

Accelerating Inclusive Business Opportunities

Business Models that Make a Difference



ABOUT IFC

IFC, a member of the World Bank Group, is the largest global development institution focused exclusively on the private sector. We help developing countries achieve sustainable growth by financing investment, providing advisory services to businesses and governments, and mobilizing capital in the international financial markets. In fiscal year 2011, amid economic uncertainty across the globe, we helped our clients create jobs, strengthen environmental performance, and contribute to their local communities—all while driving our investments to an all-time high of nearly \$19 billion.

For more information, visit www.ifc.org.

ABOUT IFC'S INCLUSIVE BUSINESS MODELS GROUP

Launched in 2010, IFC's Inclusive Business Models Group mobilizes people, ideas, information, and resources to help companies start and scale inclusive business models more effectively.

For more information, visit www.ifc.org/inclusivebusiness.

ACKNOWLEDGEMENTS

This report would not have been possible without the pioneering efforts of IFC's clients, on whose inclusive business models it is based. IFC thanks all of these clients for their inspiration and leadership.

The writing team included Beth Jenkins, Eriko Ishikawa, Alexis Geaneotes, Piya Baptista and Toshi Masuoka with input from Antara Ganguli, Detelina Kalkandjieva, and Peter Tynan from Dalberg Global Development Advisors. The team would like to give special thanks to their IFC investment colleagues Adrian Bastien, Andi Dervishi, Samuel Dzotefe, Gabriel España, Alex Oliveira, and Miguel Toledo for their insights on the models described here, and a special thanks to Junko Tashiro and Takao Takahashi from the Inclusive Business Models Group.

RIGHTS AND PERMISSIONS

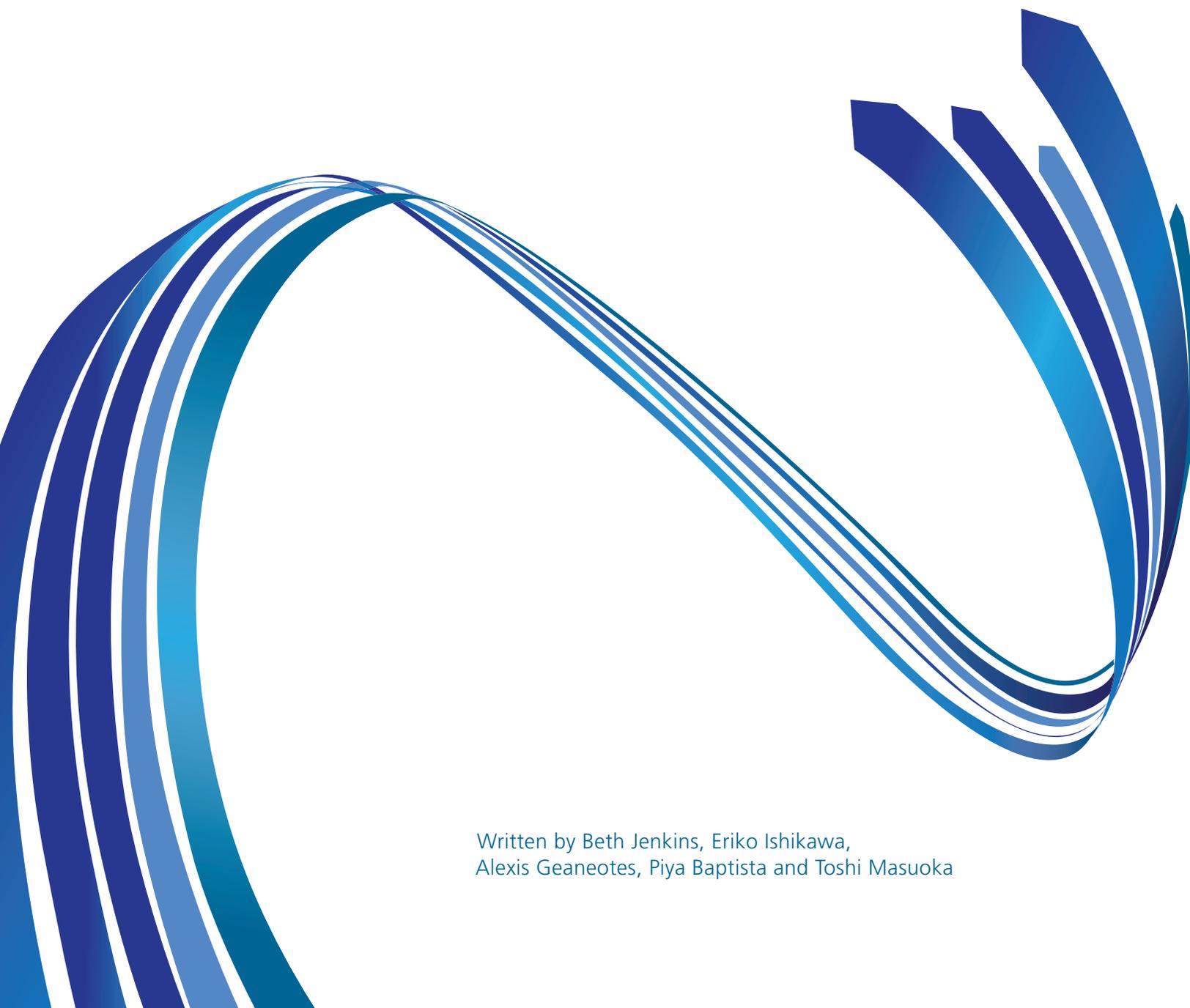
The material in this publication is copyrighted. Quoting, copying, and/or reproducing portions or all of this work is permitted provided the following citation is used:

