EVALUATING THE IMPACT OF BOTTOM OF THE PYRAMID BUSINESSES

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PRESENTED AT:

The International Conference of the Greening of Industry Network
Waterloo, Ontario
June 2007
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The well being of the poor has traditionally been the concern of governments, international institutions, and non-government organizations (NGOs). C. K. Prahalad and Stuart Hart helped reframe this conception for many business practitioners and scholars in a seminal article called “The Fortune at the Bottom of the Pyramid” (Hart and Prahalad, 2001). The bottom of the pyramid (BOP) concept suggests that business has a vital role to play in meeting the unmet needs of the 4 billion poorest people on the planet. The ensuing discussion has produced a rich and growing set of cases, a modest amount of theory building (Prahalad, 2004, Hart, 2005) and considerable controversy.

The UN Year of Microcredit (UN, 2005) and the recent awarding of the Nobel Peace Prize to Mohammed Yunis for his pioneering work in microcredit have dramatically increased public awareness of financial dimensions of BOP business. The number and magnitude of success stories in the world of microfinance (Robinson, 2001), along with the gap between successes to date and the huge unmet needs (Ledgerwood and White, 2006) has focused considerable attention on the potential problems and opportunities inherent in BOP business.

Consideration of the issues raised by BOP business has produced considerable disagreement concerning the motives and the capabilities of business to address unmet needs of the poor. For some, efforts by MNCs and small businesses signify a remarkable new approach to addressing the unmet needs of the poor. To others, the efforts of MNCs to sell products in the developing world constitute an unconscionable attempt to exploit the poor by turning them into consumers, without any genuine concern for their real needs. The focus on the role of MNCs in
bottom of the pyramid business has diverted attention from the need to evaluate the effects of all types of BOP business.

Business at the bottom of the pyramid includes microenterprises, small and medium enterprises (SMEs), and increasingly, multinational corporations (MNCs). It is often useful to distinguish between different scales of business for evaluation purposes. Microenterprises, sometimes poetically labeled “barefoot capitalism” (Klobuchar, 2005) are enterprises employing one or a few people, typically with very low income. Small and medium-sized enterprises (SMEs) range in size from a few to a few thousand employees, but remain predominantly local or regional in scope. Multi-national corporations (MNCs) by definition are larger, international businesses engaged in commerce outside their home countries. MNCs have received the bulk of scholarly attention and research to date in the discussions of BOP business (see for example Prahalad, 2004, Hart, 2005). However, any theory of bottom of the pyramid business that does not include the full spectrum of businesses must necessarily be incomplete. Accordingly, this paper will discuss approaches to evaluation that are equally applicable to businesses at all three scales.

Recent scholarly discussions have identified significant issues concerning the effects of BOP opportunities (Paton and Halme, 2007). These include questions such as:

- How do we define responsible BOP-business?
- Under what conditions will a BOP-business be responsible?
- What are the key elements of success in addressing the needs of the poor?
- What foreseen and unforeseen positive and negative outcomes could BOP business have?
- What are the environmental implications of BOP business?
- Does MNC involvement in BOP business undermine local business?
The research community focused on BOP business is beginning to progress beyond anecdotes and cases to systematic assessment and practical advice. The most notable research success to date has been the pioneering work of Prahalad (2004), Hart (2005) and others to document and evaluate the business models of successful BOP businesses, and the scholarly assessment of microfinance by Robinson (2001), Daley-Harris (2002), Cohen, (2002), Ledgerwood and White(2006) and others.

But a gap exists between the research on bottom of the pyramid businesses and the more established research on microfinance. Microfinance research has included a wide range of evaluation and measurement on issues including efficiency and effectiveness. Research on newer aspects of bottom of the pyramid business has, understandably, focused on case studies, and analysis of business models, scalability, and related issues. Serious advances in research on bottom of the pyramid business will require effective evaluation of the social impacts these businesses are having on the people they are supposed to benefit.

Evaluation will allow us to identify conditions in which specific business interventions can address unmet needs fairly and effectively. Evaluation can provide valuable information about a wide range of questions such as effectiveness in meeting the targeted needs, economic efficiency, effect on competition and technological innovation, and distributional effects. This paper focuses on evaluation to assess the effectiveness of bottom of the pyramid businesses in addressing the social problems they are targeting.

