Open Symposium II: Working with SMEs and the Corporate Sector in Social Entrepreneurship

Open Symposium II sought to explore the potentials and challenges of working with small and medium enterprises and the corporate sector in advancing social entrepreneurship in Asia. Guests were from management schools doing research in social entrepreneurship from Barcelona and Copenhagen and a practitioner from India who will be joining us via a video link. Prof. Bala Ramasamy of the China-Europe International Business School (CEIBS) in Shanghai chaired the symposium.

Profitable Business Models and Market Creation in the Context of Deep Poverty: A Strategic View by Dr. Johanna Mair[1]

Framing the entry into underdeveloped countries as a business opportunity is conceptually appealing. While previous work on strategies to pursue the bottom level of the global income pyramid has shifted paradigms about poverty, the focus in this paper is to move from the "whether to do it question" to contribute to a better understanding of "how to do it" from the perspective of corporate and competitive strategy. Using three cases, two from Bangladesh and one from India, insights are generated into how business models can be structured and executed to generate the necessary profits for companies to justify investments into market entry and market building, while at the same time integrating and serving the poorest and their unique needs as well. Focus is given on how to recognize, access, and configure resources that local pioneers have already built in extremely poor countries. The aim of this paper is not to develop prescriptions but to generate ideas about the opportunities available to companies working in tandem with local entrepreneurial organizations to build business models that are able to achieve multiple strategic objectives concomitantly.

In the context of deep poverty, companies face a triple dilemma – First, there may be no market to enter and that there could be a need to actually build the market; second doing it alone might not be feasible given current company resources and capabilities; and third, the absence of markets means the lack of local companies needed to provide the locally relevant resources and capabilities.

The main arguments why companies should care about underdeveloped markets are well established. It is estimated that there will be 2.2 billion more people in the next 40 years, majority of which will be poor. This is a vast market if one is to view the poor as customers rather than mere recipients of donations. In the face of hyper-competition and lack of growth in the mature markets of highly developed countries, the absence of markets for many goods and even whole industries in underdeveloped countries might be the ultimate opportunity for creating market space.

Companies face the question of how to create and occupy new market space in the context of deep poverty. A complex set of factors might explain the lack of corporate action in the context of mass poverty. Resources and capabilities that companies have may be of low or uncertain value in the context of poor countries.

Social entrepreneurs in poor countries have the capability to operate at the base of the economic pyramid. These entrepreneurs have developed resources and capabilities to achieve a blend of social and economic objectives. Their skills and approaches are very relevant to the local context and are potentially of strategic importance for companies that consider building a presence in an underdeveloped country. Accessing these resources and capabilities could form an important base for companies to build up business models that reach a suitable scale and generate the necessary profit levels that can justify investments. The following three cases illustrate this.

During the 1990s, Grameen Bank and Norwegian telecommunications company Telenor went into a partnership for a telecommunications business in Bangladesh. Known for its overpopulation, extreme poverty, political instability, and corruption, Bangladesh nevertheless became Telenor's most profitable growth market.

The joint venture led to the formation of two organizations: GrameenPhone which aimed at building a purely commercial model, and GrameenTelecom which endeavored to cater to the poorest by teaching them to use phones for entrepreneurial purposes. From starting out in 1997, GrameenPhone became profitable in 2000, passed 2 million subscribers in 2004, and 6 million in 2006. GrameenPhone is now one of the largest private companies and the second largest taxpayer in Bangladesh. GrameenTelecom created more than 100,000 jobs, provided phone services in previously unconnected villages, and facilitated savings on costly administrative trips to the capital Dhaka. GrameenTelecom is also profitable and accounts for more than 10% of the revenues of GrameenPhone.

The Grameen-Telenor joint venture exemplifies a *symbiotic model* of market creation in a deep poverty context. Symbiosis was achieved with the effective interplay of Telenor's technology and capital with that of Grameen's reputation, credibility, and special skills in accessing, communicating, and working with the rural poor in more than 50,000 villages throughout Bangladesh. Symbiosis was also in play in the economic-social operations tandem of GrameenPhone and GrameenTelecom, ensuring both financial and social bottom-lines.

