

Poor Idea

The New Republic, 7 March 2005 - In 1996, I stumbled across a curious experiment in global capitalism in the jungles of Borneo. On the Malaysian side of the island, in a beautiful river city called Kuching, a U.S. company was building Borneo's second electronics factory. I remember standing uneasily in the mud and muck of a construction site that had been carved out of a rain forest near Kuching's small airport. In the heat of the day, wearing a hard hat, a perspiring executive from Middle America named Bob Snyder began excitedly telling me about his "experiment."

Snyder worried that Kuching, with only about 300,000 people, was too small to supply him with all the workers he would ultimately need. Relying only on city folks, he feared that he would soon exhaust the local labor supply and that wages would rise. His solution was to devise a test: Take a man out of the jungle and turn him into a reliable worker. If he succeeded, Snyder wagered, he would never face a shortage of labor.

Snyder then revealed that he had recently hired such a man, a subsistence tree-cutter and rice planter who hailed from a village a few hours away. The man's name was Donald Jagau. He was 28 years old, a husband, a father, and a member of a Dayak tribe native to Borneo's dense forests. His village lacked electricity and could be reached only by riverboat. With a reasonable command of English and a sharp mind, Jagau was proving a worthy pupil--so worthy that Snyder had sent him to California to train (for nearly a year) in Silicon Valley. Jagau would soon return to Kuching to be among the first workers in Snyder's new factory.

Once back in Kuching, Jagau thrived. Over time, he rose from simply tending a machine to training other new arrivals from the jungle. His salary grew to nearly \$500 per month, which gave him and his family a higher income than 50 percent of Malaysian households. The company sent him to Scotland for further training on the latest machinery. Jagau even had health insurance and enough disposable income to purchase a motorcycle.

Documenting Jagau's transformation from impoverished forest dweller to upwardly mobile high-tech worker became a side project for me. Over the next few years, during trips to Southeast Asia, I visited him several times, writing about him in *The Wall Street Journal*, for which I was a foreign correspondent, and also in a book I wrote about globalization. As I charted Jagau's ascent, I marveled at the "invisible hand" of capitalism. In the pursuit of his selfish interests, an American executive had transformed the material circumstances of Jagau's life. Deep in the jungle, a would-be Colonel Kurtz was disciplined by market forces. Charity was alien to Snyder's mentality, and he could be accused of exploiting Jagau, who, in time, came to resent the relentless monotony of the factory and his absence from the tranquil forests he so enjoyed. Yet Snyder had done more for Jagau than any philanthropist could. Just ask Jagau's brother, Jonathon, who remained an impoverished tree-cutter. Despite his misgivings about being rushed into modern life, Donald Jagau would never choose his brother's life, with its grinding insecurity and deprivation. And it is easy to understand why. The last time I saw Jonathon, he was firing a .22-caliber rifle at the faint outlines of a small animal. Hungry, he hunted not for sport. And that night he missed.

The tale of Donald Jagau would surely warm the heart of C.K. Prahalad, a business consultant and management expert. Born and raised in India, Prahalad, who teaches business at the University of Michigan, is a leading thinker in a movement of wealthy, successful capitalists who now suffer from guilty consciences. About the time Jagau was chopping down a tree and hearing an ad on his portable radio for a job in a high-tech factory, Prahalad was asking himself, "What are we doing about the poorest people around the world?"

Helping the world's poor is not standard fare for business, but Prahalad wants to change that. He wants to bring serious discussions of poverty out of the Ford Foundation and the World Bank and into the corporate boardroom. He offers an immodest proposal: not to alleviate poverty, or reduce it, which is the goal of development experts. Nope. That's too low a bar for Prahalad, who has the over-the-top confidence that comes from selling his ideas to senior management. (He is, according to BusinessWeek Online, "one of Corporate America's top management gurus.") Instead, Prahalad talks unabashedly of "eradicating" poverty, as if the global poor were a neglected market to be reevaluated, readdressed, and, ultimately, conquered with a re-branded product.

