

History of the economic pyramid economics essay

[Economics](#)



**ASSIGN
BUSTER**

Introduction

The purpose of the paper is to study the antecedents of new business model development in multinational corporations attempting to launch new initiatives targeting entry into base-of-the-pyramid (BoP) markets (Prahalad & Hart, 2002). BoP market offer a good context for studying new business model development. It will then move on to draw a demarcation between two microfinance models, Grameen Bank and SKS Mircofinance, on how microfinance works for the poor in Bangladesh and India.

Q1 How do the business models operating " at the base of the economic pyramid" differ from more traditional business models?

In recent years, there has been growing interest in Bottom of the Pyramid concept by C. K. Prahalad, according to which organisations can help to eliminate poverty by entering the market of four billion low-income people that constitute the base of economic pyramid. The 4 billion people at the base of the economic pyramid (BoP) are generally those with low incomes below \$3, 000 in local purchasing power which accordingly living in relative poverty (IFC, 2007). Their incomes in current U. S dollars are less than \$3. 35 a day in Brazil, \$2. 11 in China, \$1. 89 in Ghana, and \$1. 56 in India. The estimated market sizes of these segments are illustrated in figure 1. Yet together they have substantial purchasing power as the BoP constitutes a \$5trillion global consumer market (refer to appendix) (IFC, 2007). Most companies have not traditionally considered people at the base of the economic pyramid as potential customers due to low level of their individual incomes (DI, 2007). The idea behind of the BoP concept encourages

multinational companies to serve the highly underserved and less competitive market at the BoP, as it gives a new market opportunity from making significant profits and perhaps contributing to the alleviate poverty by selling products to the poor (Are « Bottom of the Pyramid » strategies scalable?). BoP business model-The developing of products customised for BoP markets must take its starting point in the conditions and demands of BoP consumers (CRS EUROPEAN). The extreme price sensitivity of bop consumers requires dramatic cost reductions to create products and services that these consumers can afford. This calls for a business model that accepts a low margin per unit sold in exchange for a high volume of sales (CRS EUROPEAN).-In order to successfully manage business conditions at the bop, companies must be innovates in their approach and customise their products, production, and price to the realities in bop markets.-An ideal example to demonstrate such business model is Danone Grameen which recognized that there are opportunities to combat poverty and malnutrition through innovative business practices. Their aim is to sell at a very affordable price a nutritional dairy product tailored to meet the nutritional needs of Bangladeshi children (World Bank Institute, 2008). 5 principles- There are several principles in appropriately managing the BoP strategy on how an organisation to develop BoP initiatives that contribute to poverty alleviation.-The predominant importance to develop a business model in BoP market is to identify the relevance of the final goods and services (CRS EUROPEAN). The organisations required to recognise and understand the needs of poor customers in order to be aware that the sold products effectively contribute to the communities' development objectives. In addition, it is vital to understand the expectations of all of the partners such <https://assignbuster.com/history-of-the-economic-pyramid-economics-essay/>

as international NGOs, development agencies and local government can be considered for such partnerships. The idea behind this is mainly to organise for the lack of information, inadequate infrastructure and informality linked to BoP markets (Scalable). Local partners such as NGOs provide knowledge on the market and understanding of the local context (London & Hart, 2004).-In addition, organisations interested in exploring the opportunities at the BOP should look for solutions in the form of new products and new business models that can provide products and services at affordable prices to support purchasing power and market access from the poor (CRS European). Some of the first initiatives along these lines were taken by Procter & Gamble and Unilever, which have developed affordable, for-profit consumer products for some of the poorest regions of the world and simultaneously targeted widespread social problems such as water pollution and iodine deficiency (Olsen & Boxenbaum, 2009).-The companies need to build network in production, distribution and sales processes to evade the lack of transportation infrastructure linking to these areas in BoP market (CrS Euroocean). Companies use a network of local community to transport production closer, accomplish distribution and marketing process, and this helps to reduce transport costs while providing jobs and income opportunity to the local community (CRS Eurepoean). For instance, Danone Grameen utilizing a local production and distribution system designed to create jobs for the local community, including " Grameen ladies" who will make sales door-to door, and minimizing its environmental impact (World Bank Institute, 2008).- Information and training services are fundamental in BoP strategy as they can provide the knowledge for companies to achieve the maximum benefits of the products and services offered (CRS EUREPOEAN).- BoP

business models attempt to minimise the negative externalities and promote positive externalities (CRS EUREPOEAN). As it is believe that business has a licence to operate which can be revoked if the externalities are too negative.

Differences between BoP Model and Traditional Business Model

There are distinct differences between those business models operating in BoP market compared to a more traditional business model. Traditionally, most of the organisations have systematically developed opportunities in the top three tiers and pay no attention to the needs of the bottom tier simply because of erroneous assumptions about its purchasing power and accordingly the economic viability of reaching it (Jose, 2008). Prahalad and Hart (2002) argue that the main assumptions held by most companies about the low purchasing power. As a result, it results to limited market opportunity, difficulties in distribution and gaining access to the market, and the assumptions that the poor are not brand conscious or technology knowledge (Jose, 2008). On the other hand, a market-based business model starts from the recognition that being poor does not eliminate business and market processes as it is essentially all poor trade cash or labour to meet their basic needs (IFC, 2007). In other words, business model operate in BoP market focuses on people as consumers and producers which will make markets more efficient and competitive so that people from the bottom of the pyramid can benefit from them (IFC, 2007). Moreover, traditional business model tend to address unmet needs for health care, clean water, or other basic necessities by setting targets for meeting those needs through direct public investments, subsidiaries, or other contributions (IFC, 2007).

