STANFORD
GRADUATE SCHOOL OF BUSINESS
STANFORD SOCIAL INNOVATION *review*

Romanticizing the Poor

By Aneel Karnani

Stanford Social Innovation Review
Winter 2009

STANFORD
GRADUATE SCHOOL OF BUSINESS
Stanford Social Innovation Review
518 Memorial Way, Stanford, CA 94305-5015
Ph: 650-725-5399. Fax: 650-723-0516
Email: info@ssireview.com, **www.ssireview.com**

Romanticizing the Poor

By Aneel Karnani | Photograph by David Turnley, Corbis

Market solutions to poverty are very much in vogue. These solutions, which include services and products targeting consumers at the "bottom of the pyramid," portray poor people as creative entrepreneurs and discerning consumers. Yet this rosy view of poverty-stricken people is not only wrong, but also harmful. It allows corporations, governments, and nonprofits to deny this vulnerable population the protections it needs. Romanticizing the poor also hobbles realistic interventions for alleviating poverty.

Fighting poverty with business has become very popular. Organizations from the environmental think tank World Resources Institute (WRI), to the World Bank, to the United Nations Development Programme are promoting business strategies to increase poor people's[1] consumption and entrepreneurship. Business schools such as those at the University of Michigan and the University of North Carolina at Chapel Hill have set up centers to find out how businesses can better involve the bottom of the pyramid (BOP)—that is, the 2.5 billion people worldwide who live on less than $2 per day.

Meanwhile, books such as John Weiser's *Untapped*, Craig Wilson and Peter Wilson's *Make Poverty Business*, and Vijay Mahajan and Kamini Banga's *The 86% Solution* suggest how serving the BOP can reap profits. Multinational corporations, including Unilever and S.C. Johnson & Son, offer products and services that both appeal to and purportedly aid the BOP. The world's top CEOs discussed strategies for targeting the BOP at the most recent World Economic Forum. Even the term "bottom (or base) of the pyramid" has become common usage in both development economics and business.

A billboard peddles beer in a South African township. Corporations often exploit poor people's vulnerabilities, while NGOs and governments overestimate their strengths.

Proponents of these market solutions assume that poor people are fully capable and willing participants in free market economies. For example, in the first paragraph of his best-selling book *The Fortune at the Bottom of the Pyramid: Eradicating Poverty Through Profits*, University of Michigan business professor C.K. Prahalad urges readers to recognize the poor as "resilient and creative entrepreneurs and value-conscious consumers."[2] On its Web site *Nextbillion.net*, WRI emphasizes the "potential of the world's poorest citizens as entrepreneurs, employees, and discerning consumers." The United Nations' Web site declares that microentrepreneurs are using small loans "to grow thriving businesses ... leading to strong and flourishing local economies."

