ‘ok, so you offer the product, so do ten other companies’ (R. Wells, personal communication, January 13, 2010)

By getting involved at the community level, TWI has been able to create POU solutions appropriate to the specific needs of the community, develop trust in the product and the company itself, provide a community platform for education, training, and promotion on the need for clean drinking water and the TWI solution, provide ongoing support, and create a vested-interest in the distribution and success of the TWI product—a significant competitive advantage over other companies that offer similar products but struggle to develop trust, awareness, consumer sophistication, and demand as described my Harris (2005).
Two additional advantages have emerged from TWI’s strategy as well. The first is a result of TWI’s efforts towards creating a capacity to consume. By offering financing options to those who need it, TWI has been able to gain advantages over competitors by offering a way for consumers to finance their purchases. The second is a result of TWI’s innovative technology coupled with an overall lack of confidence in the water quality throughout Mexico in all markets. For example, as TOP consumers have gotten word of TWI’s product, the company has been experiencing an unanticipated demand from Mexico’s higher income markets as people are asking why they shouldn’t be able to benefit from the products as well (R. Wells, personal communication, July 1, 2009). Such additional TOP demand adds support for Prahalad (2006) claims that although products designed for TOP markets are usually incapable of transferring to BOP markets, the reverse scenario is entirely possible. If TWI decides to offer product options to TOP markets, this diversification opportunity could potentially allow them the financial advantages for scaling into BOP regions they are currently unable to reach.

According to R. Wells, the most significant disadvantage that the model faces is TWI’s current inability to scale into the harder to reach rural regions because in order to keep TWI’s investors investing, the firm has to produce returns quickly (personal communication July 1, 2009). The major issue is that investing in BOP ventures is a relatively new concept for most people and most investors are still unfamiliar with the different investment perspective that is required to enable BOP ventures to produce higher returns. As Wells noted, BOP ventures like TWI require upfront capital to get going and to scale into multiple regions and a long-term approach from investors who understand that BOP ventures take a little more time on the front end as they must scale into and become established in multiple communities and regions.

Investors must understand that long-term investments will take a little bit longer to get going because in low-margin areas, returns on investment will be all about the volume achieved, and in BOPs, where infrastructure is poor and pre-existing networks and relationships are limited, this takes time. For TWI, the conflict with the venture’s needs and investors’ demands has been the limited the ability of the company to reach the poorest of the poor in Mexico’s rural regions where the lack of infrastructure and the dispersed nature of the people slows down the scaling up process.
HOMEBUILDING: THE SELF-BUILD SECTOR

According to Mexico’s National Housing Commission (Comisión Nacional De Vivienda [CONAVI]) 2006 estimates, by 2012, Mexico will have a housing shortage of approximately 4.4 million housing units and require the construction of an estimated 633,000 new houses a year to meet the current demand. In addition, because many Mexicans do not have the ability to use financing to assist in the improvement and maintenance of their homes, many houses are left to slowly deteriorate over time. As a result, in addition to the new homes that will need to be built by 2012, CONAVI (2006) estimates that 2.9 million homes of country’s current housing stock will need to be improved, modified or even substituted altogether during the 2006-2012 period. In other words, it will take an estimated 455,000 improved houses per year, in addition to the ones that existed at the time of CONAVI’s estimates, to keep up with the country’s needs (CONAVI, 2006). Further, by the year 2025, when the 25-50 year old demographic (the age segment that is most likely to enter home purchases) will be the largest age demographic in the country, Mexico’s population is expected to grow to 125 million, increasing the total estimated demand for new housing to 42.2 million units and raising the number of units that would have to be constructed per year to keep up with demand to approximately 750,000 housing units per year (Ecoblock International, 2009a).

An Industry Background

In Mexico, there are two main ways homes are built in Mexico, developer-built and self-built. The first produces homes that are built for sale and are generally sold with a full title transfer. Because the mortgage industry is still new in Mexico, with less than 20% of the population having access to mortgage loans, developer-built homes tend to be concentrated in the middle and upper income markets with buyers who need little or no financing (Ecoblock International, 2009a). Coupled with the many other structural limitations in Mexico’s housing market such as high taxes and tenant-heavy legislation that make securing property rights or even basic services difficult, this exclusion of access to developer-built houses has resulted in high levels of owner-occupied homes that have been constructed over a period of years through non-equity generating processes of self-construction (Ecoblock International, 2009a).
Discussing the self-construction process, Sharma et al. (2003) explain that the high and rising costs of construction materials in Mexico and the inability of the poor to finance them result in untrained self-builders purchasing building materials little by little and then storing them outdoors over a period of years, where they are subject to weather and theft. Further, because the actual construction of a home generally falls solely on the head of the family building it, construction is limited to sporadic weekends and holidays when the head of the household has time off from work (Piazzesi, 2007) and because there are usually no trained professionals assisting in the construction of the house, the result is a spontaneously designed home based on local customs and poor construction that will require continuous maintenance. In fact, according to Ecoblock International (2009b) currently self-builders spend an average of 30% of their annual income on housing repairs and maintenance. Consequently, Mina Lopez, a representative of Échale a Tu Casa, observed, it is not uncommon for self-built housing to take 15-20 years to complete, end in a significant amount of financial and material waste, and result in low quality homes incapable of offering any equity to families (personal communication, September 10, 2009).

¡Échale! a Tu Casa: Delivering an Affordable Housing Alternative to Mexico’s BOP

According to M. Lopez (personal communication, September 10, 2009), one of the biggest problems with programs in Mexico aimed at addressing the country’s housing issues is that they tend to operate on the belief that the real need behind Mexico’s housing shortage is that the poor simply lack access to the proper building materials they need to build proper homes. Lopez says the organizations behind these programs believe that if the poor are given access to materials, they will be able to build their own homes and the housing shortage will disappear. However, Lopez insisted, simply giving materials to poor families that have no education or formal training when it comes to homebuilding and then expecting them to construct homes that will resolve the country’s need for adequate housing is just not realistic. In reality, a more accurate assessment, as noted by Francesco Piazzesi, founder of Échale’s predecessor (discussed below) and President and CEO of Échale a Tu Casa, is that, instead of being a partial solution to Mexico’s housing problem, self-building actually magnifies the situation by exacerbating the inability of so many Mexican families to possess adequate
housing and thus to build wealth through property ownership (personal communication, September 10, 2009).

Examined in this thesis for its innovative product and inclusive business model, Échale a Tu Casa is for-profit housing delivery entity, based in Mexico City, implementing an assisted self-build model designed to address the flaws inherent in the self-building process. According to Ecoblock International (2009b), the company was born out of a desire to find a way to overcome the rising price of construction materials to deliver efficient housing solutions to the poor throughout Mexico. Though originally a not-for-profit organization known as Adobe Home Aid (ADA) that began in 1985 as a means of providing relief to Hurricane victims, the organization eventually evolved into the for-profit Échale a Tu Casa it is known as today (Ecoblock International, 2009b).

The shift toward becoming Échale a Tu Casa began when the people behind ADA started to see the country’s larger housing needs and the lack of both affordable and appropriate housing solutions for Mexico’s BOP as a potential business and social development opportunity. As ADA evolved into Échale, it expanded its target market to include Mexico’s low-income to lower middle-income segments, where demand for housing has been found to be the densest and where the majority of homes are self-built and thus characterized by low and decreasing quality, increased maintenance needs, and construction periods of upwards of 15 years (Ecoblock International, 2009b). The company is now structured as a holding company that wholly owns the construction subsidiary and the company’s financing entity, Ecoblock International and since its inception, over 25,000 homes have been constructed through the Échale program and its predecessor entities (Ecoblock International, 2009a).

The core of the Échale business model is the Adopress 3000 machine, a patent-protected means of creating the Adoblock, a construction block, made of 70% dirt, 30% of water and cement, which, in addition to being cheaper, stronger, and more eco-friendly than the traditional cement block, also has both acoustic and thermal properties (F. Piazzesi, personal communication, September 10, 2009). In addition, the Adoblock was also designed to comply with the strict requirements of a comprehensive construction system (versus just a block with holes in it) whose final product, a stabilized cement floor, also complies with the building standards of Mexico, some of the strictest in the world. Finally, in addition to the
product obtaining approval from INFONAVIT, SHF and the Instituto Mexicano del Cemento y del Concreto (IMCyC), the Adopress 3000, is portable across communities and deskilled so that operation requires little more than loading the materials and pulling three different levels--features that enable the Adoblock to be produced locally by local self-constructors, and thus contribute to overall cost reduction.

According to Piazzesi, the design and creation of the Adoblock and Adopress 3000 were the result of the company’s search for an alternative construction material that was just as good as or better than the traditional cement block but whose price could be kept down for BOP consumers. Ultimately, the machine and the Adoblock were co-designed and created with ADA and the CRATerre Institute of the University of Grenoble in France, an institute dedicated to the study and promotion of the viability of soil as a construction material (Ecoblock International, 2009b).

The Business Model

Although there are several moving parts to Échale, the program can actually be summed up in the eight simple steps listed in Table 8 as listed in Ecoblock International, 2009a). With the portable and deskilled Adopress 3000, Échale is able to reduce the cost of delivering its homes to communities by employing local labor and producing the Adoblock on-sight. In addition, its overall business model is designed to address the numerous other BOP challenges involved with doing business in Mexico’s low income economies, such as being able to respond to a diversity of local needs while also maintaining the ability to easily replicate the business model into other BOP markets.