However, the results have not been noticeably successful. In contrast, those business operate in BoP market recognise that it is not just the very poor who have unmet needs and demands cooperation to pay across market segments (IFC, 2007). As a result, it appears to be a resolution in the form of new products and new business models that can provide goods and services at affordable prices. Overall, it can be say that traditional business model do not point forward sustainable solution. While a market-based model recognises that only sustainable solutions can scale to meet the needs of 4 billion people in the bottom of pyramid.

Q2 Compare and contrast the SKS Microfinance model with the Grameen bank model

This section makes a comparison between two banks involved in social banking using microfinance.

Grameen Bank

-Grameen Bank in Bangladesh, have demonstrated that a well-developed, carefully managed commercial system of microlending which help people from the bottom of the pyramid move out of poverty (Prahalad, 2002). The Grameen model is based on borrowers' ownership of the Bank, and all profit is reinvested in the Bank (Peter, 2011). They offer micro-credit, savings and social services without collateral to the poor in order to make capital easily accessible to them for economic activities (Garud, 2013). Grameen bank uses local knowledge, peer-group evaluation, a focus on women, and specific viable projects to extend credit and mitigate risks in lending to the poor (Prahalad, 2002). The bank offer loans to poor particularly the women in groups of five or small groups in order to create peer social pressure and

enable them the opportunity to purchase equipment and engage in micro enterprises (.....). According to Muhammad Yunus the founder of the Grameen Bank, emphasized that it builds some sort of social power to the poor as they often lack of collateral (....). He argued that the conventional banking system is anti-poor, anti-women and anti-uneducated and thus, has contributed to maintaining the statusquo between the rich and poor (.....).- Instead of giving micro-credit to the group of people, Grameen Bank has been able to demonstrate the effectiveness of microfinance programs towards sustainable development for the rural poor in Bangladesh (Rafiqur & Nie, 2011). For example, Grameen launched its yoghurt business, GrameenDanone, which provides malnutrition children with a low-cost source of nutrition.

Weaknesses

-The repayment system of 50 weekly equal instalments is not practical because the poor do not have a stable job (....). In addition, in a typical rural community, during lean seasons it will become practically impossible for them to repay the loan.-Pressure for high repayment drives members to money lenders (..). Credit alone cannot alleviate poverty and the Grameen model is based only on credit. Consequently, haste can lead to wrong selection of activities and beneficiaries.

SKS

-SKS Microfinance is the largest microfinance institution in India and is widely considered one of the fastest growing microfinance institutions worldwide (Donald & Philip, 2011). It operates primarily in India where the largest market for bottom of the pyramid. SKS's model was initially based on the <https://assignbuster.com/history-of-the-economic-pyramid-economics-essay/>

highly successful Grameen Bank's Joint Liability Group model of lending, where the company provides small value, collateral free loans for income generation to poor women in groups (...not found..). This model has proven extremely successful with over 99% repayment rates due to group model, which ensures credit discipline through mutual support and peer pressure. The SKS microfinance model finances poor individuals and entrepreneurs with contract requiring beneficiaries to do weekly repayments and allow borrowers to take loans for a range of income generating activities (...).-The founder of SKS Microfinance, Mr. Akula expressed his agreement with the Grameen Bank's group lending model, but not on Yunus's theory that microfinance firms should be merely as social businesses (Vikram, 2008).- SKS Microfinance converts from being a non-bank finance corporation into a bank, the objective of this model is to make maximum profit as it is investor driven based (...).-SKS Microfinance believes for-profit models as the only way to provide enough capital to the microfinance business (Peter, 2011).

The argument between Muhammad Yunus and Mr. Akula

-Muhammad Yunus expressed that he does not oppose microfinance making a profit, but doubt that SKS will be able to manage its social mission with the demands of a traditional profit-maximising business (Kwong, 2010). The main commitment of any public company is to make dividends for its shareholders, while the main commitment of microfinance is to serve the poor. Yunus argued that SKS will place its shareholders' interests above the ones of the poor. On the other hand, Mr. Akula emphasized that having access to commercial capital markets as the only way to raise sufficient funds to the microfinance business to meet the needs of the poor (Kwong,

2010). In addition, he argued that it is extremely difficult to secure a banking license in India. In response, Muhammad Yunus claimed that the instability and unpredictability of the commercial capital markets will (Kwong, 2010).

Weaknesses

The model is heavily dependent on investors' and lender's funds as the SKS model do not accept deposit of any kind on their own (...). Since the objective of the SKS microfinance model is profit maximization, thus all efforts are made to put the interest rate above 35%. According the Reuters News, the over pressure on loans beneficiaries push customers to commit suicides as the loans are inflexible and pressing borrowers through high interest rates due to the huge structure being set up by this model operational cost turn to be very high (Kashyap & Munroe, 2010). The Indian government has pushed new regulation in the attempt to get rid of the high interest rates. The development deeply affected the rating of SKS shares, but it also affects the credibility of SKS.

Conclusion

It is well known that conventional banks are profit maximizing whereas Grameen Bank's objective is to provide financial services to fight against poverty.