How? Sweeping aside decades of experience and a mountain of literature with a few caricatures, Prahalad presents his own, very simple, solution to poverty: Give the poor decent products at affordable prices. In short, treat the poor as consumers. Companies who do, he argues, will find "the fortune at the bottom of the pyramid." The phrase, which is the title of Prahalad's latest book, refers to the world's wealth pyramid. Out of six billion people, one third are relatively wealthy and one third are absolutely poor, living on a \$1 per day or less. Prahalad says these people, plus two billion more who live on between \$1 and \$2 per day, make up the "bottom of the pyramid," or BOP for short.

Prahalad argues that multinational corporations should pursue the poor because they are "a growth opportunity." In treating the poor as a new market, Prahalad contrasts his own BOP approach with that of the older and better-known corporate social-responsibility (CSR) movement. CSR argues that companies have a moral obligation to do good. But, in Prahalad's view, CSR is ultimately about handouts, while BOP is about building profitable businesses that happen to serve the poor. He insists, "If we stop thinking of the poor as victims or as a burden and start recognizing them as resilient and creative entrepreneurs and value-conscious consumers, a whole new world of opportunity will open up." By catering to the poor, Prahalad sees the chance for multinational corporations--ever seeking fresh customers--to build profitable businesses in unlikely places.

If you haven't heard of Prahalad or his ideas, you haven't been hanging out with the folks who attend the World Economic Forum in Davos, Switzerland, or hobnobbing with Bill Gates or Ted Turner, billionaires who are trying to save the world, or at least a bit of it. For multinational corporations that have tried just about every scheme to put a human face on markets, Prahalad's belief that doing well and doing good go hand in hand is a welcome tonic. The New Yorker's James Surowiecki and Fortune's David Kirkpatrick warmly recommend his ideas, and The Economist predicts that Prahalad's book "seems destined to be read not just in boardrooms but also in government offices." Former Secretary of State Madeleine Albright says of Prahalad, "If you are looking for fresh

thinking about emerging markets, your search is ended." Gates praises Prahalad for providing "a blueprint for fighting poverty." Prahalad has the ear of Kofi Annan and served recently on a U.N. Development Program (undp) commission on "the private sector and development." And, in mid-December, Prahalad convened a meeting in San Francisco of his fellow travelers in the BOP movement, including the CEOs of Hewlett-Packard, Visa, and Vodaphone. He was joined by emissaries from such global poverty-fighters as the World Bank, the U.S. Agency for International Development, and the undp. And Prahalad's "eradicating poverty" confab was funded by, among others, Shell, Microsoft, ChevronTexaco, Dupont, the Inter-American Development Bank, and investment bank ABN Amro.

Prahalad's theory that doing well jibes with doing good may seem like pabulum, but its popularity among corporate leaders and luminaries of globalism is worth pondering. In the past, the world's largest corporations have often acted as if profit-seeking and ethics are in conflict. So, in one respect, Prahalad deserves credit for exhorting the biggest businesses to try harder to square moral and financial imperatives and to begin by crafting new strategies and tactics to liberate the poor from what he calls the "poverty penalty." Traditionally, businesses that specialized in the poor also specialized in gouging them, extorting extra-high profits as a "reward" for going through the trouble of dealing with them in the first place. In the United States, we have laws to counteract the practice. In many poor countries, however, gouging the poor is the norm, so even basic goods (bags of rice, matches, a container of cooking oil) are sold at inflated prices. Smartly, Prahalad argues that multinational corporations have abetted this sorry state of affairs by limiting themselves to the pursuit of wealthier customers in poor countries on the theory that consumers with more money to spend are likelier to buy their products. Instead, he says, big business should design products for the poor from scratch so that reasonable profits can be earned even on lower prices.

But why would multinational corporations go to the trouble of, say, catering to the hygiene or communication needs of the poor in Cambodia, if not to burnish their moral images? Profits and growth is Prahalad's answer. Taken collectively, the "purchasing power" of even the poorest segments of poor countries is substantial. There is money to be made from the poor, he argues, and someday, the poor may be richer and they will move upmarket (to more expensive goods and services) with the brands they know.