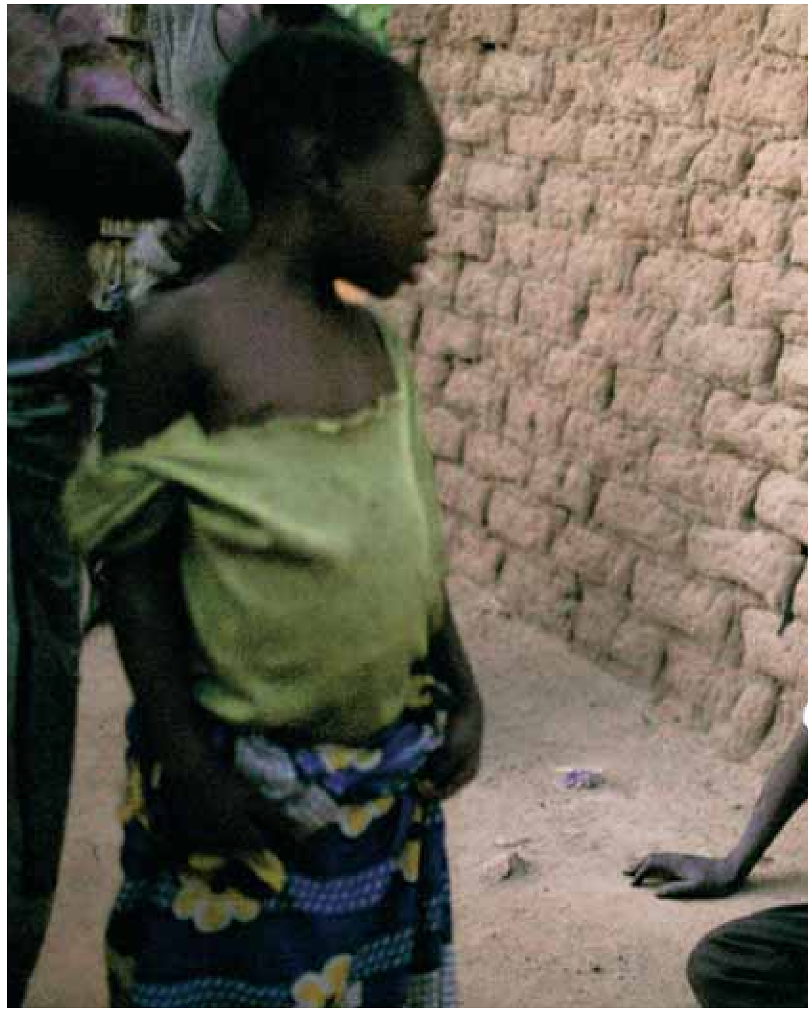
Beneath these beliefs in the market readiness of poor people lies a more basic assumption: people in dire straits are well-informed and rational economic actors. Yet this view denies the fact that poor people often act against their own self-interest. Of course, wealthier people sometimes do so, too. But poor people face far worse consequences for their bad choices than do more affluent people. And so romanticized views of BOP people as value-conscious consumers and resilient entrepreneurs are not only false, but also harmful. These views lead states to build too few legal, regulatory, and social mechanisms to protect the poor, as well as to rely too heavily on market solutions to poverty.

I do not advocate sprawling governments, high taxes, or tightly regulated private sectors. For decades, such statist policies stifled economic growth in countries like India and China, and contemporary economic history clearly demonstrates that the free market system is the best way to achieve overall growth and development. I do believe, however, that states must impose some limits on free markets to prevent the exploitation of the poor. (As the recent collapse of U.S. financial markets shows, they also need regulation to prevent the self-destructive tendencies of free markets.) Another vital role of the state is to provide basic services such as infrastructure, public health, and education. More broadly, businesses, nonprofits, and governments must recognize that poor people face fundamentally different social, psychological, physical, and economic realities than do their wealthier counterparts.

BAD CHOICES

Many advocates of market-based solutions to poverty view poor people as rational consumers who, if given more options, would make better choices—that is, choices that would increase their economic welfare. They see no problem with encouraging the poor to spend their already meager incomes on low-priority products and services. They further argue that the poor have the right to determine how to spend their limited income and are in fact the best judges of what is in their best interests.