According to M. Lopez (personal communication, September 10, 2009), BOP consumers throughout Mexico have different needs, capabilities, and environments that influence both their housing needs and their abilities to participate in an assisted self-build program. For example, Rivera offered, extreme variations in geography, climate, and customs result in very different needs and preferences regarding housing design, while characteristics of BOP consumers and environments, in general, demand a sensitivity to local customs and power structures, the ability of a firm to build trust, overcome entrenched interests and unproductive mindsets to create cooperative participants, and create the capacity to consume in light of low incomes and the lack of access to credit.
Table 8. Échale a Tu Casa Business Model

<table>
<thead>
<tr>
<th>Step</th>
<th>Description</th>
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<tr>
<td>1.</td>
<td>Community identification&lt;br&gt;Upon identification of an interested community by a promoter, an introductory presentation of the entire program will be given to the interested community members.</td>
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<td>2.</td>
<td>Pre-Qualification Process&lt;br&gt;Community members that would like to commit to the program begin the pre-qualification process, which includes an extensive third-party review of background, work history, ability to pay, and credit history.</td>
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<tr>
<td>3.</td>
<td>Creation of SHPU&lt;br&gt;Those that qualify go on to form an SHPU whereby a social agreement is drafted to incorporate the future plans of saving and ultimately financing the purchase of a self-build kit. It is here when management is elected and a promoter is assigned to the SHPU.</td>
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<tr>
<td>4.</td>
<td>Savings period commencement&lt;br&gt;From there, the SHPU begins the yearlong savings process that serves as a prerequisite to the program.</td>
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<tr>
<td>5.</td>
<td>Delivery of self-build kit&lt;br&gt;Upon completion of the year-long savings requirement, the self-build kits are delivered to the SHPUs and the construction process can commence.</td>
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<tr>
<td>6.</td>
<td>Construction process&lt;br&gt;Homes are constructed over a period of seven to nine weeks through which construction is alternated among the individual homes within the SHPU.</td>
</tr>
<tr>
<td>7.</td>
<td>Loan payback period&lt;br&gt;Loans are paid back in a structured and streamlined process identical to the manner in which the savings were collected. Should a borrower fall behind on his payments, the guarantee and protection mechanisms in the SHPU will come into effect.</td>
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<tr>
<td>8.</td>
<td>Extinguishment of Loan&lt;br&gt;Upon the completion of the final payment at the term of the financing, the borrower has extinguished his obligations to EcoBlock and the loan is terminated.</td>
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The Échale model, F. Piazzesi (personal communication, September 10, 2009) noted, addresses these challenges through its two main symbiotic and interrelated components: the company’s financial products—which enable the consumer to finance the process, and the construction package and process—which involves working with local Social Housing Production Units (SHPUs) to co-create housing designs and ultimately results in the building of the actual Échale home.

**THE SAVINGS-CREDIT-SUBSIDY ECONOMIC MODEL**

Échale streamlines and facilitates the self-build process through the sale of housing kits to consumers. As noted in Ecoblock International (2009a), the kits, which can be built in as little as two months, are sold in three different home sizes and incorporate everything that an individual would need in order to construct their homes such as, construction materials (including the Adopress 3000 rental, cement, tools, iron etc), the technical assistance to oversee the process (a detailed construction manual, the full-time assistance of a trained mason to oversee construction, and a supervisor) and the architectural expertise to guarantee structural integrity and safety. The sale of the self-build kits is facilitated through the company’s capacity to finance the purchases of them much in the same way as an auto dealership where consumers can purchase and finance their autos simultaneously. As noted by Ecoblock International (2009a), Échale does this by way of its wholly owned subsidiary, Ecoblock International SA, a legally structured SOFOM, or non-deposit taking financial intermediary that has designed financial products to match the payment ability of borrowers with the cost of the self-built kits.

Échale has structured its financial economic model to include three aspects (savings-credit-subsidy), for those households that make no more than 5MW and two aspects (savings-credit) for those that make more than 5MW (F. Piazzesi, personal communication, September 10, 2009). According to Piazzesi, all participants in the Échale program are first required to demonstrate one full calendar year’s worth of savings before they can be considered eligible for financing a self-build kit. Typically people save whatever they can, which ideally, Piazzesi noted, is between 25% and 30% of their yearly income.

To facilitate the savings process, Piazzesi explained that Ecoblock has established a relationship with Banamex, one of Mexico’s leading banks, by using its credibility to set up
savings accounts for BOP borrowers to remit monthly savings, and to help overcome the deep mistrust many BOP individuals have of financial institutions. According to Piazzesi, Ecoblock makes sure that each participant receives a card with the name of the financial institution, account number, branch number, CLABE number, and their name which is used as a reference that allows the participant to see that every deposit he/she makes will be earmarked for the construction of his/her own home. The significance of providing these cards and a transparent system is that it not only builds consumer confidence and sophistication, but also gives consumers a sense of formal identity, something many of the poor, long been excluded from the benefits of the formal world, rarely ever get to experience.

Once the one year savings period has been completed, kits are delivered to the families and the financing begins. As noted by Ecoblock International (2009a), with this model, financing is made directly to the customer in the form of a loan and not in the property in the form of a mortgage. In order to mitigate the risks associated with this type of lending, Ecoblock’s products incorporate many of the best practices borrowed from successful housing microfinance entities that include several stops and guarantees to maintain the low default rates common to the microfinance industry (Ecoblock International, 2009a).

As mentioned, there are two different financing categories. Families that make over 5 MW fall into the savings-credit category while families that make less than 5 MW may also qualify for a government subsidy to put towards the financing of their home, putting them into the savings-credit-subsidy category. According to F. Piazzesi, in Mexico, the government has a subsidy program designed to provide one-time housing assistance to families that make up to 5 MW but has traditionally experienced great difficulty identifying qualifying recipients and distributing the money to them (personal communication, September 10, 2009). Partnering with Échale has given the government a way of identifying those families that qualify, distributing the funds, and obtaining an assurance that it is being used toward the provision of quality homes and has given Échale a way to better reach the country’s poorest sectors, creating a win-win-win scenario for the government, Échale and Échale’s consumers.
THE SOCIAL HOUSING PRODUCTION UNIT

The SHPU is made up of qualifying community members who have committed to the Échale program. According to F. Piazzesi (personal communication, September 10, 2009), each SHPU must agree upon and sign a social agreement that incorporates the future plans of saving and ultimately financing the purchase of a self-build kit. SHPUs are then held responsible for the distribution of industrialized materials that come with the kits, the production of the Adoblock, the promotion of the program—both inside and outside their own communities, and the construction of the self-build kits (Ecoblock International, 2009b).

The three main components of SHPUs as listed by Ecoblock International (2009a) are (a) a management team, composed of an elected President and Secretary as well as members of the Échale team that will serve as technical assistants to oversee the self-build process; (b) a promoter, elected by the community, who is responsible and compensated for introducing the program to neighboring communities and other interested SHPUs and servicing and coordinating the savings requirement and loan payback period, thus acting as the main liaison between the banking institutions collecting the payments and the SHPUs rendering payments, and Échale and the SHPUs; and (c) a developer/builder for the homes constructed. As discussed in detail later in this thesis, SHPUs both leverage the expertise of professionals provided in their self-build kits and are trained themselves in the production of the Adoblock and the construction of their homes.

WORKING WITH SHPUs TO CO-CREATE HOME DESIGNS

Once the SHPU has been established, the Agreement signed and the yearlong savings period completed, the self-build kits are delivered to the SHPUs and Échale begins to research the customs of the community to gain insights into what home designs are most appropriate and how the community works together (Ecoblock International, 2009a). In rural Mexico, for instance, many BOP communities have a system of “usos y custumbres,” or customary practices, in which they have established a system of working together and giving of labor for public works projects (Cohen, 1999). However, the extent to which people actually participate in these customs and the social repercussions that are associated with not participating differ from one community to the next (Cohen, 1999). Further, M. Lopez
(personal communication, September 10, 2009) explained that some communities barely talk to each other, while others have homes that are very close and people talk and work together more naturally. Culture is very different in this way, in different places, Lopez explained, and firms must be very respectful of the different customs of each community. Additionally, geography and climate can also play a big role in determining local needs and thus how homes must be designed.

A home in the desert will have very different needs from one located in the coastal areas or rainforests, so it is important to work with communities to learn how their environments shape their customs and needs. For example, some homes need to be more protected and others more open because of the heat. Also, not all communities sleep in beds, some here in Mexico sleep in hammocks so the house must be designed with places where they can be hung (M. Lopez personal communication, September 10, 2009).

According to M. Lopez, all of these locally specific differences create huge incentives for working directly with the community, which is why, in addition to the creation of SHPU s, Échale brings the families in to be active participants in the co-creation of their homes (personal communication, September 10, 2009). By co-creating, Lopez noted, Échale is able to address needs and customs that may not have been immediately apparent to the company and design a home that provides the most benefit and dignity to both the family and the community itself.