Fortunately, there are several approaches to evaluation that have been developed in other contexts that can be brought to the analysis of BOP business. This paper explores the potential insights from applying theory-driven evaluation (Chen, 1989, 1990). This approach has emerged as a valuable stream of research methodologies from assessments of public policies and
educational programs. Theory-driven evaluation offers significant promise as a framework for assessing the social effects of BOP businesses.

This paper makes a modest start at incorporating relevant theory into the theory-driven evaluation of BOP business. A wide variety of useful frameworks has emerged in recent research on the causes of and solutions to poverty. These frameworks overlap considerably in the issues they address but each emphasizes a different aspect of the life of the poor. They differ in the emphasis they place on the function of products and services in meeting unmet needs. Together, they have the potential to provide very complementary insights into the social effects of BOP business.

This paper uses the financial life cycle to illustrate the potential usefulness of theory-driven evaluation in assessing the social impact of bottom of the pyramid business (Cohen, 2002, Wilson, 2002). This framework focuses on helping families and individuals gain economic self-sufficiency. This framework is taken from a much broader range of theories emerging within the communities of development practice and research. Many other useful frameworks are beyond the scope of this paper, but could be incorporated usefully into theory-driven evaluation of BOP business.

The next section describes the key concepts of theory-driven evaluation. The following section describes the financial life cycle framework and provides an illustration of how the framework might be used in a theory driven evaluation of BOP businesses.

THEORY-DRIVEN EVALUATION

Theory-driven evaluation (Chen, 1989, 1990) offers an approach to assessing the successes and limitations of BOP businesses by exploring why a venture does or does not
achieve its social objectives. Theory-driven evaluation allows researchers to consider the perspectives of stakeholders as well as insights from frameworks established in social science research. A theory-driven evaluation seeks to articulate what a particular business or program is trying to achieve, then evaluates what the program is or isn’t doing to achieve its goals successfully.

“Program theory” is a central element in theory-driven evaluation. A program theory is a "plausible and sensible model of how a program is supposed to work" (Bickman, 1987). It describes a chain of "causal assumptions linking program resources, activities, intermediate outcomes, and ultimate goals."

Chen (1990) divides program theories into two broad types -- normative theory and causative theory. Normative theory focuses on the goals or methods and the outcomes that should be pursued in order to achieve the desired social objectives. Causative theory explores the causal links between the intervention being evaluated and the outcomes. BOP business could benefit from both normative and causative evaluations. However, this paper focuses on causative analysis, and leaves normative analysis for future studies. This paper focuses primarily on the evaluating the causal links or mechanisms by which BOP businesses achieve (or fail to achieve) their social objectives.

Program theories are seldom articulated explicitly for business ventures. Clearer specification of the program theory could significantly improve the evaluation of current ventures and the design of future ones. Articulating a program theory explicitly can help identify the weak links in the chain of events that must occur for a venture to achieve its desired effects.

Theory driven evaluation distinguishes between two distinct elements that determine the success or failure of a venture. Figure 1 illustrates these two elements. The “action theory”
describes the link between the intervention and the immediate change in behavior of the target participants. For example, the action theory for a microcredit program would focus on how to provide loans so that participants can start microenterprises. Evaluation of the “action theory” would focus on whether the microcredit program actually delivered the funds to the target population and whether those loans were sufficient to allow participants to create microenterprises. The “conceptual theory” describes the link between the change in target participant behavior and the desired outcome. For example, the conceptual theory for a microcredit program can be evaluated to determine whether the participants who actually started businesses were able to succeed in their businesses and whether they have been able to emerge from poverty as a result.

Figure 1 about here

The key insight to be gained from using this framework is to realize that both the action theory and the conceptual theory must be effective for an intervention to achieve its intended objectives. If either link is ineffective, the BOP business may fail to achieve its intended social effects. If either link is functional, but sub-optimal, the program can be marginally successful but may be considerably less effective than it could be if both were finely tuned. Effective evaluation will require independent assessment of the separate links to assess their effectiveness.

