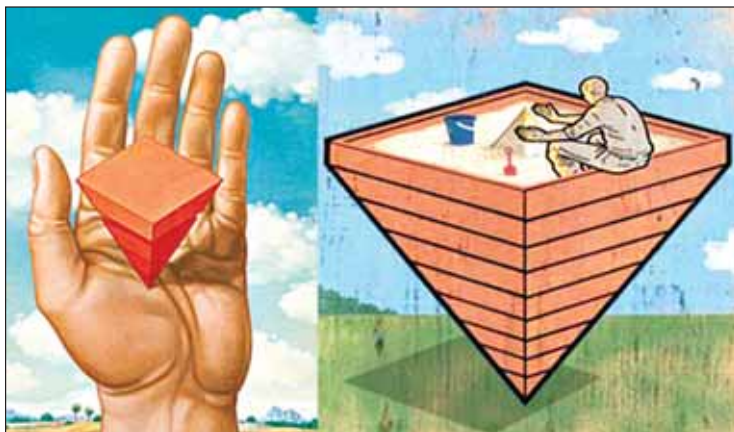




# Bottom of pyramid A market full of fortune



Courtesy: Booz & Company Inc

About half of the different types of raw materials used in manufacturing coatings are imported into India, which corresponds to approximately 30 per cent of raw material requirements. Most are petrochemical based, and therefore fluctuations in crude oil pricing and changes in import duties had a significant impact on profitability. This will be a challenge in addressing the bottom of pyramid market.

■ **Dr Mosongo Moukwa**

Recent research on business models that target the 'Bottom of Pyramid' (BOP), the vast untapped market potential made up of the world's poorest people has emphasised the need for Multinational Companies (MNCs) to radically change their approach and to fundamentally rethink every step in their supply chains. Companies are advised to build new resources and capabilities to implement multiple strategies concomitantly, and to partner with multiple constituencies that often have different strategic objectives

The complexities and potential costs involved in these recommendations for the paints & coatings industry, constitute severe hurdles in practical decision making and realising the financial returns that would justify such investments.

**Paints industry**

The top three producers of paints & coatings represent around 30 per cent of the industry value, and many operate in multiple segments & regions. Companies like AkzoNobel (\$ 13.4 billion), Sherwin Williams (\$ 6.5 billion) and PPG (\$ 10.2 billion) are leading the pack. Their size gives them an added advantage in the market with respect to manufacturing, supply chain and Research & Development (R&D).

The scenario of the Indian paints & coatings industry is depicted in Figure 1. The organised sector comprises indigenous companies as well as subsidiaries of MNCs. The top four are Asian Paints, Kansai Nerolac Paints, Berger Paints and ICI Paints (now part of AkzoNobel). The other players in the segment are subsidiaries of MNCs.

The organised sector represents 57 per cent of the volume. For large companies, the channel-to-market is through paint stores that sell many

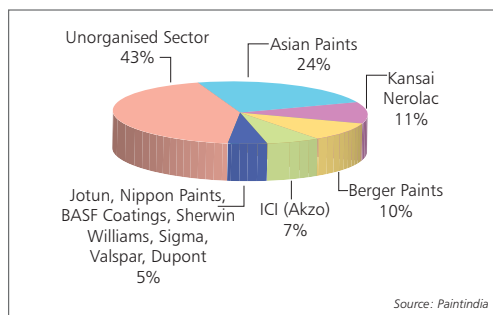


Figure 1: Indian paints industry (marketshares by volume)

Table 1: Indian income pyramid

Income class	Income (\$) at Purchasing Power Parity	Population	
		Million	%
Highest	36,276	26	2
Upper middle	8,736	73	7
Middle	3,432	282	26
Lowest	1,248	701	65

Source : World Development Indicators (2009)

different brands, catering to several layers of customer segments, which have installed the necessary tinting systems for each brand. To support this system, the majors have established large manufacturing facilities in the four main regions within the country.

### Integrating opportunities

In their paper, 'The Fortune at the Bottom of the Pyramid', Late C K Prahalad and Stuart L Hart (2002) defined the target group at the BOP in terms of incomes of less than \$ 1,500 per year. MNCs were thought to be best positioned to face the challenges of selling to the poor, and at the same time fighting poverty. This is because these could draw from a global resource base & superior technology to address local customer needs and to develop those markets, thus stimulating economic development in poor countries.

According to Prahalad and Hart, MNCs would be better off if they integrate in their economic model consumers, who are economically backward and are living in the emerging countries - four billion people living with less than \$ 5-6 a day (Figure 2). The reason is that, even though margins may be weak with this group of consumers, the poor represent a significant latent penetrating opportunity by virtue of their numbers - \$ 13,000 billion - according to Prahalad and Hart. Table 1 shows recent income distribution in India (2009).

### Scale and brand

Markets for selling to the poor usually do not involve significant economies of scale. Markets of the rural poor are

often geographically and culturally fragmented. This, combined with weak infrastructure, makes it hard to exploit economies of scale. Indeed, products sold to the poor are often less complex, reducing the economies of scale in technology and operations.