Describing Échale’s co-creation process with SHPU members, M. Lopez explained that once the Échale team has conducted all their research, a workshop is set up and all the SHPU members and their significant others are invited to participate in the designing of their individual homes (personal communication, September 10, 2009). Here, Lopez noted, husbands and wives are asked, separately, to draw the layout they would like for their home and inevitably each comes up with a very different idea for how the interior should be laid out, reflecting the different values each holds for the house itself. For example, Lopez offered the men tended to view the house as an object of value or how much it would be worth when finished and designed their layouts accordingly. The women, on the other hand, Lopez noted, tended to see the home in terms of its value for the family, or as something that must function around and facilitate the family life, thus their layouts were usually drawn to reflect a design that would best accommodate the family’s needs.
Once all designs have been drawn up, the professional advisors and co-creating family members work together to reconcile the differences and account for the local needs and legal housing standards and decide upon a final design. This final design is then officially drawn up to use during the construction process and although small changes such as the location of a door or window can still be made but at this point, the main design remains the same (M. Lopez, personal communication, September 10, 2009).

**CONSTRUCTION**

The next step in the Échale model transitions the SHPU into the construction stage. The company’s assisted self-construction process is characterized by the capacity building of individuals, through the training and support of home builders; local, paid labor; economic development; and a community effort. Thanks to the deskilled Adopress 3000, F. Piazzesi reported, qualified (or specialized) labor is required only for the construction process itself and includes one on-site architect and one trained mason per house in addition to one head supervisor per every 10 homes, thus allowing for costs to be kept to a minimum (personal communication, September 10, 2009). Additionally, Piazzesi noted that Échale also tries to purchase all housing products like windows and doors from local businesses in order to keep costs as local as possible for consumers and to help stimulate the local business economies. For each home, Échale trains seven individuals from the local community, five of who are trained to specialize in the production of the Adoblock and two who are trained and later certified in the actual construction of the house—a skill they can use for future employment long after Échale is gone (F. Piazzesi, personal communication, September 10, 2009). Each of these seven individuals is then paid for all the labor they contribute. According to Piazzesi, this paid labor aspect is crucial because low-income families often cannot afford the opportunity costs involved with giving up time they would normally use to earn money for the household to participate in the assisted self-construction project.

Ecoblock International (2009b) clarifies that the participating families are the first selected for these seven positions and when a participating family is not able to be a part of the team, the slot is deferred first, to the closest family members, and then to people from the community. Understanding the need for capacity building amongst community members who have usually had little if any formal training on home building, the Échale model also
integrates four training sessions per house at critical junctures of the pre-construction and construction processes so that homeowners can properly implement the program and take away transferable skills (Ecoblock International, 2009a).

The Échale homes are constructed over a period of seven to nine weeks through which construction is alternated among the individual homes within the SHPU. Although both men and women contribute to the laboring, to the surprise of Échale, the majority of the workforce is often the women and even the children (M. Lopez, personal communication, September 10, 2009). According to Lopez, this is often because the men usually still have to go to their other jobs but the women and children, excited about the prospect of their new homes, pick up the slack while the men are gone.

**THE ÉCHALE HOME**

When all is said and done, the Échale home stands as the tangible reminder of all the community has achieved and ways in which their lives were forever changed. The (basic model) finished home, explained by F. Piazzesi (personal communication, September 10, 2009), is built according to the United Nation’s (UN) established guidelines for a Vivienda Digna (Affordable Home) and is a 35 square meter basic unit that is designed to easily allow future additions of up to 72 square meters. Further, Piazzesi noted, because the blueprints are transferred to the homeowner upon completion of construction, the homeowner can expand or amend the home as he so chooses at anytime in the future.

According to F. Piazzesi (personal communication, September 10, 2009), the layout of the basic model includes one bedroom, one bathroom, one kitchen, and one dining room, as well as a basic hydraulic, electric and plumbing systems, a water tank (cistern) to store water, a place to wash clothes, and the following eco-friendly systems: a solar water heater, a patsari stove--which is designed to take smoke out and away from the house (a feature few unassisted self-constructed homes incorporate), and whose surface is made of a material (adobe) that stays cooler, thus decreasing the risk of children getting burnt; rainwater collection (to allow water to be accumulated and used for other things); sewage and a biodigester. Community surveys, noted in Ecoblock International (2009b), have indicated that the Mexican population largely prefers housing that maintains the appearance of a block and mortar type of construction. Thus, in addition to delivering environmentally sustainable
homes, the Échale program has been able to provide aesthetically-pleasing ones as well, an aspect the majority of the company’s competitors have, so far, not been able to do.

Further, the new home and the say and involvement families are given in its design and construction creates in the new homeowners a sense of pride, ownership and accomplishment, and gives them a visual reminder that they are capable of changing their own lives.

Most of these people and their grandparents have never lived in a home like this, one that allows dignity, so this is a life changing and generation changing thing for them. The parents and children see that this (a dignified home) becomes a reality for them, they see how they can work together to change their lives for the better (M. Lopez, personal communication, September 10, 2009)

Advantages and Disadvantages

In light of the many challenges present in Mexico’s homebuilding industry and its BOP in general, such as rising construction costs; inefficiencies involved with self-building (lack of resulting equity, lengthy time frames, lack of affordable, quality materials and lack of self-builder training); lack of access to credit and the nascent mortgage industry in Mexico; lack of networks and traditional value chain infrastructure; the characteristic low-margins/high volume demand for BOP businesses, local diversity, consumer skepticism, and lack of consumer sophistication, the Échale model has given the company numerous advantages.

Several aspects of the Échale model have contributed to its ability to keep costs manageable and commercial viability achievable. For example, the patent-protected construction technology and deskill Adopress 3000 have given the company a way to produce a cheaper, more functional Adoblock on sight using local labor. Second, the company’s vertically integrated business model consisting of its construction entity and its finance entity has allowed Échale to incorporate local labor, use minimal specialized labor, and leverage local financial capabilities. Third, Échale’s use of BOP appropriate costing mechanisms has prevented it from passing on expensive variable costs to the poor, such as the transportation of additional construction machines. Fourth, the company’s policy of sourcing as many materials as possible from the local community has also helped it keep costs as local as possible. As a result of these advantages, Échale expects to be fully
profitable and generating internal returns of 52% by the fourth quarter of 2010 (Ecoblock International, 2009a).

A major advantage of the SHPU is that it provides Échale with a specific way to easily replicate into various communities while also maintaining the flexibility needed to accommodate a variety of local demands and the diversity the company encounters from community to community. For example, replicated and established every time the company moves into a new community, SHPUs allow Échale the ability to become local, co-create solutions, create a capacity to consume, delegate responsibilities throughout the community and create accountability measures, and gain trust and commitment to the project, while simultaneously enabling the company’s ability to continuously scale into new communities. Further, Échale uses the SHPUs to create its own networks where none existed before. It accomplishes this by turning communities, where SHPUs were set up, into new branches of the company that continue to work to promote the Échale program among other households in that community and in additional communities throughout Mexico and prepare them for the creation of SHPUs of their own (Ecoblock International, 2009b). In terms of achieving scale through future housing projects, Échale’s strategy of constructing homes in such a way that allows for them to be expanded upon in the future; turning SHPU communities into branches of the company; and offering a housing solution that adds significant social value to communities have all given the company an advantage in creating demand, identifying and accessing new communities, and receiving direct referrals from both governments and NGOs.

Finally, getting involved at the community level and working with participants in such a way as to provide them with new jobs, economic stimulation, continuous training and ongoing support both toward a much-needed financial education and the development of construction skills that are transferable to future jobs, has given Échale a way to build and deliver homes efficiently (in as little as seven weeks, compared to the self-build’s usual 15-20 years); and develop trust, a shared vision, a strong company reputation, and BOP networks to help further Échale’s expansion throughout Mexico. This local intimacy has also enabled Échale to gain important local insights; develop appropriate housing designs; work respectfully and efficiently with communities; be in direct contact with the BOP so as to address issues immediately as they arise; provide ongoing support and training; stay on top of
changing needs and attitudes; influence mindsets and inspire communities to influence their own futures.

The disadvantages to the Échale model, as expressed by F. Piazzesi (personal communication, September 10, 2009) are few in comparison to the advantages but significant nevertheless. For example, the first disadvantage is the company’s susceptibility to construction material price shock. Even with the Adoblock, Échale still uses some materials in the construction of its homes that are subject to market-based pricing and thus any extreme price shock could cause a disruption in the business. The second and most significant disadvantage stems from the fact that the social investing concept is still in its infancy in Mexico. Because Échale, like most other BOP ventures, are characterized by low profit margins and thus the need for high volume, the company needs to be able to scale into multiple BOPs quickly. However, to do so, Échale must have upfront capital that would allow it to make numerous loans on the front end. According to F. Piazzesi (personal communication, September 10, 2009), to reach the 4.2 million people that can pay the social mortgage, the company needs approximately US $35 billion. Speaking to the potential that lies at the BOP, Piazzesi observed, “There are over a billion people living in the world that live in shacks. We can get the savings and credit from the people, but the problem is in the funding.” Without capital, loans cannot be made and without the loans, revenue cannot be made.