The Map Agro and Waste Concern partnership demonstrates a *complementary model* of market creation. It shows how the resources of companies and social entrepreneurs can come together to enable a different type of value chain that creates a new and very profitable market for the company partner.

In the mid 1990s, Dhaka City in Bangladesh faced a waste management crisis. Despite investments, initiatives, and earlier efforts, the Dhaka City Council could only deal with 40% of waste created. As a result, waste piled up in the streets and in landfill sites, causing disease, insufferable odor, leakage of pollutants into water resources, and exposing women and children "waste-pickers" to hazardous substances.

In 1997, two entrepreneurs launched Waste Concern, with the simple idea of turning waste into compost fertilizer and selling it as a substitute to chemical fertilizers. Waste Concern integrated community based house-to-house collection, composting, and marketing. Initially, products were sold only to gardeners and small organic farmers. However, a measurable elimination of the waste-problem required access to much larger markets in order to create a pull for building supply-side scale and cost efficiency.

Despite initial setbacks in striking a partnership with Map Agro, the largest fertilizer company in the country, Waste Concern prevailed to have the company go on a "trial contract" that guaranteed annual sales of 200 tons of compost. When positive feedback and impact from farmers increased, Agro Map invested in a purpose built enrichment factory and started selling enhanced compost on a larger scale, currently at 50,000 tons per year. The financials for Map Agro are attractive. It buys compost at 2,500 Taka per ton and sells pure compost at 6,000 Taka per ton, and enriched compost at 12,000 Taka per ton.

The new value chain created a number of new jobs, lowered exposure of poor communities to health threats, and helped the government to deal with a seemingly insurmountable social problem. The partnership also enabled Waste Concern to obtain funding, technical expertise, and support from international organizations.

In India, two non-profit organizations, Aurolab and Aravind Eye Hospital teamed up to provide eye surgery to poor people while maintaining a viable enterprise. David Green, the founder of Aurolab, built a state-of-the art intra-ocular lens production facility next door to Aravind and integrated it with the patient care model of the hospital. Today, the group of Aravind Eye Hospitals screens over one million patients a year and performs several hundred thousand eye surgeries. Aurolab is already among the largest suppliers of lenses in the global market with a share of more than 10%.

The overall strategy that both entities employ is "maximizing the numbers of people served". In the model, the poorest patients pay nothing (they comprise 50% of surgeries), 35% pay well above cost (more affluent customers), and the overall business model generates a net profit margin of 60%.

The Aurolab-Aravind experience exemplifies an *integrative model* of market creation in a deep poverty context. The activities and objectives in this strategy are mutually reinforcing to create a consistent business model. Free surgery helped achieve scale very quickly and also accessed community partners. The diversity of interesting patient cases made the enterprise an ideal training center, attracting top doctors from all over the world at very low costs. Scale also enabled both Aurolab and the doctors to drive down the learning curve fast. These have had positive effects on both the cost and quality dimensions of the business model.

In all three cases, distinct and operationally separate organizational structures have cooperated to form an overall business model. The Telenor-Grameen partnership (symbiotic model) is a business model that is built on separate organizational structures with different strategic objectives and different target customers, yet together they build an overall model for social and economic development.

In the case of Waster Concern and Map Agro, both partners enable a different part of the value chain but together create a new business model that satisfies expectations for both social and economic returns (complementary model). With highly complementary objectives, the organizations could construe a new value chain that neither of them could have pursued alone.

The collaboration between Aurolab and Aravind demonstrates how creating a radically different quality to price ratio coupled with a consistent business model around clear strategic objectives allows for serving underdeveloped markets effectively and profitably. The joint venture between the two entities (integrated model) allowed for the effective interplay of a manufacturing plant and a health service provider. Very different cultures and management systems are necessary to drive the unique operational objectives of each entity, yet with shared strategic objectives, the venture was able to serve more people and even earn along the process.

There is a need to study many more examples of collaborative efforts to learn how they can be best managed from a corporate strategy perspective. It remains to be seen to what extent the cases described here are just unique observations or whether these types of collaborations could become a model for companies to build large-scale market presence that is positively driven by but also drives socio-economic development in today's poor countries.