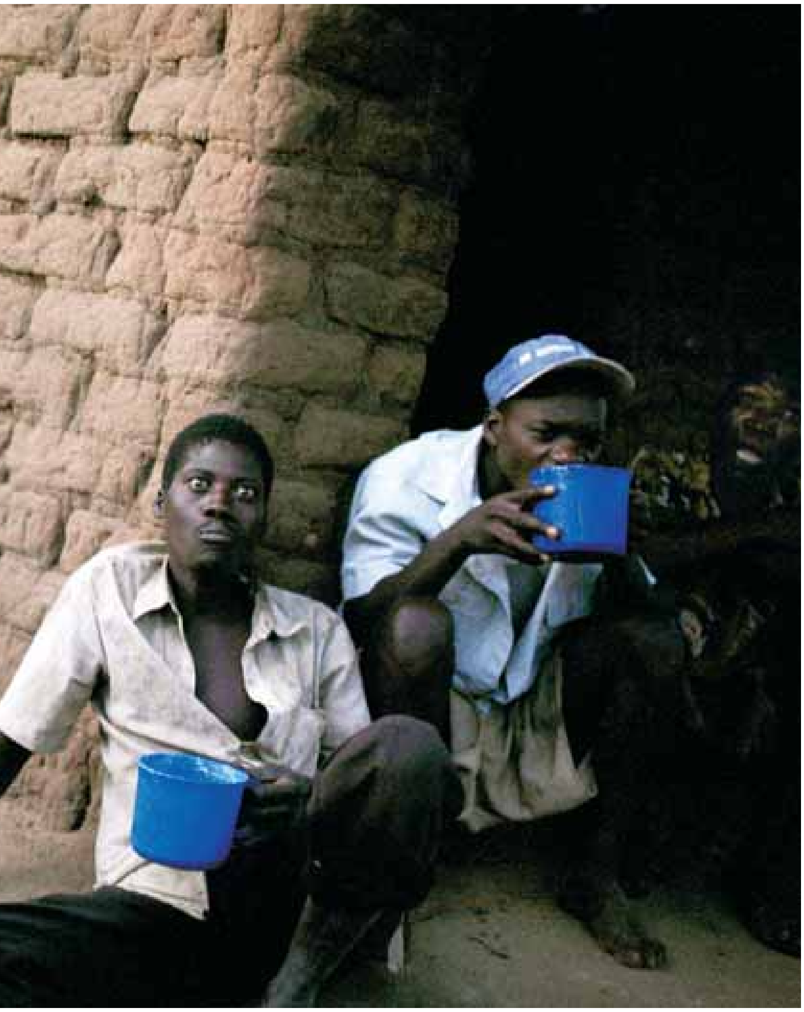
Yet these advocates do not acknowledge that the poor lack the education, information, and other economic, cultural, and social capital that would allow them to take advantage of—and shield themselves against—the vagaries of the free market. More generally, they do not recognize how strongly people's backgrounds and experiences shape their desires and actions. As Amartya Sen, the Nobel Prize-winning economist, noted in his 2000 work, *Development as Freedom*: "Deprived people tend to come to terms with their deprivation because of the sheer necessity of survival, and they may, as a result, lack the courage to demand any radical change, and may even adjust their desires and expectations to what they unambitiously see as feasible. The mental metric of pleasure or desire is just too malleable to be a firm guide to deprivation and disadvantage." In other words, poor people—even more than wealthy people—do not necessarily do or want what is truly in their best interests. Even *The Economist*, a stalwart advocate of neoliberal policies, agrees that the choices poor people make "are not always the best ones."[3]



All people have moments of weakness when they make bad decisions—say, because they lose self-control and yield to temptation. But poor people seem to lose control more often, for reasons that reflect the realities of their daily lives. For example, poor people typically do not have bank accounts, and so they are more likely to spend their readily available cash on impulse purchases, find economists Abhijit Banerjee and Esther Duflo.[4] Some mundane temptations—such as giving their children a treat—prove especially difficult for poor people to resist because so many other people take them for granted.

In addition, poor people more often encounter stressors—including hunger, pollution, crowding, and violence—that lead them

Aneel Karnani is an associate professor of strategy at the University of Michigan's Ross School of Business. His research focuses on competitive advantage, strategies for growth, global competition, and emerging economies. Karnani is also the author of "Microfinance Misses Its Mark," which appeared in the summer 2007 issue of the *Stanford Social Innovation Review*.