Products sold to the poor are also usually less marketing- and brand-intensive, further reducing economies of scale. Critics to Prahalad have made the observations that all the examples cited in his work are from small or local organisations. Through their decades of on-the-ground experience in developing countries, MNCs have

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probably already realised that there is no competitive advantage at the bottom of the pyramid, and consequently, have avoided major investments in these markets. To the extent that there are opportunities to sell to the poor, it is usually small to medium sized local companies that are best suited for exploiting these opportunities. Small-scale paint manufacturers in the unorganised sector, 2,400 of them in India, may represent an entry point. The dichotomy is that paint manufacturers mostly want to move the market up the income ladder.

### Quality and cost

One way of alleviating poverty is to reduce the cost of goods and services to the poor, thus, increasing their effective income. In the BOP proposition, Prahalad states that quality should not be reduced. The BOP proposition calls for a price reduction of over 90 per cent. This is too ambitious a target. There are a number of ways to reduce prices. One can reduce profits and costs without reducing quality, and reduce costs by reducing quality. Unless current paints and coatings manufacturers are mostly inefficient, business process redesign will not reduce cost by over 50 per cent without reducing quality. It can be argued that significant improvement in technology allowed for dramatic cost reductions in the IT industry. It has been difficult, however, to find such dramatic cost reduction outside the IT and telecommunication industries.

It is often necessary to reduce 'quality' in order to reduce costs. The challenge is to do this in such a way that the cost-quality trade-off is acceptable to the target. The poor simply cannot afford the same quality products as the rich. They have a different price-quality trade-off. In the decorative paints segments, the range of products varies. At one end of the spectrum, the low-cost distempers, animal casein-based, sold in large volume, estimated at about 2,00,000 tonne per year, (approximately 20 per cent of the decorative sector) products are sold at less than ₹ 40. They still find

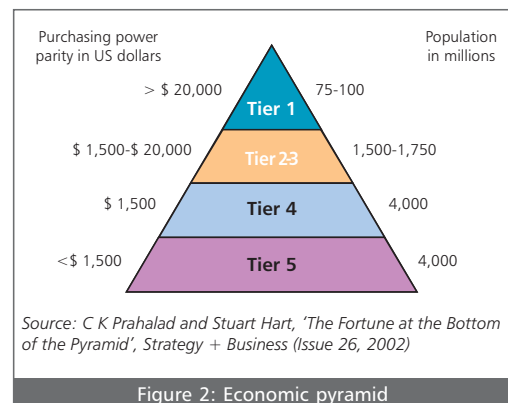


Figure 2: Economic pyramid



## COATINGS CORNER

widespread use in rural areas. Lime powder also continues to serve as a paint substitute in the poorest sections of India. These low-cost materials are far away in terms of quality compared to the premium paint brands. At the other end of the spectrum are the highly durable exterior latex paints, priced at more than ₹ 300.

### New capabilities

The concept of BOP is in some way debatable because of its seductive simplicity, to the point of creating superstitions. Some think that the theory of BOP undervalues the intelligence of entrepreneurs. Indeed, the market is myopic; it is rarely a long-term affair. Opportunities as considerable as \$ 13,000 billion would not escape the vigilance of MNCs, who are constantly looking for new markets. Some consider that BOP market is not only small, but also unlikely to be profitable, especially for a large company.

In reality, the market of BOP does not exist. It must be created, which is different. It is about creating conditions of supply, where infrastructure is lacking, but also of a demand, which would require complex marketing approaches. Converting the poor into consumers is one of aspects of market development which calls for new models and capabilities.

The Resource Based View (RBV) is considered to be the dominant strategy perspective explaining firm-level financial performance. According to RBV, firms achieve above average

performance: through the acquisition of resources at a cost below their potential to create financial returns; and by deploying & configuring these resources into capabilities that create more than the average benefits for customers, and also allow owners to capture part of that value.

Resource scarcity at the BOP makes it difficult if not impossible, to acquire relevant and valuable resources. Even if they are accessible, the value of such resources for use

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in new ways and unusual contexts is not known ex-ante, and can only be accurately assessed where they are currently being utilised. Developing new resources and capabilities, as has been suggested by BOP research, will be challenged by time compression diseconomies, which push the point of expected value creation further into the future. Non-traditional and uncertain environments increase the difficulties in predicting their value-creation potential in new usages. Hence, there is significant risk of getting it wrong while building business models based on new capability configurations at the BOP. Could Prahalad be talking about a target consumer group that is actually in the 'middle of the pyramid'?

### Conclusion

By viewing the poor as customers and not merely as recipients

of donations, the large body of BOP literature has importantly contributed to shifting restrictive paradigms about poverty. However, while several articles & studies on the BOP presented strong arguments for whether & why MNCs should enter low-income markets, they remained relatively silent on how to enter these markets and how all these ingredients, capabilities, resources & partners should be managed & assembled within a given context, to create value.

Large paint manufacturers are continually striving to differentiate through technology advances and to proactively develop new products that can offer contemporary formulations & finishes to the consumer with improved performance. If they want to operate in the BOP markets, there is a need for them to develop new models for these markets with links having non-traditional operators, public or others.

The ability to leverage existing models is limited, and existing research does not provide insights. Serving the poorest of us is an obvious logic of capitalism. However, one has to question the veracity of the take founded on the fight against poverty. The private sector can play a key role in alleviating poverty by viewing the poor as producers, and emphasising buying from them rather than only selling to them. ■



Courtesy: Rainbow Marketing & Exports



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