Though the company has made many efforts to obtain investments from larger companies, because the concept of social investing and investing in BOP markets is still so new, potential investors are still very skeptical and risk adverse. For example, according to F. Piazzesi (personal communication, September 10, 2009), most of the large organizations Échale has approached have wanted in return more collateral, more guarantees, the deed of the land (of which only 1% of the population has), or 70% rate of returns--all impractical demands when dealing with the BOP. Others organizations, Piazzesi added, have even conditioned funding on the exchange of up to 90% ownership in Échale or the deed of the company as collateral. However, Échale, Piazzesi insisted, is not willing to be bought out, largely because the people behind the company understand that in order for it to achieve its mission of bringing a new kind of freedom to families in need, a patrimonial democracy, the company must be enabled to keep its strong social focus. At the time of the interview with
Piazzesi, the company was partnering with microfinance organizations to provide financing beyond what Échale was currently capable of and exploring other funding options such as going public and creating a trust where all monies saved would go into one large pool instead of separate ones for each community.

**DISCUSSION OF FINDINGS**

The findings of this chapter, summed up in Table 9, offer numerous insights for informing the thesis questions regarding the major challenges to BOP entry and long-term success, how strategies are designed to address challenges and capture opportunities, what the advantages and disadvantages are from using these strategies and finally, what insights firms operating at the BOP have to offer. Although the three companies interviewed for this thesis hail from different industries (homebuilding, POU water systems and microinsurance) and naturally faced their own unique opportunities, access to resources, challenges, limitations and obstacles, their shared experience is attempting to do business in Mexico’s BOP with inclusive strategies.

Not surprisingly, the companies face some similar challenges in regard to obtaining BOP specific market insights; creating BOP appropriate and affordable products; engaging consumers whose income streams are small and unpredictable, whose access to credit is menial, and whose educational, consumer sophistication, and trust levels for new firms are low; designing effective entry and long-term business strategies for target markets that are spread all over the country and range from rural to semi-urban to urban spaces, live in areas with limited or non-existent networks and infrastructure, and have a diverse set of needs, capabilities, resources, and strategies for interacting with the world around them.

In regards to the findings regarding how strategies are designed to address these challenges and enable firms to take advantages of the opportunities identified, it is important to note that although the firms overall approaches are uniquely their own, many of the strategic elements that comprise them are common to three firm strategies and thus offer important insights into the effectiveness of the parts and how they are successfully combined and implemented. As a whole, all three firm strategies demonstrates the ability to access and engaging local BOP markets in a way that combines local inputs and an understanding of
Table 9. Chapter 6 Findings

<table>
<thead>
<tr>
<th>Challenges</th>
<th>Non-Traditional Partner Consequences</th>
</tr>
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<tbody>
<tr>
<td>• Lack of BOP specific insights and market research</td>
<td>Positive:</td>
</tr>
<tr>
<td>• Low and unpredictable incomes</td>
<td>• Allowed immediate distribution of</td>
</tr>
<tr>
<td>• Low consumer sophistication</td>
<td>products and the leverage of</td>
</tr>
<tr>
<td>• Target market’s lack of access to credit</td>
<td>partner’s reputation and intimacy</td>
</tr>
<tr>
<td>• Widespread target markets with different local needs and circumstances</td>
<td>with BOP consumers</td>
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<tr>
<td>• Non-existence of or limitations in existing networks and infrastructure</td>
<td>• Helped create a capacity to consume</td>
</tr>
<tr>
<td>• Developing trust</td>
<td></td>
</tr>
<tr>
<td>Strategies</td>
<td>Negative:</td>
</tr>
<tr>
<td>• Performed on the ground research</td>
<td>• Appropriate partners were not always</td>
</tr>
<tr>
<td>• Developed products designed specifically for BOP consumer needs</td>
<td>available</td>
</tr>
<tr>
<td>and capabilities</td>
<td>• Partner’s had limitations in regard</td>
</tr>
<tr>
<td>• Used BOP appropriate costing mechanisms and priced products</td>
<td>to consumer confidence, urban</td>
</tr>
<tr>
<td>affordably</td>
<td>reach, and scaling-out</td>
</tr>
<tr>
<td>• Used non-traditional partners</td>
<td>• Outsourcing customer relationships</td>
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<tr>
<td>• Facilitated one-to-one interactions, capacity building through education</td>
<td>to partners left firms out of</td>
</tr>
<tr>
<td>and training, and co-created efforts to create a shared vision and</td>
<td>touch with consumers and without a</td>
</tr>
<tr>
<td>win trust</td>
<td>real understanding of the BOP</td>
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<tr>
<td>• Designed models simple enough to replicate yet flexible enough to</td>
<td>market</td>
</tr>
<tr>
<td>address local differences</td>
<td></td>
</tr>
<tr>
<td>• Created a capacity to consume</td>
<td></td>
</tr>
<tr>
<td>• Developed value chains by forming their own relationships, networks,</td>
<td></td>
</tr>
<tr>
<td>and channels</td>
<td></td>
</tr>
<tr>
<td>• Maintained upper management attention to BOP venture</td>
<td></td>
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<tr>
<td>Target markets</td>
<td></td>
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<tr>
<td>• Demand for products found in BOP households exceeding $6,000 per year</td>
<td></td>
</tr>
<tr>
<td>• Demand for products found in TOP markets for 2 out 3 firms</td>
<td></td>
</tr>
<tr>
<td>• Conflicts with investor demands created challenges for the pace of scale</td>
<td></td>
</tr>
<tr>
<td>firms were capable of and for scaling into the harder to reach places</td>
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</tr>
</tbody>
</table>

Valuable community resources: the women

• Responsible for household budget and majority of purchases for the family
• Tend to be the savers in the family
• Entrepreneurial potential
• Participate in hard manual labor beside or independent of the men, often with their children strapped to their back or helping alongside
local capabilities and limitations; accommodates local demands; enables consumers; contributes to economic and social development; and is capable of being replicated and scaled into a variety of BOP markets. In terms of their parts, all the firm strategies incorporate to some extent co-creation, capacity building, the use of non-traditional partners, and social embeddedness, providing further support for the findings in London and Hart’s (2004) study.

Presented in Table 9 is an overview for some of the specific ways these elements are incorporated into business strategies to not only address the challenges at hand but to help transform them into valuable firm resources and more capable consumers. For example, where deeper insights of the BOP are needed, firms supplement available market research with their own on-the-ground R&D initiatives. Where low incomes, a lack of access to credit, a difficulty finding products to meet their needs, and high amounts of uncertainty create consumer demands for products with high functionality and low pricing firms have created products designed specifically for the BOP consumer’s needs and capabilities, allocated costs in a way that kept the larger ones from being passed on to the consumer, create a capacity to consume through the provision of in-house micro-financing options (when capital is available for doing so), partnering with microfinance institutions, utilizing government subsidies, facilitating job creation, and/or setting up savings programs to leverage existing monies. When an environment places demands for a business model to be capable of both addressing a variety of local demands and scaling into multiple geographical areas, firms have created platform solutions flexible enough to incorporate local inputs while standard enough to replicate easily from place to place.

The firms take different approaches to how their strategies are designed to incorporate local inputs but found in all are efforts to co-create products, designs, or community infiltration and to capacity building to develop greater capabilities in the people both as consumers and participants in the firm’s business model itself. For example, Échale uses a basic housing kit and SHPU, each of which has basic guidelines to follow but are flexible enough to account for a variety of capabilities and local variations, to co-create solutions, and to train households to participate in the labor of building their homes. Additionally, TWI has designed its POU technology as a platform that is uses to address a variety of water quality needs and co-create with communities. Once in the community, the
firm follows a basic set of pre-established guidelines for establishing and training value chains from location to location. The local partners provide valuable BOP insights and serve as a product promotion and sales force. Finally, Seguros Argos uses platform-like mutuals that are equipped, trained, supplied, and supported by Argos but owned and operated by people from the BOP. Argos maintains a close relationship with these mutuals, allowing Seguros to achieve a greater level of social embeddedness and to stay on top of changing needs, demands, and consumer situations and to co-create new products.

In regards to capacity building the firms use trainings, presentations, hands on demonstrations, and ongoing supervision support during the learning process to help increase consumer sophistication and to develop overall and firm specific skills. This aspect is incorporated into firm strategies in various ways such as teaching individuals how to participate in formal savings programs, obtain and repay microloans, become effective sales people, promoters and other key value chain and business model participants, and helping them to become more familiar with products and firm processes.

Finally, to compensate for absent or fragmented infrastructure and a lack of formal institutions, the firms create ways to gain trust, buy-in, and access to consumers through two main approaches: the use of non-traditional partners and going into communities directly. For example, when available—as in the case of Argos—non-traditional channels are being used to distribute products, educate consumers, accept payments, and transfer the trust and relationships that have been built with the BOP over the years to the firm via association. The second method the firms are using is going into the BOP themselves to work with the people and communities in a more direct and inclusive manner. With this approach, firms are developing their own relationships and networks, working with the people directly, and developing their own trust and one-to-one relationships which are then used toward developing product awareness, community involvement, value chains, consumer sophistication and other such strategic elements.

The findings derived from the experiences of firms involved with using non-traditional partners provided some unexpected insights in regards to the both the negative consequences of relying on non-traditional partners to supply the trust, BOP insights, and distribution channels to consumers and the potential competitive advantages of going into communities to form relationships and networks directly. For example, according to the
experience of these firms, outsourcing the contact with consumers to non-traditional partners may allow firms to start product distribution quicker, but it also leaves firms out of touch with their consumers. On the other hand, going into communities directly and establishing their own relationships allows the firms to co-create with communities; gain a deeper understanding of BOP needs, environments, and ways of living; develop trust, a shared-vision, company specific value chains, and reputational benefits. Given the harsh realities; extreme sensitivities; and very different environments, needs and characteristics of people at the BOP, firms seeking to achieve long-term success in these environments cannot not afford to be out of touch. Thus, although BOP researchers, like Prahalad (2006) and Simanis and Hart (2009) have asserted that companies seeking to access BOP consumers should partner with non-traditional partners to leverage their BOP intimacy, understanding, relationships, and trust, the experiences of the companies interviewed here indicate that although such partnerships can certainly be beneficial, depending on them too much might actually put the firm at a disadvantage.