Prahalad's argument sounds convincing until you realize that providing goods and services to the poor, fairly and effectively, is difficult for private corporations. He insists that "large-scale and widespread entrepreneurship is at the heart of the solution to poverty," yet he offers few examples, and his favorites are presented over and over again: in India, a prosthetic foot manufacturer, an eye clinic, and a single-package shampoo from the Indian arm of Unilever, the global consumer products company. He is high on a Brazilian department store, Casas Bahia, which sells in Rio's favelas mainly to self-employed service workers. He applauds the Mexican cement giant Cemex for helping the poor build homes through careful purchases of cement. He sings the praises of microfinance, invoking the well-worn example of Bangladesh's Grameen Bank and its thousands of spin-offs. He favors new technologies, citing the rapid growth of mobile phones in poor countries, and extols the virtues of telecenters, which, in many parts of

the world, have given the poor cutting-edge communications tools for the first time in history.

But there are two sets of problems with Prahalad's examples. First, so long as the poor spend what little money they have, they will remain poor, even if they now benefit from higher-quality goods. Prahalad glides over this critical point. In fact, the poor can still be poor even if they pay less for certain essential goods. How? To start with, they can be persuaded (by those aggressive corporations suddenly paying attention to them in pursuit of profit) to purchase things they did not formerly need. Prahalad, for instance, repeatedly celebrates the success of Avon in selling cosmetics in the heart of the Amazon without asking who benefits, really, from those purchases.

Prahalad's blase attitude toward the effects of marketing on poor people is willful blindness. He ought to know better. Members of the middle class are not alone in trying to live beyond their means. Poor people try, too. And they can be ensnared even by well-intended marketing campaigns. I am reminded of a Frito-Lay push I witnessed in the mid-'90s in Bangkok. Potato chips were alien to the Thai diet, dominated by fruit- and rice-based snacks. Unhappy with locally grown potatoes, Frito-Lay trained Thai farmers to grow better quality ones. Assured of this supply, the company blitzed the snack market, even trumpeting the "nutritional" value of its chips on its packaging. The nutritional labeling gave a healthy impression and was successfully used by Frito-Lay to cut into the sales of countless roadside snack peddlers. But even the best-packaged snack foods are a poor substitute for plentiful local fruits and rice dishes, usually available at a fraction of the price. In short, a taste for packaged potato chips are making Thai people fatter and less healthy--and cannot possibly help the budget of any poor person buying them. Such a clear contradiction--how better services to the poor can nevertheless ravage their daily budget--seems lost on Prahalad.

Then there is the problem that Prahalad's favorite examples--say, the low-cost prosthetic foot and the bargain eye surgery--are priced too high for the genuinely poor to afford. What's more, multinational corporations, despite Prahalad's exhortations, aren't well-positioned to serve the poor. In India, for instance, domestic companies, not multinationals, are most attuned to impoverished consumers. Consider the push by Tata, one of India's largest domestic carmakers, to build an auto for the masses. The company's goal: a new car priced at \$2,200 that will appeal to the five million Indians who own motorbikes but can't afford a standard car. Tata plans to sell both ready-to-drive and kit versions of the car. The kit version, the company thinks, could spawn a cottage industry of small auto assemblers around the country. No multinational carmaker has a business model that can be easily adapted to match Tata's bold goal of a people's car. The same is true in such diverse fields as pharmaceuticals, where India's leading companies are far ahead in making drugs for the poor, and in water pumps, where the most reliable and least costly devices are Indian-designed and -made. That India's leading companies concentrate on the poor shows the benefits of restraining, not unleashing, multinationals. It was India's protectionist trade rules, maligned for decades, that gave its domestic companies the living space out of which today's innovations flow.