Jenkins, B; Ishikawa, E; Geaneotes, A; Baptista, P; and Masuoka, T (2011). Accelerating Inclusive Business Opportunities: Business Models that Make a Difference. Washington, DC: IFC.

The findings, interpretations and conclusions expressed herein are those of the authors and do not necessarily reflect the views of IFC.

Accelerating Inclusive Business Opportunities

Business Models that Make a Difference



Written by Beth Jenkins, Eriko Ishikawa,
Alexis Geaneotes, Piya Baptista and Toshi Masuoka

Foreword



The International Finance Corporation (IFC) was created 55 years ago to finance private sector growth in developing countries, thereby providing opportunities for people to better their lives. The private sector, as it grows, increases demand for supplies and services from other parts of the economy, creating new business opportunities and jobs. At the same time, pioneering companies have shown how the private sector can bring lower-income populations into this dynamic, engaging smaller suppliers and serving lower-income consumers. This means that the private sector can be an engine for growth and economic inclusion at the same time.

It is IFC's great honor to support more than 200 clients pursuing growth and inclusion across emerging markets, accelerating access to goods, services, and livelihoods for those 4 billion people living at the base of the pyramid—engaging them as suppliers, distributors, retailers, and consumers in ways that are financially, socially and environmentally sustainable. These clients operate in sectors with the potential for widespread engagement and impact on the urban and rural poor, such as financial markets, infrastructure, health and education, and agribusiness.

IFC is providing these clients with long-term debt, equity, and risk-sharing facilities that help them do business in new ways with new population segments. We are providing advisory services that help them address the toughest operational challenges and market conditions.

As a long-term investor, IFC puts its own money and reputation at stake to ensure that projects are successful. We closely monitor our clients' inclusive business models using financial, social, and environmental tools to appraise and evaluate projects before, during, and—for some mature projects—after completion. In this report, we provide an overview of some of the most common inclusive business models in our portfolio for the first time. We believe these models will be useful to anyone interested in how the private sector can be an active player in inclusive growth.

IFC is committed to accelerating inclusive business. We invite those reading this report to join us on this important journey.

Rachel Kyte
Vice President for Business Advisory Services
International Finance Corporation



Readers may have heard the parable of the old Sufi master teaching his disciples about the three levels of knowledge. “There are different ways to know a river,” he began. “First, you can read books about it and learn its length, its source, the types of fish it contains. Then you can go see it. You feel the sand that borders it, and you watch the birds that play over it. Finally, you can dive in. You feel the river’s current, the gradients of temperature, its depth. You wonder if you’re strong enough to swim its length.”¹

When it comes to inclusive business, IFC has been swimming in the river for a long time. IFC invested in GrameenPhone in 1999 and Compartamos in 2001, for example. In the last five years, we have committed over \$5 billion to more than 200 companies with inclusive business models.