PHOTOGRAPH BY PER-ANDERS PETTERSSON/GETTY

In Galufu, Malawi, men consume beer in the street. Poor people have higher rates of alcohol abuse partly because alcohol takes the edge off the stresses of poverty.

to act in ways that may alleviate suffering in the short term, but hinder economic prosperity in the long term. Take bad behaviors such as smoking, drinking to excess, and eating fatty and sugary foods, for example. People everywhere smoke, drink, and eat "comfort foods" to take the edge off the hardships they encounter in their daily lives. Tobacco, after all, is an antidepressant, alcohol is a sedative, and comfort foods dampen the release of stress hormones in the body, as well as increase the production of dopamine—a brain chemical that produces feelings of pleasure.[5]

Accordingly, research documents that the less income people have, the more likely they are to smoke, binge drink, and eat a sugary, fatty diet.[6] These behavioral patterns are reflected in people's spending patterns: poor people spend a larger portion of their incomes on alcohol and tobacco than do more affluent people.[7] Indeed, a recent field study in Sri Lanka reveals that more than 10 percent of poor male respondents regularly spend their entire incomes on alcohol.[8]

The world's poorest people also spend a surprisingly large part of their budgets on ceremonies and festivals—which, in the absence of television and movies, are often the best distractions available. In Udaipur, India, for example, more than 99 percent of extremely poor people—that is, people living on less than $1 per day—had spent money on a wedding, a funeral, or a religious festival in the previous year.[9] The median expenditure on festivals among these extremely poor households was 10 percent of their annual budget.

Mounting evidence suggests that just being poor hinders people's ability to make good decisions. Dozens of psychological studies find that, compared to wealthier people, poorer people feel more powerless, depressed, and anxious, and believe that they have less control, mastery, and choice.[10] "Perhaps at some level this avoidance is emotionally wise," write Banerjee and Duflo: "Thinking about the economic problems of life must make it harder to avoid confronting the sheer inadequacy of the standard of living." Similarly, almost 100 years ago George Orwell observed in his book *Down and Out in Paris and London:* Poverty "annihilates the future."

DIRE CONSEQUENCES

The consequences of bad choices are bad for everyone, but even worse for the poor, who lack the resources—financial, psychological, social, and political—to compensate for their errors. Consider the story of Hasan, a rickshaw puller in Bangladesh who spends 20 cents per day on tobacco. When public health experts Debra Efroymson and Saifuddin Ahmed asked Hasan whether his three children ever eat eggs, he exclaimed: "Eggs? Where will the money come from to buy them?" But if Hasan didn't buy tobacco, each of his children could eat an egg a day, and be healthier as a result.[11] More generally, poor people "could easily save more without getting less nutrition by spending less on alcohol, tobacco, and food items such as sugar, spice, and tea," Banerjee and Duflo conclude. For example, the typical poor household in Udaipur could spend up to 30 percent more on food if it did not spend money on alcohol, tobacco, and festivals.

Consuming alcohol and tobacco not only takes money away from a family's nutrition, but also sets off a cascade of other problems that poor people more frequently encounter. Alcohol abuse, for instance, reduces work performance while increasing accidents, domestic violence, and illness. Because many indigent people earn their livelihoods through physical labor, falling ill means not earning money. Once sick, these people have no insurance or unemployment benefits to restore their health or to prevent their families from sliding even further into poverty. If they are lucky enough to live close to doctors and medical facilities, they rarely have the money to pay for these services. Even in the United States, poor people lack money for and access to high-quality medical services.

NO PROTECTION

Another reason that poor people suffer disproportionately for their bad choices is that corporations, governments, and nonprofits offer them fewer services and protections than they offer richer people. The annual report of virtually every large company claims its mission is to serve some larger social purpose besides making profits. Yet in a recent article about corporate social responsibility (CSR), *The Economist* concludes that for most large public companies, "CSR is little more than a cosmetic treatment."[12] Even nonprofits and foundations skew their offerings to better-off people, finds Stanford University political scientist Rob Reich (see "A Failure of Philanthropy" in the winter 2005 issue of the *Stanford Social Innovation Review*).

In addition, many corporations exploit poor people's vulnerabilities, such as their lack of education and their desire for cheap relief from chronic distress. For example, in Malaysia, bottles of samsu—cheap spirits that poor people favor—claim to be "good for health [and to] cure rheumatism, body aches, low blood pressure, and indigestion." Labels also claim that samsu is good for the elderly and for lactating mothers, finds Australian public health expert Mary Assunta.[13] In an ironic twist on the BOP strategy of selling goods in single servings so that poor people can afford them, samsu is available in small bottles of about 150 milliliters and is sold for as little as 40 cents. "It is obvious that these potent drinks are packaged to especially appeal to the poor," writes Assunta.