In regard to the advantages and disadvantages that arise from the use of specific inclusive strategies, a summary of the different advantages and disadvantages discussed in each case study throughout this chapter is presented in Table 10. Overall, for each firm, the advantages of the inclusive strategy that have been derived from using the inclusive strategy have far outweighed the disadvantages. The strategies allow the firms to obtain valuable BOP insights; develop innovative products that are capable of meeting an important need; develop and utilize existing resources, mechanisms, and networks to create entirely new and more efficient ones; design business models that are beneficial to both the firm and the company; create and leverage trust and social relationships; and attend to local needs while maintaining the ability to scale into a variety of other geographical locations.

The disadvantages speak largely to the limitations the models face as a result of the weaknesses in existing channels (management, scale ability, and urban reach) and the still underdeveloped and thus largely unfamiliar concept of BOP venture investments. For instance, the smaller firms in this chapter (TWI and Échale) have emphasized that to achieve the volume that produces large social and financial gains, they must obtain the capital that would allow them to move into multiple areas, and get loans and projects set up and going. According to R. Wells, (personal communication, July 1, 2009) it usually takes about two
### Table 10. Business Model Advantages and Disadvantages

<table>
<thead>
<tr>
<th></th>
<th>Initial model Advantages</th>
<th>Initial model Disadvantages</th>
<th>Mutual Model Advantages</th>
<th>Mutual Model Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Seguros Argos</td>
<td>- Ability to assess risk and insurability of consumers through methods more appropriate to BOP environments&lt;br&gt;- Ability to begin immediate distribution and product education and leverage trust through existing channel partners&lt;br&gt;- Product and process design (prompt cash distributions) builds firm credibility&lt;br&gt;- Sustainable</td>
<td>- Limitations of existing channels become firm limitations&lt;br&gt;- Few urban channels&lt;br&gt;- Firm out of touch with BOP consumers and environments</td>
<td>- Additional professional channel options with which the firm has greater influence&lt;br&gt;- Increased opportunities for scaling up&lt;br&gt;- Increased consumer sophistication&lt;br&gt;- Closer contact with BOP consumers and co-creation of new products designed with and for BOP consumer needs&lt;br&gt;- Access to grant funding&lt;br&gt;- Expected to be sustainable</td>
<td>- Limited urban reach</td>
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<tr>
<td>Microinsurance</td>
<td></td>
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<tr>
<td>The Water Initiative (TWI):</td>
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<tr>
<td></td>
<td>Advantages</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>- Product platform design gives flexibility needed for local needs and simplicity needed for replication and scale&lt;br&gt;- Competitive advantages of trust, loyalty, and BOP understandings by going into communities directly and forming new relationships, networks, and value chains&lt;br&gt;- Influential community members open doors in the community by becoming spokeswomen and distributors for the firm&lt;br&gt;- A capacity to consume is created through appropriate pricing and financing options&lt;br&gt;- Product ability to capture additional demand for TOP markets&lt;br&gt;- Sustainable</td>
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<td></td>
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<tr>
<td></td>
<td>Disadvantages</td>
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<td></td>
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<tr>
<td></td>
<td>- Difficulty scaling into harder to reach rural areas due to conflicts with investor goals</td>
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</tbody>
</table>
Table 10. (continued)

<table>
<thead>
<tr>
<th>Échale a Tu Casa Assisted Self-built Housing</th>
<th>Advantages</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>• Manageable costs for firm and consumers</td>
</tr>
<tr>
<td></td>
<td>• Utilization of local labor</td>
</tr>
<tr>
<td></td>
<td>• A shared vision is created with the community, instilling loyalty to project</td>
</tr>
<tr>
<td></td>
<td>• Social Housing Production Units provide replicable platform solutions with flexibility to address local needs and situations</td>
</tr>
<tr>
<td></td>
<td>• Firm specific networks are created where none existed before</td>
</tr>
<tr>
<td></td>
<td>• A capacity to consume is created that develops a culture of savings and accountability and increases consumer formal financial sophistication</td>
</tr>
<tr>
<td></td>
<td>• Economic and social development through education, training, paid labor, skill development, local sourcing of materials, and certifications for new skills acquired</td>
</tr>
<tr>
<td></td>
<td>• Multiple methods for referrals generated</td>
</tr>
<tr>
<td></td>
<td>• Company placed close to BOP and in continuous contact with consumers that allows local insights, identification of changing needs and wants, and a deep understanding of BOP consumers and environments</td>
</tr>
<tr>
<td></td>
<td>• Delivery of a dignified home in 7 weeks</td>
</tr>
<tr>
<td></td>
<td>• Sustainable</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Susceptible to construction material price shock for non-Adoblock materials</td>
</tr>
<tr>
<td>• Difficulties in obtaining funding on the front end due to investor doubt and unfamiliarity with BOP ventures</td>
</tr>
</tbody>
</table>

years for a BOP venture to get going on real revenues. However, most investors are accustomed to developed market initiatives where infrastructure is already in place and consumers are more affluent. Thus they are used to investments that provide high returns in much shorter time frames. In the meantime, firms like TWI and Échale provide evidence, that these strategies can still profitable and sustainable even while moving at a slower pace. Overall the findings of this chapter are consistent with greater BOP literature in general in regard to the effectiveness of inclusive strategies with and the work of London and Hart (2004) in particular in terms of the effectiveness of elements like co-creation, capacity building, non-traditional partners, and social-embeddedness.
Additionally, the findings provided support for the claims of researchers like Hart and Milstein (2003) and Prahalad (2006) that maintain the BOP represents significant opportunities for firms who learn to look at it from a different perspective and understanding and seek out ways to work with the existing resources rather than seeking to overcome limitations in the short term. Additionally, the findings in this chapter regarding potential target markets reveal that not only is there a market at the BOP with those households making US $6,000 per year but firms are also finding demand for their products from households exceeding this figure in the lower-middle classes. Furthermore, two of the three companies have already experienced demand coming from TOP markets. Such findings confirm the theories of Prahalad (2006) and Hart and Milstein (2003) that the BOP represents unique innovation opportunities for firms where products designed for the BOP may ultimately find additional markets at the TOP from consumers currently served by inferior products.

Finally, BOP research has revealed that in many developing countries the role of women at the BOP, when it comes to saving, spending, and acting as entrepreneurs, is significant and some companies have found that incorporating capable women who are influential within their communities into business models gives firms business representatives who know the people and are trusted by them. Based on the experiences of two of the firms interviewed for the thesis and literature on the microfinance movement in Mexico, such claims appear to be applicable in Mexico’s BOP as well. For example, TWI trains and equips women to act as spokeswomen, salespeople, and promoters while Échale incorporates both men and women into the design, production, labor, and administration processes of the model.

As a final note regarding the findings of this thesis, Mexico’s BOP contains many unique variables, both static and dynamic, that work together to influence the specific needs, limitations, and capabilities of BOP households and often differ from region to region and even neighborhood to neighborhood and create high incentives for firms that lack real insights and understandings of BOP markets to become more socially embedded and localized, confirming the findings of London and Hart (2004). However, overall, the country’s BOP shares many of the attributes as those described in other BOPs throughout the literature. Similarly, the findings regarding the major challenges for doing business in
Mexico’s BOP are not unique to Mexico alone and thus, the findings of this thesis should easily be transferable into other countries as well.
CHAPTER 7

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

This chapter will review the study and is divided into three sections. The first will provide a brief summary of the study to include its conceptual framework, primary purpose, and design of the investigation. The second section will present important findings and the resulting thesis conclusions. Finally, the third section will offer recommendations and discuss the implications of some for future research.

SUMMARY

Recently it has been suggested that instead of being disillusioned by the fewer than anticipated numbers of middle classes found in EMs, firms should start to see the large numbers of low-income people at the BOPs as economic beings who have thus far been largely excluded from markets and the benefits of globalization, and who, collectively, represent the new markets firms have been searching for. According to some researchers, although it is true that individually these people represent much smaller margins, their sheer volume--approximately two-thirds of the world’s population representing a potential market of almost US $13 trillion (Hammond & Prahalad, 2004)--suggests the potential for very significant profits for company’s willing to engage them.

Although the difficult and very different environments of EMs and particularly those of the BOPs there have rendered many firm strategies ineffective, causing many to question whether or not the hazards and unfamiliarity of these markets serve to negate any possible first-mover advantages a firm might obtain, a new group of BOP researchers have taken a different perspective. These researchers suggest that the failure of companies in EMs may have more to do with their use of inappropriate strategies and less to do with the “impossible” scenarios represented by EM conditions. In light of the substantial potential for future markets in the BOP and the increasing anti-globalization sentiment and protests, researchers like London and Hart (2004), Prahalad (2006), and organizations like
WBCSD (2005) believe that firms should begin to think more inclusively in regards to their strategies to create a more inclusive capitalism that proves that new markets can benefit all. If done correctly, these researchers believe firms can benefit from a dual social and financial return as doing business becomes an opportunity to both increase the financial bottom line and contribute to poverty alleviation through the development of markets and consumers.