The most serious shortcoming of Prahalad's feel-good message is that it ignores the experience of the poorest part of the world: sub-Saharan Africa. China and India, where Prahalad is most excited about the promise of a BOP strategy, have seen dramatic reductions in poverty over the past 20 years. What's more, these achievements were not the result of the private sector pursuing profits from the poor. In fact, multinational corporations have spent billions pursuing Chinese consumers over the past decade, and almost none of them have any profits to show for it. Instead, with the help of big government, China has exported its way out of poverty, becoming the workshop for the world. India has grown in a more complex fashion, through a sharper focus on its domestic market. But Africa is poorer today than in 1990. This striking trend sets the continent apart from the rest of the world. In the '90s, the percentage of people living on \$1 per day in East Asia fell by half, from about 30 to 15 percent. South Asia (chiefly India, Pakistan, and Bangladesh) saw rates fall from the low forties to the low thirties. Only in sub-Saharan Africa, where poverty rates were already the highest in the world, have they grown higher still, now approaching 50 percent.

Africa arguably needs a BOP strategy more than anywhere else in the world, yet Prahalad has virtually nothing to say about the region. He offers no formal case studies--or even extended examples--of BOP successes in Africa. (The index to his book, *The Fortune at the Bottom of the Pyramid*, contains no entries on Africa, or even individual African countries; a single entry, for an obscure food enterprise in Nigeria, is the lone reference.) Prahalad's neglect of Africa betrays the big lie at the heart of his argument: that business, pursuing profits, can provide the essentials of a good life to the poorest members of society; that the goods and services we hope even the poor can possess--things like clean water, decent schools, basic electricity, public safety--can be delivered at a profit, and by a private business.

Prahalad says the BOP model can vastly improve public services for the poor, and one consequence of his ideas is to underscore the importance of privatizing failing public enterprises. Indeed, the capacity of private corporations to deliver services once viewed as the sole purview of government is central to the BOP movement. To be sure, public services for profit work in some places--and they would work in Africa, too, if there were profits to be made. But there are not. Privatization is a bust in Africa, and not always because Africans have made it difficult for private actors. Consider a brief example of a best-case scenario: the capital city of Accra, Ghana, where, for the past few years, an honest government in a peaceful country has tried to attract foreign capitalists to invest in its creaky water system. The plan, which received the blessing of the World Bank, was well-conceived. To entice investors, the government raised water rates in advance of improvements in the water system--in the hope that higher revenue would entice a foreign savior to plunk down cash to pay for much-needed improvements in service. (Most of Ghana's poor city-dwellers have no piped water, and even those who do are subject to frequent outages.) Of course, this all sounds like a great bottom-of-the-pyramid opportunity, except for one problem: No foreigners, or even locals, offered to invest in water delivery. Not one of the world's three major water companies was interested in putting money into Ghana. No local entrepreneurs wanted to either. And

they didn't for a good reason. There's no profit in it. The truth is that extracting money from poor Africans in exchange for water isn't a business at all. It's a public service.

The best solution to poverty is, of course, the creation of good jobs--of the sort that changed the life of my Malaysian friend Donald Jagau. And, to be sure, good jobs are of little value if no markets exist to serve these newly enriched consumers. But Prahalad turns this traditional model--first jobs and then markets--on its head. Instead, he argues for elevating the weakest consumers--insisting that the most powerful capitalists ought to take them as seriously as the wealthiest people of the world. In doing so, he presents a seductive alternative reading of the multinational corporation--as an agent of transformation and empowerment, not a force for exploitation and the concentration of wealth. It's no wonder he has inspired the allegiance of the world's CEOs.

But can selling to the poor help alleviate poverty? And can multinational corporations really profit from the impoverished while at same time delivering goods and services the poor value? In a Harvard Business Review article two years ago, which was the seed for his new book, Prahalad conceded that "big companies are not going to solve the economic ills of developing countries by themselves.... But it's clear to us that prosperity can come to the poorest regions only through the direct and sustained involvement of multinational companies." But Prahalad's confidence in big corporations is not justified by their performance thus far. His curious experiment, still in its infancy, may yet prove his faith in the "fortune at the bottom of the pyramid." But, more likely, it will show that he traded in false hopes.

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