Like any other approach to evaluation, theory-driven evaluation has limitations. Baker (2000) observes that identifying the theories underlying a particular business may be “inherently complex”. As a result, theory statements may be missing or not stated clearly for effective
testing, measuring each step in the chain of intended results may be difficult, and results may be
difficult to generalize from one BOP business to another.

Despite these shortcomings, theory-driven evaluation can be valuable because it forces
practitioners and evaluators to be as explicit as possible about the chain of events that the BOP
business is intended to set in motion. Applying theory-driven evaluation will not provide a
definitive assessment of BOP problems and opportunities. But it can provide practical advice for
practitioners, by grounding the discussion in more tangible information on why ventures do or do
not succeed in providing the desired social benefits.

THEORY-DRIVEN EVALUATION IN A FINANCIAL LIFE CYCLE FRAMEWORK

The financial life cycle framework focuses on the effectiveness of a BOP business in
addressing the full range of financial needs that the poor experience. This perspective emerged
from research and evaluation concerning microfinance institutions (Wilson, 2002). The financial
life cycle approach focuses on matching the products and services offered by businesses
(whether large or small) to the actual needs of clients. Despite their positive contributions, many
BOP businesses fall short of reaching their potential to enhance the financial well-being of their
clients. Theory-driven evaluation can identify shortcomings and help businesses identify
opportunities to modify their product and service offerings as well as their business models to
meet clients’ real needs.

This approach acknowledges that many financial services for the poor are focused
narrowly on providing the means to start and run microenterprises and may not address other
financial needs necessary for a person to emerge from poverty (Cohen, 2002). While
microenterprises have been a significant force in raising clients from out of poverty,
microfinance has not met many of the financial needs of the poor, (Wilson, 2002). Other life events, such as marriage, the birth of a child, education, a daughter’s wedding, death of a spouse, and old age are financial events that may greatly outweigh the effects that management of a microenterprise may have on a poor person’s life. In addition, less-predictable events such as floods, crop damage and losses to crime can impose financial constraints that microcredit clients must adjust to.

The life of the poor is largely defined by risk (Sebstad and Cohen, 2000). Many of the poor in countries such as Bangladesh live in areas exposed to flooding or other climate-related catastrophes that can put their life, health, and financial well-being at risk. Until the relatively recent emergence of micro-insurance, the poor have largely relied on informal structures such as extended family to mitigate risks. (Brown and Churchill, 1999) However, given the physical proximity of extended family members in many instances, single catastrophic events such as floods can overwhelm the ability of these informal systems to manage the relevant risks effectively.

The experience of AIG Uganda in the microinsurance business illustrates the value-added of incorporating the financial life cycle framework (McCord et al, 2005) into a theory-driven evaluation. In 1996, FINCA Uganda, a microfinance organization, convinced AIG Uganda, the local affiliate of American International Group, to begin offering insurance to help clients survive the financial shocks associated with the death of a family member. AIG Uganda was the only licensed insurer willing to provide coverage for the microfinance institutions’ clients. AIG Uganda was unable to offer life insurance benefits because of licensing restrictions. However, they were able to offer accident insurance, including accidental death benefits. By 2004, AIG Uganda had grown to cover 1.6 million individuals and generated an estimated $800,000 in
annual premiums from FINCA's and other microfinance organizations' clients in Uganda, Tanzania, and Malawi. The insurance business now involves over 70,000 transactions per month.

Most of the microfinance institutions partnering with AIG Uganda are village banks working with groups of 20-25 low income clients. Loan officers in the microfinance institutions are responsible for processing insurance claims. Because loan officers serve loan case loads of up to 400 clients each, insurance products have received limited attention.

The program theory for AIG Uganda’s microinsurance business is not stated explicitly, but can be inferred from the CGAP case study (McCord et al, 2005). The action theory focuses on providing insurance products for the poor and encouraging them to participate. The conceptual theory focuses on the use of insurance to help clients avoid catastrophic losses in the event of illness or death of a family member. Both the action theory and the conceptual theory must be effective for the microinsurance to achieve its objectives. In practice, both theories demonstrate significant flaws that significantly limit the effectiveness of the program.