A review of the strategy literature reveals that because most firm strategies have been focused on the TOP markets of developed countries, there is little literature regarding how firms should proceed into BOPs. Currently the BOP strategy formation is in its initial stages with only a handful of MNCs even attempting new strategies and many academics continuing to remain skeptical of the need for strategy development specific to BOPs at all. However, the aforementioned BOP researchers and others, like the IDB and WBCSD have created a starting point with case studies, lessons produced from trial and error experiments, reports and a couple exploratory studies comparing successful and failed or failing firms at the BOP for insights into key factors for BOP success. So far, there have been only a few emerging strategies from the numerous experiments currently being tested in BOPs. Yet, one thing is clear from all the experiences so far, firms will need to gain a better understanding of and visibility on the heretofore extremely unfamiliar environments of EMs and their BOPs and learn to work with them, not in spite of them.

Doing business in EM countries, alone, poses numerous challenges to firms in terms of infrastructure, security, rule of law, crime, corruption, and different ways of doing business. At the BOP, the psychic distance that firms face is multiplied as the severity of these challenges increases and the unfamiliarity of the BOP environment and consumer are tacked on. Given the very different environments, realities and capabilities found at the BOP, especially in those of developing nations, and the experiences of firms there, several researchers have come to believe that for companies to be successful, they are going to have to take very different approaches than those they have become accustomed to. For example, the low and unpredictable incomes, high levels of social deprivation, and low levels of education, literacy, and consumer sophistication may require firm initiatives toward building local capacity and creating a capacity to consume (London & Hart, 2004; Prahalad, 2006) different approaches in regards to promotions and marketing to accommodate more concrete reasoning consumers (Viswanathan et al., 2005).
Further, several researchers have found that the informal and highly social nature of BOPs appears to require firms be able to create social capital and/or to become embedded in the social infrastructure that dominates these markets if they are to gain the trust they need and overcome the lack of formal institutions in BOP markets. To this end, BOP researchers recommend firms recognize that large scale efforts to target the masses all at once simply aren’t feasible in these environments and that smaller scale, bottom-up initiatives, designed to be inclusive and capable of both addressing local needs and replicating into multiple regions are more likely to create competitive advantages and find success in BOP markets. According to Preston et al. (2007), the BOP can represent a stable and substantial market for companies willing to engage in it responsibly and with commitment and creativity, and despite the claims of previous studies regarding the EM negation of first-mover advantages, researchers like Arnold and Quelch (1998) assert that firms that move now stand to gain huge advantages over latecomers in regards to BOP information and understanding, relationships and networks, and reputation establishment.

Although some firms have attempted to gain social legitimacy through CSR efforts that are non-related to their core business activities and thus unsustainable over the long-term, organizations like the WBCSD along with BOP researchers like Brugman and Prahalad (2007) and Simanis and Hart (2009) claim that companies should think bigger and recognize the opportunity to create win-win scenarios where the poor are incorporated into the business model itself in such a way that creates real advantages for the firms and economic development opportunities for the markets they are serving. In this way, market and economic development can occur naturally, as firms are allowed to focus on what they do best--doing business.

However, given the relatively new focus on BOP markets and inclusive-style strategies to most firms, there currently exists very little in the literature on what kinds of inclusive strategies and approaches are most effective. Furthermore, most of the current BOP strategy literature is broad based, addressing BOPs and strategies as a whole versus a more specific country to country approach. In light of the fact that every country has its own unique variables, as well as characteristics common to BOPs worldwide, which may influence strategy formulation, this thesis adds to the current BOP literature first, with its analysis of Mexico—a country that shares many characteristics with other Latin American
countries--and it’s BOP market potential and characteristics; and second, with case studies incorporating industry and strategy insights from firms currently doing business in Mexico’s BOP using some form of an inclusive strategy.

The purpose of this thesis is to highlight some of the important characteristics of BOP consumers and the environments in which they live in order to enable a better understanding of the needs and realities of the people who live there and to provide a more informed “jumping off point” for strategy formulation; to examine Mexico’s BOP potential and characteristics to gain insights into any unique opportunities, challenges, capabilities and limitations represented there; and finally, through three case studies, to extract insights from firms regarding (a) how Mexico’s BOP influenced the formulation of strategies (b) how strategies incorporated inclusive elements and (c) what, if any, advantages or disadvantages were derived from doing so.

To address the thesis questions, the thesis is divided into seven chapters. Chapter 1 contains the introduction and plan of the thesis. Chapter 2 provides a background on the BOP with a discussion of some of the distinctive characteristics of low-income sectors and consumers and presents the basic theory of BOP markets and the proposals regarding its market potential. Chapter 3 uses aggregate statistical data compiled by INEGI, Mexico’s national statistical bureau, along with international NGO indexes and other literature sources to provide an overview of Mexico and its BOP characteristics and market potential. Chapter 4 then provides a review of the emerging market, global, and BOP business strategy literature to see what kinds of existing insights were available for informing firms on how to proceed into BOPs.

The literature review highlights some of the current advantages, disadvantages, and overall experiences firms were noting from using their traditional strategies in EMs and BOPs. Further, it sheds light on how experience in BOPs is influencing firm attitudes and approaches toward doing business at the BOP; what, if any, global trends firms are emerging; and what kind of new information, insights or strategies are emerging in the literature. Further, the review reveals that the majority of strategy literature over the years has focused mainly on the TOP markets of developed countries and though the literature on EMs has begun to grow, studies specific to BOPs have been largely absent. However, insights are available regarding the frustrations and disadvantages firms have encountered when trying to
employ traditional strategies in EMs and BOPs, and through a comparative analysis of the literature on firms using traditional strategies against the literature on firms using more innovative approaches, the thesis was able to glean a deeper understanding of the people and environments found in EMs and their BOPs. Finally, new approaches and emerging characteristics of successful BOP initiatives are revealed and subsequently used to guide the research efforts of the thesis.

Chapter 5 provides a methodology for the research effort that produced the findings for Chapter 6. Chapters 6 presents and discusses the findings of the research from three case studies obtained from semi-structured, open-ended interviews conducted with three companies from three different industries using inclusive business strategies in Mexico’s BOP. Two of these companies were domestic firms and one was an international new venture. The areas addressed in the interviews and discussed in Chapter 6 are (a) the BOP need/opportunity addressed; (b) the major challenges as perceived by the company to successful market entry in terms of accessing and engaging potential BOP consumers; (c) the products and business models designed to exploit the opportunities identified and to successfully address the challenges at hand; (d) the major advantages and disadvantages of, or limitations to, the company’s specific business model/mode of entry; and (e) the learning that has come from the company’s experiences in and with the BOP. Finally, Chapter 7 provides a summary of the overall thesis effort, discusses the limitations of the study, and presents the final conclusions and recommendations for going forward.

In regard to the limitations and weaknesses of the study, some of the main limitations of this research were in regard to the reliability of the data compiled by INEGI. For instance, the three main challenges as listed by Negrete (2006) were are (a) in regard to the fact that accounting practices for economic aggregates assume accounting at a production units level, yet, by definition, the informal sector does not follow conventional accounting practices; (b) in regards to obtaining accurate income/revenue figures as in an informal sector that, by nature, is particularly adverse to declaring its production and income levels; and (c) in regards to the ability to determine earnings and expenditures on an annual basis based only on data given for one quarter of a year, especially when considering that “no small number of activities in the informal sector offer a marked seasonal character (acute variations as the year goes on) as well as changes according to the season of the kinds of service or goods
being offered” (Negrete, 2006, p. 5). However, understanding these limitations, INEGI has
designed its surveys to incorporate some creative solutions to capture information through
more indirect routes and experimented with a method for inferring the activity level year
without needed month by month sales inputs (Negrete, 2006). However, it is important to
note that INEGI is a professional, national statistical agency and the measurement issues
raised by Negrete above are not particular to only Mexico and INEGI but are, rather, general
issues that stand out wherever national statistical agencies try to measure informality and
BOP households and businesses. Thus the limitations of the data are in the nature of the
measurement, not in INEGI’s approach or institutional capacity.

The second limitation of the study was in regard to the small sample size of case
studies conducted for the thesis. Time and money constraints allowed for only a few firms to
be interviewed in regard to the thesis questions, and, as a result, it is difficult to make any
broad generalizations or to draw inferences about larger patterns based on the strategy
insights derived from the three firms in the thesis. However, all appropriate guidelines and
procedures for conducting research were followed and insights did appear to support other
BOP studies from the literature as well offer helpful hints for creating competitive strategies.