Advantages and Challenges of Working with the Corporate Sector by Dr. Kai Hockerts[2]

Corporate sector participation in social entrepreneurship has been a rapidly growing. To name a few examples – World Food Program and TNT for providing logistic support to humanitarian aid, VSO and Randstadt for borrowing skills from flex work industry for overseas volunteering, Accion and ABN Amro Banco Real for micro-finance in Brazil, and Telenor and Grameen Bank for mobile phone operations.

There are a number of reasons why the corporate sector would want to cooperate with social enterprises. It is important for social enterprises to be aware of the reasons why firms engage in cooperation. In being aware of the motivations of the corporate sector, social enterprises can tailor-fit their involvement with firms in order to create more sustainable relationships.

Firms cooperate with social enterprises to reduce risk. In working with socially relevant initiatives, firms can avoid consumer boycott, maintain their license to operate, and avoid unfavorable legislation. It is perceived that these contribute to risk reduction.

Attaining efficiency is another major reason why firms cooperate with social enterprises. Efficiency is achieved by receiving free advertising, motivating or inspiring the staff, and getting lower cost of capital from ethical investors.

By being identified with socially relevant activities, firms can also go into premium pricing, maintain customer loyalty, and gain new clients. These lead to improved margins and sales. Subsequently, firms get to develop new markets by building its skills for innovation and developing the bottom of the pyramid market.

While the corporate sector gains from engaging in socially relevant initiatives, it also offers a number of advantages for social enterprises. At the outset, it provides social enterprises an opportunity for financial and legal risk sharing, and immediately provides business core competencies and research capabilities.

In partnering with corporations, social enterprises gain more credibility and visibility to other businesses, government agencies, and the public in general. Social enterprises also gain cheaper access to financial, human, communication, and distribution resources.

Notwithstanding the advantages that corporations and social enterprises gain from each other, there are also risks associated with their partnership. The desire for efficiency may exclude marginal beneficiaries since businesses may be tempted to focus on the most profitable beneficiaries and exclude loss-makers. Corporations may also leave a partnership when the business encounters heavy losses, the top management changes or loses interest, or the management in general moves its focus towards core business.

In building partnerships with corporations, social enterprises run the risk of losing its reputation among its other partners. It also has to contend with ownership issues i.e. who should own the social enterprise – the beneficiaries or the company – to which corporate partners are particular about especially in cases of successful enterprises.

Working with SMEs and the Subsector Approach
by Mr. Vijay Mahajan[3]

Eradicating poverty is one of the key challenges of our time. It is even expressed as the number objective in the Millennium Development Goals. Poverty alleviation has been traditionally done by the government and NGOs such as BRAC, Grameen, and Ashoka; however, the private sector has been increasingly getting engaged in this task as well. This is partly due to the expression of the private sector of corporate social responsibility and also due to the objective of business to expand to markets towards the "bottom of the pyramid". Thus, the role SMEs in social entrepreneurship is emerging more strongly as a result of the above-stated trends.

There is a need to go beyond the concept of poverty alleviation and to move towards livelihood promotion. Poverty alleviation only focus on increasing household income to go above the poverty line as a one-time exercise and does not adequately recognize the role of the poor. Further, poverty alleviation programs require heavy government intervention and subsidy. As a result, households are still left vulnerable to risks and shocks. On the other hand, livelihood promotion focuses on building the assets and capabilities of poor households as a long term solution. It recognizes that a vast majority of the poor are economically active and that market-based entrepreneurial solutions are important.

There are various approaches to livelihood promotion, and the four major ones are the following: micro-credit based, sub-sector based, rights-based, and integrated approaches.

A micro-credit based approach focuses on the provision of credit or doses of small loans as a response to "the missing input" for livelihood development. The exemplary experiences in this approach are embodied by Grameen Bank, ASA in Bangladesh, SHARE, SKS, and Cashpor in India. This approach have reached millions of poor households, has provided credit with high repayment rates and profitable operations. However, critics claim that a micro-credit approach has inadequate impact on household empowerment, providing some partial poverty alleviation, but not making livelihoods more robust and leaving households still vulnerable. There have been improvements done regarding this approach, in Grameen II savings and insurance services were added and in Cashpor veterinary care and other livelihood promotion services were included.