Local alcohol producers are not the only ones exploiting indigent people; multinational corporations are also getting in on the act. DOM Benedictine, a French liqueur that contains 40 percent alcohol, touts its health-giving and medicinal properties to poor people in Malaysia. United Kingdom-based Diageo likewise assures Malaysian consumers that Guinness Stout promotes virility. Although laws in the European Union ban advertisements that claim alcohol improves health, African nations either do not have or do not enforce these laws. Advertisers therefore capitalize on the reputed aphrodisiac qualities of beer to promote it heavily to poor people.

It is not only tobacco and alcohol companies that exploit the weaknesses of the poor: Even Unilever, a consumer products company, preys on the anxieties of disadvantaged people. The multinational corporation markets a highly profitable skin-whitening cream called Fair & Lovely to women in 40 countries across Asia and Africa, especially India. Allen L. Hammond, former vice president of WRI and a leading advocate of marketing to people at the bottom of the pyramid, says that Fair & Lovely is a positive example of BOP strategy because it makes poor women "feel empowered" and think that they have choices.[14]

Although Fair & Lovely is doing well for Unilever, it probably is not doing much good for its purchasers or for society. Fair & Lovely's commercials typically depict a depressed woman with few prospects who gains a brighter future by attaining either a husband or a job after making her skin markedly fairer. Several nongovernmental organizations (NGOs) and government officials say that the ads are racist and sexist, and that they entrench women and darker-skinned people's disempowerment.[15] Nevertheless, Unilever still claims to be socially responsible.

Corporations not only work around existing protections to sell poor people things that they do not need, but also work with governments to rewrite laws in their own favor. For example, SABMiller has enjoyed great success in Africa with Eagle, a cheap beer made from locally grown sorghum rather than imported malt, reports *The Economist*. In Uganda, Zambia, and Zimbabwe, SABMiller can price the beer lower than mainstream clear beers because governments reduced the taxes the corporation has to pay. Meanwhile, these countries pass up valuable alcohol taxes that other countries would likely use to support public education and rehabilitation programs.

Tobacco companies are similarly notorious for persuading governments to relax restrictions on the production and promotion of tobacco products (see, for example, "Smoke and Mirrors" in the summer 2008 *Stanford Social Innovation Review*).

Should poor people have the right to consume alcohol, tobacco, and other unneeded products? Yes. Should companies have the right to profit from the sale of these products to the poor? Of course. But in rich, capitalist economies, governments put some constraints on these rights, such as "sin taxes," advertising restrictions, and prohibitions of sales to minors. Yet in many developing countries, these constraints are either poorly enforced or missing entirely.

Governments have a responsibility to guard their most vulnerable citizens from unsavory practices. Yet governments in all countries have problems regulating markets. This is all the more true in developing countries with corrupt governments that are in cahoots with firms. And even when governments in poor countries have good intentions, they often lack the resources and competence to design and administer appropriate regulations.

Other social mechanisms for protecting consumers are likewise very weak in developing countries, and even more so with regard to poor people. Emerging economies often do not offer Alcoholics Anonymous, residential detox programs, or the nicotine patch. The civil society organizations that do exist in these economies usually lack the resources to offer much protection to anyone.

THE MIRAGE AT THE BOTTOM OF THE PYRAMID

BOP PROPOSITION
REALITY

The BOP market size is $13 trillion to $15 trillion.
The BOP market size is only $360 billion.

The poor have untapped purchasing power.
The poor have a low savings rate and little untapped purchasing power.

Profit margins in BOP markets are high.
BOP markets are not very profitable because customers are price sensitive and the cost of serving them is high, given small transaction sizes and poor infrastructure.

Companies can reduce prices dramatically without reducing quality.
For most products, the only way to reduce prices significantly is to reduce quality.