**Conclusions**

Mexico and its BOP share many of the same characteristics as those described being
present in other developing countries throughout the globe. Such characteristics include a
high incidence of urbanization, over burdensome regulatory environments, high levels of
inequality and poverty, large informal economies, gaps in infrastructure, widespread
corruption, and lack of transparency with government officials. Further, many people at the
BOP can be characterized by low levels education, unpredictable income streams, and
limited access to credit, markets, and opportunities. Although it is true that the country’s
economy has been growing and improving per capita income levels for all income segments
throughout the years, high levels of inequality have contributed to keeping nearly half the
population at the BOP. Despite the increases in GDP and overall income over the years,
Mexico still struggles to create enough formal jobs to cover the labor force’s new entrants
(971 thousand jobs created to 1.14 million new entrants per year; Garcia-Verdu, 2006) and
the informal sector is still estimated to account for a good 30-40% of the country’s economic
activity, suggesting there may be some validity to the claims of De Soto (2000), Peng and Luo (2001), and Arnold and Quelch (1998) that assert that large groups of people in countries, like Mexico, that experience significant levels of inequity may be hindered from following a path toward “westernization” (or modernization to use a less ethnocentric term) and be left on the outside looking in.

Though Mexico’s BOP exhibits many of the same characteristics as those in other developing countries throughout the world, there remain many unique variables, both static and dynamic, that work together to influence the specific needs, limitations, and capabilities of BOP households and can differ from region to region and even neighborhood to neighborhood. Such variables include things like variations in geography, climate, communities, informal sector dynamics and hidden rules, local governments, people, cultures, customs, levels of exposure to markets and globalization, and household experiences of poverty and marginalization. These unique aspects of BOPs create high incentives for firms that lack real insights and understandings of BOP markets to become more socially embedded and localized, confirming the findings of London and Hart (2004).

On the whole, Mexico’s smaller cities tend to show higher rates of social deprivation, as a percentage of the population, than do larger cities. However, the severity of the poverty issue appears to be greatly influenced by regional factors. For example, Mexico’s central and southern regions, where the country experiences its highest levels of social deprivation, are where 38.6% of the country’s cities that report very high levels of marginalization are found clustered in just the four states of Mexico, Vera Cruz, Puebla, and Guerrero. Although regions with low social deprivation levels may indicate regions where income is able to be spread a little further, areas with high deprivation may represent significant opportunities for those firms capable of seeing opportunities in the gaps.

INEGI measures income groups in terms of the minimum wage multiple households fall into. Those groups with incomes up to US $6,000 were represented by minimum wage multiples 1-6. According to the data provided by INEGI for one quarter, the average total quarterly income per household for this group was US $934 and the average total quarterly expenditures per household was US $968—representing a collective US $14.9 million dollars per quarter when multiplied by the categories’ 14, 859, 831 households. Additionally, a breakdown of household expenditures revealed that the main categories of current spending
money for these households were food, beverages and snuff (46%); transport and communications (17%), education and recreation (14%) and housing and fuels (12%) and personal care and clothing and footwear each with 7%. Of these the major subcategories were found to be food and beverages consumed in the household, public transportation, education, electricity and fuels, and prescription drugs. Further, there was an average 21% increase in overall expenditures with each increase in minimum wage multiple. Of additional note, though not listed in the INEGI statistics, Ecoblock International (2009b) reported that low-income households were also estimated to spend an average of 30% of their annual income on housing. Such expenditure figures appear to confirm previous claims from authors like Prahalad (2006) that low-income households are still economic entities that collectively represent a significant market opportunity.

In regards to the findings regarding how strategies are designed to address these challenges and enable firms to take advantages of the opportunities identified, it is important to note that although the firms overall approaches are uniquely their own, many of the strategic elements that comprise them are common to three firm strategies and thus offer important insights into the effectiveness of the parts and how they are successfully combined and implemented. As a whole, all three firm strategies demonstrate the ability to access and engaging local BOP markets in a way that combines local inputs and an understanding of local capabilities and limitations; accommodates local demands; enables consumers; contributes to economic and social development; and is capable of being replicated and scaled into a variety of BOP markets. In terms of their parts, all the firm strategies incorporate to some extent co-creation, capacity building, the use of non-traditional partners, and social embeddedness, providing further support for the findings in London and Hart’s (2004) study.

The findings derived from the experiences of firms involved with using non-traditional partners provided some unexpected insights in regards to the both the negative consequences of relying on non-traditional partners to supply the trust, BOP insights, and distribution channels to consumers and the potential competitive advantages of going into communities to form relationships and networks directly. For example, according to the experience of the firms, outsourcing the contact with consumers to non-traditional partners may allow firms to start product distribution quicker, but it also leaves firms out of touch
with their consumers. On the other hand, going into communities directly and establishing their own relationships allows the firms to co-create with communities; gain a deeper understanding of BOP needs, environments, and ways of life, develop trust, a shared-vision, company specific value chains, and reputational benefits. Such insights and experiences give firms advantages in developing strategies capable of creating the social capital needed where formal institutions have failed. For instance, by creating a shared-vision with the community, some of the firms interviewed were able to delegate responsibility and accountability enforcement among the various new value chain participants. This allows social capital to be leveraged in a way that also created a shared sense of responsibility and accountability. Because the failure of one affects everyone, this system allows firms to substitute social capital and social pressures for formal institutions and enforcement mechanisms.

Some of the greatest opportunities for doing business in Mexico’s BOP appear to be in finding ways to bridge the gap between exclusion and inclusion. In Mexico the effects of exclusion can perhaps be seen most clearly in the difficulty of obtaining even the most basic of needs, such as affordable housing, insurance, and quality drinking water. However, when considering that currently there are so few firms attempting to address these needs and that the needs are not just specific to Mexico, but are in fact existent worldwide, the vastness of the opportunity begins to reveal itself. Further, as experienced by two of the firms in this thesis, innovative products developed for BOPs consumers are sometimes transferable to TOP markets, creating additional market bases for firms and proving that BOPs can represent the forums for innovation capable of benefiting both BOP and TOP consumers as suggested by Prahalad (2006).

Still, in markets where incomes are small and unpredictable, social needs are high, and opportunities for advancement are scarce, there is an order to doing business with the poor that will need to be addressed before firms will see rapid assimilation of their goods, especially into the long-term. Thus, strategies that help provide the poor with access, not just to goods and services, but to opportunities, market development, and increased consumer sophistication seem to be better capable of positioning firms to benefit from long-term gains in revenues, reputations, market insights, and market growth, as the markets they invest in become more capable consumers. Further, strategies created with social and financial goals that seek to create win-win situations, appear to offer additional opportunities to firms in
terms of international and local NGO and state and local government financial (grant money and subsidies) and promotional (referrals) support.

When incorporated into the business model itself and given the appropriate training and support inputs, it appears that BOP consumers can also provide great advantages to companies in regards to obtaining local insights, creating appropriate products and strategies capable of meeting local demands, reducing costs, forming value chains, benefiting from local labor, establishing trust and social capital, and developing local markets. Thus, as suggested by London and Hart (2004) and WBCSD and SNV (2007), it appears that by providing opportunities, market development, and capacity building to the poor, firms can simultaneously benefit in regards to both their bottom line and their long-term reputations. Additionally, such an intimacy with BOP markets may also place firms in a better position to observe and understand how they influence both positive and negative spillovers, a current firm limitation noted previously by Meyer (2004), and then to adjust their strategies accordingly, either to build on the positive or to reduce the negative, before it gets out of hand—a crucial preventative measure in highly sensitive BOP environments.

The experiences of the firms interviewed by this thesis bring to light potential disadvantages of entry strategies seeking to rely on non-traditional partners like NGOs and social entrepreneurs for BOP relationships and trust. First, there may not always be appropriate organizations available to partner with. Second, potential partners often come with their own limitations, as was the experience of Argos whose partners were limited in their management and professional skills which in turn affected their consumer’s confidence in them and their ability to stay healthy and to scale into additional locations. Finally, outsourcing the relational pieces to partners can actually place firms at a disadvantage by keeping them out of touch with their BOP consumers and environments and thus denying them the same competitive advantages possessed by firms that take their inclusive models directly to communities.

The most significant challenge facing two of the three firms interviewed for the thesis is obtaining the upfront funding needed to enable firms to scale immediately into the multiple local BOP regions housing their target markets. The firms attributed this difficulty in large part to the investing community’s unfamiliarity with the very different nature of BOP ventures and the subsequent time expectations investors placed on returns. For instance,
currently, investors, more accustomed to TOP market investments in developed countries, are taking the traditional investing approach that demands returns on investment quickly, in the short-run, in order to keep them investing in what they perceive to be high risk scenarios. However, BOP ventures, especially those with a dual social and financial return, often require significant upfront investments that need investors to take a more medium to long-term approach in order to allow firms to create appropriate products, perform the necessary, on the ground research, and scale into as many areas as possible so as to obtain the type of volume needed to produce the significant returns anticipated by investors without sacrificing the quality of their offering.

**RECOMMENDATIONS**

When comparing the demands of the BOP to Bartlett and Ghoshal’s (1989, 1998) four main strategy types, the transnational strategy, with its focus on both standardization and local intimacy, comes the closest to being the most appropriate. However, as evidenced both within this thesis and in the BOP literature (Arnold & Quelch, 1998; Quelch & Bloom, 1996; Sachs, 1998), when applied in emerging economies and especially in BOPs, the many weaknesses of the strategy come to light. In particular it makes too many assumptions that, although perhaps relevant for developed countries, are inapplicable in developing countries where aspects like infrastructure, institutions, and formal sector efficiencies are not necessarily guaranteed. The major downfalls of the transnational strategy are that it was designed to address local needs at the national level, not the within country differences that require a truly local intimacy; it seeks to maintain central control to ensure product standardization and integrity in a way that often prohibits the local inputs so desperately needed; and it seeks to overcome limitations in EMs while waiting for the markets to evolve into those more familiar to those in the developed world. As a result, firm initiatives using this type of strategy often do not fare well in the long term.