A sub-sector based approached works on the full value chain of a given commodity or product / service sub-sector e.g. from the farm to the export consumer; with interventions in the entire market chain. Models on this approach are those of NDDB in India and BRAC in Bangladesh. The sub-sector approach has been recognized for its ability to offer poor households not only credit but a package of capacity building support as well such as enterprise training, market linkages, and collective action. On the other hand, this approach has been criticized as focusing too much on commodity issues rather than on the household (milk in the case of NDDB) and as being vulnerable to commodity risks (silk in the case of BRAC. Some improvements on this approach have been done. These included enabling the poor to take more active roles in the sub-sector (poultry, BRAC), building risk mitigation through insurance (livestock, NDDB), and implementing price interventions (oilseeds, NDDB).

A rights-based or empowerment-based approach focuses on organizing the poor to get their fair share in development. Examples of this are the experiences of Manushi in New Delhi, India for its work with street vendors and that of Maya in Bangalore, India for its work with informal sector workers such as construction laborers. A rights-based approach is successful in significant enhancements in incomes due to organizing and assertion of rights. Critiques on this approach include its being vulnerable to risks and changes, inadequacy in breaking out of poverty, and the size of the pie being insufficient and needing of increase or expansion. Enhancements on this approach include the addition of micro-finance services (Manushi) and innovation in market linkages (Maya).

Examples of an integrated approach are that of SEWA India which works with self-employed women and BASIX which works with rural poor in several states of India. In an integrated approach, it has been seen that significant enhancements in incomes and reduction in vulnerability were attained due to the combination of financial services, business development services, and institutional development services. However, some of the major critiques on an integrated approach were its being complex and consequently its being difficult to scale up and replicate, and its high effort and cost requirements. Improvements on the approach include building upon a core approach and adding specialized elements (SEWA trade union plus banking) and building revenue models for each service with eventual synergy (BASIX Livelihood Triad of institutional development services, livelihood financial services, and agriculture and business development services).

The Livelihood Triad is fully market based model, with each of its vertex with its own revenue center (interest on loans, fees for livelihood services). Provision of services requires mutually supportive social entrepreneurs. At the corporate level, BASIX mobilizes financial and human resources while at the village level self-employed livelihood service providers are mobilized to provide services to the rural poor.

For example: in the dairy sub-sector, 40,000 dairy farmers were organized into self-help groups (majority are women) or cooperatives. Interventions included credit provision for livestock purchase and insurance, organizing of input and equipment suppliers, milk transporters, and milk distribution agents. Several of these sectors are SMEs and some are large corporations i.e. credit and insurance providers, processing equipment suppliers or manufacturers.

In the cotton sub-sector, 5,000 small cotton farmers were organized into 20 cooperatives. The different sector players involved were suppliers of seeds and other inputs, cotton transporters, ginning mills for first stage processing, and spinning mills for specific quality processing. All of these sectors are SMEs- variably as manufacturing enterprises and others as service enterprises, some are private while others are cooperatives.

SMEs are necessary for livelihood promotion since most rural poor are engaged in production producing relatively small quantities of crops or livestock / livestock produce. This 'smallness' limits the capacity of the rural poor to process by themselves (which is necessary for value adding) and thus necessitates aggregation and manufacturing or service consolidation. While the importance of SMEs is being emphasized, it is also important to underscore the need to socially orient private business and even cooperatives. This is necessary to prevent high input prices and/or low output prices (on the part of SMEs) which could result to commodity shifting and bad manufacturing (on the part of the producers). A long run equilibrium or 'win-win' situation is needed and to do this, social entrepreneurship will play a critical role.

As a support to SME and sub-sector approach to livelihood promotion, researchers and educational institutions can develop case studies of SMEs in poverty alleviation and livelihood promotion, identify constraints to growth and effectiveness, provide capacity building in response to the constraints, and disseminate lessons to educate the corporate sector and the government about the crucial role of SMEs to livelihood promotion.

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On inculcating ethics to SMEs – (One of the major issues of concerns in partnering with SMEs is that they are one of the highest violators of human rights.)