Single-serve packages increase affordability.
Single-serve packages do increase convenience and help poor people manage cash flow. But the only way to increase real affordability is to reduce the price per use.

Large multinational corporations should take the lead in the BOP initiative to sell to the poor.
Markets for selling to the poor usually do not involve large-scale economies, and so small- to medium-sized local firms are better suited for these opportunities.

SMALL CHANGE

Despite the many disadvantages that indigent people face in the marketplace, nonprofits, governments, and businesses are flocking to market-based poverty alleviation programs. For instance, microcredit, the newest silver bullet for reducing poverty, has attracted many billions of dollars in funding. Microcreditors make small loans to poor individuals or groups of borrowers—called microentrepreneurs—whom mainstream financial institutions have traditionally snubbed. Many people have made grand claims about the impact of microcredit, including Muhammad Yunus, founder of Grameen Bank and winner of the 2006 Nobel Peace Prize, who said, "We will make Bangladesh free from poverty by 2030."[16]

As I argued in an earlier article in this magazine, however, microcredit does not significantly alleviate poverty (see "Microfinance Misses Its Mark" in the summer 2007 issue of the *Stanford Social Innovation Review*). The problem with microfinance is that it romanticizes poor people as creative entrepreneurs. Most microcredit clients are not entrepreneurs by choice; they would gladly take a job at reasonable wages if one were available. This should not be too surprising. Most people do not have the skills, vision, creativity, and persistence to be an entrepreneur. Even in developed countries with high levels of education and access to financial services, about 90 percent of the labor force is employees, not entrepreneurs. Meanwhile, as borrowers struggle to repay loans that are unlikely to lift them out of poverty, some microfinance institutions earn handsome returns—such as the 100 percent compounded annual rate of return that investors in Banco Compartamos received (see "Microloan Sharks" in the summer 2008 issue of the *Stanford Social Innovation Review*).

Another BOP strategy for alleviating poverty is to create, package, and market products to poor people. Not only will these BOP businesses bring the world's most isolated, impoverished people into the fold of the marketplace, the thinking goes, they may also make multinational companies a fortune. Prahalad argues that the poor, defined as people living on less than $2 per day, represent a market size of $13 trillion. Other economists make even grander assertions; Hammond once asserted that the BOP harbored $15 trillion in commerce.

Yet these estimates of market size are gross exaggerations. Using calculations from World Bank data available in 2006, I estimated elsewhere that the BOP market was $300 billion in 2002.[17] And then once again, using data from a 2007 report coauthored by Hammond and called *The Next Four Billion*,[18] I estimated a global BOP market size of only $360 billion, which is quite close to my earlier estimate.

My calculations suggest that the BOP market is far smaller than Prahalad and other BOP proponents estimate. Their assumptions are problematic in many other ways as well (see "The Mirage at the Bottom of the Pyramid," at left). And as I argued earlier, poor people are often not in a position to take advantage of market opportunities—and might even be vulnerable to exploitation. Consequently, many BOP programs currently on the ground are not likely to improve the lot of poor people.

MORE GOVERNMENT, PLEASE

I have found little evidence suggesting that poor people are particularly discerning consumers or creative entrepreneurs. Instead, and on many counts, they are worse consumers and entrepreneurs than their wealthier counterparts, and they suffer the worse for it. Yet corporations, governments, and NGOs romanticize the poor. As a result, they continue to rely too heavily on market solutions to poverty.

This is not to deny that free markets can help reduce poverty. In fact, the private sector must play a critical role. Rather than viewing the poor primarily as consumers, people interested in economic development should approach the poor as producers. The best way to alleviate poverty is to raise the real income of the poor by creating opportunities for steady employment at reasonable wages. Firms can do this by creating more employment opportunities in labor-intensive industries and investing in upgrading the skills and productivity of poor people, thus increasing their income potential.

For their part, governments need to help create and grow private enterprises in labor-intensive sectors of the economy through appropriate policies (such as deregulation), infrastructure (such as transportation), and institutions (such as capital markets). They must also protect poor consumers through legal and regulatory mechanisms. NGOs and social activists can help by exerting pressure on governments and companies.