However, the basic concept behind the transnational strategy--creating standardized products capable of achieving high volume (to help keep costs down and profits up) while also incorporating local intimacy aspects (to ensure products are appropriate to consumer tastes and local capabilities), is a step in the right direction for creating BOP appropriate strategies. For example, because BOP products must be both affordable and highly
functional, achieving scale is crucial for firms. To accomplish this, products must demonstrate a functional level of standardization. Further, because local needs and capabilities vary from region to region within the country and even, at times, from community to community, and overcoming consumer skepticism and developing trust is a prerequisite to success, products and models must also be capable of addressing a variety of local demands and conditions. In light of the findings of this thesis alongside those found by BOP researchers in the review of literature, it is the recommendation of this thesis that firms find their standardization aspects (a) in the need or gap their product addresses—for instance, products designed to address basic needs common to BOP’s worldwide such as for housing, quality drinking water, insurance, financing; and (b) in the product and or business model itself, by implementing a platform approach, similar to those designed by the firms in this thesis, that is designed to be used with an inclusive strategy that is capable of incorporating the poor to co-create, capacity build, develop markets, and allowing the firm to become more socially embedded.

As research and firm experiences in the BOP are still relatively new, it remains unclear as to whether there are advantages to using top-down inclusive models, like the Seguros Argos’ mutual model or the microfranchise model mentioned by Magleby and Pratt (2007), over bottom-up inclusive approaches such as those demonstrated by TWI and Échale. However, it does seem clear that, either way, the closer upper management and the company itself is to the BOP markets they serve, the more likely the firm is to gain valuable insights and relationships, act appropriately, and develop trust. Given the overall lack information regarding these strategies, this particular aspect of inclusive approaches could greatly benefit from further research and experimentation. In the meantime, the following are some helpful hints gathered from this research effort.

First, create products and business strategies with a deep understanding of BOP lives, needs, environments, and capabilities, so that they are capable of offering appropriate solutions with high functionality and affordable price tags. Second, know where the product fits and who the target markets are so the firm can quickly and easily identify them and get down to business. Understand that poverty is experienced differently by different households throughout Mexico and though income is one aspect of poverty, there are many other factors that influence the capabilities and limitations of people and play a role in people’s ability to
participate in a firm’s offerings. For example, Échale’s target consumers are defined not only in terms of income groups but also by their ability to show land ownership. Further, to be eligible for the subsidy, potential consumers have to confirm that they have never received a housing subsidy from the government. Additionally, be aware that products designed to address a particular need may not fit everywhere issues determining needs often vary from place to place. For instance, as noted Harris (2005), in Mexico, although there is a widespread need for quality drinking water, the actual water contaminants differ from region to region thus POU firms with products designed to address contaminants a and b in water would not be appropriate solutions in regions with water contaminants c and d.

Thus it is important for firms to know the specifics regarding what their product is capable of and what set of criteria must exist (in the environment and/or in consumers) for product and target market to be the right fit. While some firms may choose to create the product and then try to find a target market that suites it, an alternative, and arguably more advantageous, approach would be to obtain a solid understanding of the diversity of needs represented by BOP markets and design a product capable of adapting to a variety of needs, such as the approach taken by TWI. Finally, firms should be aware that they may experience financial challenges that limit their ability to scale into certain locations at the BOP. Thus they should equip themselves with an understanding of their alternatives (in regards to rural, urban, and semi-urban spaces), and plan appropriately.

Third, go into BOP communities and do industry relevant, on-the-ground research directly, both to further the firm’s informational base as well to create a better understanding of BOP consumers and environments for the firm’s employees. Although research from organizations like INEGI and other national and international organizations can be helpful, because of the aforementioned inherent limitations of measurement, such data should be used only as a starting point to build from with more specific on-the-ground obtained insights. Additionally, this process of going directly into BOPs can be utilized as an opportunity to form relationships with the community, and their governments, identify potential partners, and leverage any available government assistance. According to TWI (2010) government grants are beneficial not only because they help the firm financially but also because they demonstrate local support for the firm. In the same way, the availability of local and
international NGO and development grant assistance should be identified and pursued during this period.

Fourth, when relevant and appropriate, develop platform solutions with products and/or business models, as previously discussed, that are simple and standard enough to replicate easily from place to place and flexible enough to address and incorporate local needs, demands and ways of doing things. Fifth, be aware of existing networks and the opportunities and limitations they represent. When possible work with existing networks but with an awareness of disadvantages that can result from an over-reliance on partners and the potential advantages possible from establishing new networks and relationships directly.

Sixth, learn to see BOP communities in terms of what is instead of what is missing. For example, instead of assuming the BOP is not connected because their access to the internet, television, and streamlined institutional efficiencies is limited, understand that they compensate for such luxuries through well developed social networks, codes of conduct, and word-of-mouth passing of information among buyers, sellers and buyers and sellers (Viswanathan et al., 2008). Firms must learn to recognize the true resources within BOP communities, be it the social networks and influential, entrepreneurial women, or the small businesses that know the BOP consumers and their needs intimately and just need a little capacity building to become beneficial firm partners.

Sixth, develop an awareness of the target market’s consumer sophistication, capabilities, and limitations and design a strategy that incorporates, as needed, capacity building efforts such as education, training, and ongoing support. Beware of broad, arm’s length approaches to educating consumers on the firms’ products or processes, especially when consumer sophistication and trust levels are low. More effective approaches tend to involve face-to-face approaches using presentations, demonstrations, and hands on instructional approaches coupled with ongoing support and supervision to facilitate the learning process, develop trust and allow consumers to increase their levels of comfort regarding the subject matter. Further, understand that in most circumstances, firms will need to create a capacity to consume and though finding ways to provide credit and to keep prices low are useful approaches, creating opportunities to help consumers increase their incomes provide much more sustainable and long-term market development solutions—a win-win situation for all involved.
Finally, be aware that BOP profits are usually about low margins and high volume and that achieving high volume quickly may require significant financial resources on the front end. Though the case studies in this thesis demonstrate that it is possible for a firm to still be profitable and sustainable moving at a slower pace, ultimately the higher the volume, the greater the social and financial gains will be. Overall, BOP ventures and investments will usually require the patience and expectations of a medium- to long-term strategy.

BOP ventures whose social and financial goals are properly aligned offer unique opportunities to investors to use their money to “do well by doing good” by helping the firms they invest in create both social returns in the form of poverty alleviation and economic development, and financial returns. However, because BOP ventures are still largely in their experimental phases for many firms and not yet fully understood by the investing community, the concept of investing in BOP initiatives for dual returns is still in its infancy stages. Future research, development, and promotion of this type of investing would then stand to benefit firms in need of significant start-up capital for product development, R&D, initial market entry, and scaling up to the volume that allows significant returns on investment.

Further, if future research develops measurable standards for firms in terms of their social and financial performance, it could not only contribute to better insights on how firms create positive spillovers, but could also provide investors concerned with the social performance of firms with benchmarks and transparency to better inform their investment decisions while simultaneously giving firms more appropriately aligned initiatives to keeping the social performance of their business models in step with the financial goals. As noted by Preston et al. (2007), “accessing and serving Majority markets constitutes an extraordinarily challenging test for companies’ management quality, creativity and adaptability. Companies that can meet those challenges more effectively than their competitors are quite likely to be better managed, more forward-looking companies in general; and therefore financial out-performers as well, at least in the medium term” (p.3). One initiative in this direction is the Opportunities for the Majority Index created on behalf of the IDB (see Preston et al., 2007, p. 8).

When considering doing business in BOPs, firms need to be realistic in regards to whether or not its particular industry or firm will be a good fit in environments described as
having considerable amounts of “psychic distance” and high social sensitivities that may require firms to completely rethink the way they do business. For instance, it will be important for firms to be introspective to determine where they are now in regards to their resources and capabilities, company mindsets, openness to change, levels of cultural diversity among employees, familiarity with and sensitivity to other cultures and BOP scenarios, levels of comfort with risk taking, and abilities to commit to a long-term initiative that requires a different set of goals and expectations than what the firm may be used to. Further, firms will need to be willing to approach BOPs open-mindedly and with humility, with the understanding that they represent new markets that are very different from the more familiar TOP ones and for which they may not have all the answers. Thus, rather than trying to impose tried and tested developed market strategies, firms will need to be willing to realize there may be a lot of learning to be done and new approaches will most likely be necessary.

In addition to the above factors, an existing firm will need to take into consideration whether its size, goals, and current momentum can successfully manage a split in corporate focus to enable both the pursuit of new BOP opportunities and the maintenance of its existing position in developed markets. Though MNCs are well positioned to pursue BOPs in terms of financial capital and overall business expertise, their sheer size and deeply embedded corporate mindsets may make shifting gears, and adjusting models and corporate logic extremely difficult. In this way, new ventures, designed from the beginning to capture BOP markets, may have the advantage in strategy. However, in line with Di Norcia (1991) who stated that “the idea of a single model of international business, however flexible and balanced, may itself be outdated in an era of such rapid, unpredictable, and diverse social change” (p.228), the BOP may very well represent a space where a variety of strategies are applicable and where firms committed and created enough to think outside the box may find new opportunities, both in markets and in market approaches.
REFERENCES