Mr. Mahajan pointed out that he only talked about a subset in the universal number of SMEs who are focusing on the equality of livelihood promotion, adding that there are criteria for this subset to remain a positive contributor to the process. For example, they should have a progressive social orientation and they should conduct business appropriately (i.e. treat their employees fairly). Hence, he noted that he is not confident that a vast majority of SMEs will qualify for this.

Mr. Mahajan believes that something should be done about the human rights violations of SMEs, but he also think that SEs should burden itself with the additional responsibility of making the SME world fall in line with the triple bottom-line.

On the strategy of Aurolab in reducing costs of medical commodities – Dr. Mair stressed her strong belief that it is a myth that established companies have certain rates that cannot be easily matched because they produce commodities in a sophisticated manner and therefore its cost should be commensurate.

David Green demystified this. First, he worked for an organization that provided intra-ocular lenses to poor eye surgery patients until he decided and convinced his organization that they should produce the commodities themselves. He went to a manufacturing company that previously donated lenses to them. They opened their doors and David Green found out how easily the lenses can be made.

Dr. Mair's message is that social entrepreneurs should think out of the box-demystify the way things are done.

On whether there is a need for social enterprises to work together with corporate players – Dr. Hockerts does not agree that a merger is good for the SEs. He said that this might make sense in some situations but not always. There are many good reasons to gain from these kinds of partnerships but an in-depth analysis of the risks is needed. For one, all corporate groups have their motives when they move into the management structure.

Mr. Mahajan remarked that SEs need to cooperate with the business sector and vice versa. However, it is never a smooth journey and much has to do with the relatively pioneering efforts. Some problems will still rise even if expectations are fully lay down right up front. Mr. Mahajan added that learning is taking place in the fields and both sides are beginning to appreciate the value added/value brought in by each. It was his opinion that more healthy collaborations will be seen in the future, and he himself is looking forward to partnerships with several other good corporations.

Dr. Mair believes that SEs and business sectors should not merge. SEs should be innovative and creative about structuring operations. She cited some of the most exciting SEs she has encountered, such as the Fabio Rosa in Brazil.

[1] **Dr. Johanna Mair** is an Assistant Professor from IESE Business School, the graduate school of management of the University of Navarra, in Barcelona. IESE offers Global Executive MBA and PhD in Management degrees, as well as a wide range of executive education programs for global senior executives. It also offers a MBA course on social entrepreneurship with students involved in SE in various contexts such as Bangladesh and China. She is working with and on social entrepreneurs and currently conducting a research on entrepreneurial strategies to reduce poverty, innovative institutional and organizational solutions. She has a Ph.D. in Management from INSEAD, France and Master in Social and Economic Sciences degree from Wirtschaftsuniversitaet in Vienna, Austria.

[2] **Dr. Kai Hockerts** is currently an Associate Professor at the International Business School, Center for Corporate Values and Responsibility (CVR) in Copenhagen. He was Research Programme Manager at INSEAD's Centre for the Management of Environmental Resources (CMER) in Fontainebleau where he headed a team of six Research Associates. His primary research focus was on corporate sustainability strategy and environmental entrepreneurship, environmental accounting and control as well as in sustainable finance. He teaches an MBA elective on "Environmental Sustainability and Competitive Advantage" and is also involved in executive teaching. He has given numerous talks to academic audiences and practitioners on a broad variety of topics linked to corporate sustainability, environmental management, and social responsibility. Prof. Hockerts holds a Ph.D. in Management from the University St. Gallen and a Diploma in Business Administration from the University of Bayreuth.

[3] **Mr. Vijay Mahajan** is the CEO of Basix. Basix, conceptualized by the speaker in 1995, is a new generation livelihood promotion institution helping support livelihood initiatives of the poor by going beyond micro-credit. Basix has developed many innovative approaches among them the subsector approach which is the subject of his presentation this afternoon. Prior to the establishment of Basix, he established PRADAN or Professional Assistance for Development Action that is highly regarded by the NGO community and government by working with India's poorest people. In 2002, he was selected as one of the 60 "Outstanding Social Entrepreneurs" of the world by the Schwab Foundation. He graduated from the Indian Institute of Technology in Delhi and Indian Institute of Management in Ahmedabad and was a mid-career fellow at the Woodrow Wilson School of Public International Affairs, Princeton University.