Poverty cannot be defined only in economic terms; it is also about a much broader set of needs. But many market approaches to reducing poverty focus solely on economic ends, viewing social, cultural, and political benefits as by-products. In contrast, I think that social, cultural, and political benefits are desirable in and of themselves. We should emphasize the role of governments and public policies in cultivating and safeguarding these other noneconomic ends. By emphatically focusing on the private sector, market-based poverty alleviation programs distract people from correcting the frequent failures of governments to fulfill their traditional and accepted functions of ensuring safety, providing education, protecting health, and building infrastructure. No alternative to government has proven able to serve these functions. ■

Notes

1 All the research cited in this paper defines poverty as per capita consumption of $1 or $2 per day, measured according to 1990 prices. The World Bank first proposed these definitions of poverty, and experts in development economics and public policy commonly use them.

2 C.K. Prahalad, *The Fortune at the Bottom of the Pyramid: Eradicating Poverty Through Profits,* Upper Saddle River, N.J.: Wharton School Publishing, 2004.

3 "Another Day, Another $1.08," *The Economist,* April 28, 2007.

4 Abhijit V. Banerjee and Esther Duflo, "The Economic Lives of the Poor," *Journal of Economic Perspectives, 21,* 2007.

5 Tanja C. Adam and Elissa S. Epel, "Stress, Eating, and the Reward System," *Physiology & Behavior, 91,* 2007.

6 John W. Lynch, George A. Kaplan, and Jukka T. Salonen, "Why Do Poor People Behave Poorly? Variation in Adult Health Behaviours and Psychosocial Characteristics by Stages of the Socioeconomic Lifecourse," *Social Science & Medicine, 44,* 1997.

7 Shubhashis Gangopadhyay and Wilima Wadhwa, *Changing Pattern of Household Consumption Expenditure,* New Delhi: Society for Economic Research & Financial Analysis, 2004.

8 Bergljot Baklien and Diyanath Samarasinghe, *Alcohol and Poverty in Sri Lanka*, Gjøvik, Norway: FORUT, 2004.

9 Abhijit V. Banerjee, Angus Deaton, and Esther Duflo. "Wealth, Health, and Health Services in Rural Rajasthan," *American Economic Review, 94,* 2004.

10 See John Mirowsky and Catherine E. Ross, "Social Patterns of Distress," *Annual Review of Sociology, 12,* 1986; and Alana Conner Snibbe and Hazel Rose Markus, "You Can't Always Get What You Want: Educational Attainment, Agency, and Choice," *Journal of Personality and Social Psychology, 88,* 2005.

11 Debra Efroymson and Saifuddin Ahmed, *Hungry for Tobacco: An Analysis of the Economic Impact of Tobacco on the Poor in Bangladesh,* Dhaka, Bangladesh: PATH Canada, 2001.

12 Clive Crook, "The Good Company," *The Economist*, January 20, 2005.

13 Mary Assunta, "Impact of Alcohol Consumption on Asia," *The Globe,* 2001. Also see Mary Assunta, S.M. Mohamed Idris, and Mohamed Azmi Abdul Hamid, "The Alcohol Problem in Malaysia," *The Globe*, 2001.

14 Allen L. Hammond and C.K. Prahalad, "Selling to the Poor," *Foreign Policy*, May/June 2004.

15 Aneel Karnani, "Doing Well by Doing Good Case Study: 'Fair & Lovely' Whitening Cream," *Strategic Management Journal*, December 2007.

16 "Bangladesh Will Send Poverty to Museum by 2030," *Financial Express*, February 18, 2007.

17 Aneel Karnani, "The Mirage of Marketing to the Bottom of the Pyramid," *California Management Review*, June 2007.

18 Allen L. Hammond et al., *The Next 4 Billion: Market Size and Business Strategy at the Base of the Pyramid*, Washington, D.C.: World Resources Institute and International Finance Corporation, 2007.