The action theory focuses on enrollment of village bank members in effective insurance programs. By 2004, all but one of the microfinance organizations required loan recipients to purchase microinsurance to cover loan repayment in case of the recipient’s death. This assured that participation rates were very high. However, cultural barriers and confusion about coverage have limited the effectiveness of the insurance for several reasons. First, loan officers received little training on the insurance products and therefore were ineffective in answering clients’ questions about what risks the insurance policies addressed. A bigger barrier concerned the
designation of beneficiaries. Reviews of policy documents showed that women were likely to designate minor children or non-spouse relatives because the instructions given to them specified that the beneficiary should be “someone they trust”. Many chose not to trust their husbands to spend insurance payouts on family. Payout to a minor child can cause major legal problems because of inadequate laws to protect their interests. Finally, payout to recipients takes an average of three months to process. As a result, beneficiaries must depend for long periods of time on the financial resources of their group until the payout is received.

The conceptual theory focuses on enabling enrolled members to avoid catastrophic loses. The insurance offered appears to be effective at protecting families from two types of catastrophic loss. First, in the event of an insured family member’s accidental death, the insurance covers repayment of the microcredit loan. Second, the insurance will cover business losses from fires that cover areas wider than the individual business. The insurance is not effective at covering the financially catastrophic loss in earning power that often follows from the loss of a working age family member.

The result is a profitable product for the insurance companies that is only marginally effective for clients. Because of licensing rules, AIG has been unable to provide true life insurance, even though that is the most important insurance need. As a result, AIG Uganda’s microinsurance business is considerably less effective than it could be in achieving the social objectives it is intended to accomplish.

The theory-driven evaluation approach helps to identify limitations in both the action theory and the conceptual theory underlying the business. The action theory could be implemented more effectively if microfinance loan officers received more effective training and stronger incentives to ensure that clients understand the benefits, and can have their claims
processed more quickly. The conceptual theory could be realized more effectively if the
insurance products offered addressed the need for life insurance in addition to the loan
repayment insurance offered. The substantial success of AIG Uganda’s initial efforts provide a
strong incentive for AIG or another insurer to resolve the licensing issues in order to provide a
life insurance product that meets the real needs of the poor.

CONCLUSION

Both scholars and practitioners have identified the need for improvements in the
evaluation of BOP businesses. Cheston and Reed (1999) point out that evaluations of
microcredit, for example, have focused on measuring “the profitability of the lending institution
and the quality of its portfolio. They don’t tell us whether our clients become less poor due to
the services we provide”. The same criticisms seem to apply to other aspects of bottom of the
pyramid business.

The financial lifecycle framework described in this paper provides a glimpse into the
great complexity of addressing the unmet needs of the poor and helping them escape from
poverty. In evaluating BOP businesses we must avoid the temptations to be either too
demanding or not demanding enough. We must avoid demanding that a BOP business address
all of the necessary requirements to lead their customers from poverty. At the same time, we
must avoid uncritical acceptance of small successes without understanding the role that BOP
products and services play in the lives of the poor.

Theory-driven evaluation can provide a useful compromise between these extremes. We
should not expect every BOP business to articulate their contributions in terms of all three
possible theoretical frameworks. Neither should we limit our theoretical examination to the
single framework described in this paper. However, we can reasonably expect each BOP
business to articulate its theory about its role in enhancing the life of the poor in terms of some reasonable framework concerning poverty alleviation. Clear exposition of explicit action theories and conceptual theories can help identify the gaps between intended social benefits from BOP business and benefits actually accomplished. By forcing BOP businesses to make explicit their assumptions about the social benefits they will provide, theory-driven evaluation can identify opportunities for increasing effectiveness or extending the reach of BOP businesses.

REFERENCES


Paton, B, and Halme, M. “Reframing the BOP Debate” (forthcoming in Business Strategy and Environment).


Figure 1: Program Theory Framework

After Chen (1990)
Figure 2: (Implicit) Program Theory for AIG Uganda’s Microinsurance Program

Provide Microinsurance Policies → Eliminate Loan Default Risk → Eliminate Client Financial

Action Theory: Insurance will eliminate loan default risk in case of borrower’s death
Conceptual Theory: (Implicit) Eliminating loan default risk will help survivors avoid financial catastrophe

After Chen (1990)