As an investor, IFC considers swimming in the river its main reason for being. We learn through hands-on experience providing our clients with investment and advisory services. Only recently have we asked a small team to get out, towel off, and sit down upon the river’s banks to reflect on what we’ve learned. We are systematically reviewing our investment commitments, identifying portfolio companies with inclusive business models. We are capturing those models on paper, writing 31 case studies so far. We are working hand-in-hand with clients to understand the impact those models are having, on the bottom line and on the poor. And we are figuring out how we can do even more.

We are at an early stage in our efforts, with all the analytical limitations that implies. **But we know that the time to start sharing is now.**

This report offers an overview of inclusive business models found within IFC’s portfolio—the challenges they face and the innovative combinations of solutions that make them work. We hope it is a useful reference for other investors and business leaders swimming in this river. And we look forward to engaging with those who want to know more.

Toshiya Masuoka
Director, Inclusive Business Models Group
International Finance Corporation

¹ Adapted from Michael Fairbanks et al. 2009. *In the River They Swim*. West Conshohocken, PA: Templeton Press. Page 3.

Table of Contents

Executive Summary.....	2
IFC’s Perspective	5
Why is Inclusive Business Important to IFC?	5
Why is IFC Important to Inclusive Business?	7
Why This Report?	9
Overview of Inclusive Business Models in IFC’s Portfolio	12
Micro Distribution and Retail	14
Experience-Based Customer Credit	16
Last-Mile Grid Utilities	18
Smallholder Procurement	21
Value-for-Money Degrees	24
Value-for-Money Housing	27
e-Transaction Platforms	29
Insights Across Models	31
Strengthening the Inclusive Business Ecosystem.....	34

Executive Summary

IFC's mission is to create opportunity for people to escape poverty and improve their lives, and we pursue it by investing in the private sector. At a fundamental level, it is the private sector that drives economic growth—a basic ingredient in poverty alleviation. At the same time, the private sector can expand access to goods, services, and livelihood opportunities for the poor, helping to ensure that growth is inclusive. IFC is particularly interested in investments with this dual rationale—investments in what we call inclusive business models.

Inclusive business models expand access to goods, services, and livelihood opportunities for those at the base of the pyramid in commercially viable, scalable ways.

Inclusive business models are helping companies turn underserved populations into dynamic consumer markets and diverse new sources of supply. In the process, companies are developing product, service, and business model innovations with the potential to tip the scales of competitive advantage in more established markets as well. And they are providing clean water, electrical power, modern communications, health care, education, financial services, and income-generating opportunities to millions

of people at levels of quality and affordability they have never experienced—if they ever had access—before.

In the past five years, IFC has invested over \$5 billion in more than 200 companies in nearly 80 countries around the world. We know it can take time to overcome the challenges to inclusive business success, and we aim to help companies accelerate that journey. The need for experimentation and iteration may never be eliminated entirely, but adapting proven models—learning from the experience of others—is quicker and easier than starting from scratch.

As a result, we have decided to publish this overview of a number of the inclusive business models in our portfolio, summarizing and analyzing patterns in the solutions they are using to succeed. IFC has invested in all of the models summarized here. This means that extensive financial, environmental, and social due diligence was done; that the financial projections showed a sufficiently high commercial return; and that all projects have been monitored on a quarterly basis for financial, environmental, and social results. Mature investments in companies with inclusive business models show returns very similar to those of IFC's portfolio as a whole.

MODELS FEATURED IN ACCELERATING INCLUSIVE BUSINESS OPPORTUNITIES: BUSINESS MODELS THAT MAKE A DIFFERENCE

Micro Distribution and Retail: Reaches base of the pyramid (BOP) end consumers who tend to make small, frequent purchases close to home by leveraging and effectively serving existing retail outlets in the neighborhoods where those consumers live. Such outlets are often small, with little space for excess inventory, and run by staff with little business training, scarce working capital, and no access to finance. They need small, frequent deliveries and the ability to buy on credit. They may need custom assortments and/or small-sized products (e.g., airtime cards in small denominations) or pay-per-use services (e.g., minutes of shared mobile phone use) that match BOP consumers' limited, sporadic cash

flows. Many companies using the Micro Distribution and Retail model also provide business skills training and other forms of support to help such retail outlets increase sales, recognizing the link between the outlet's business success and the company's own.

Experience-Based Customer Credit: Generates additional revenue in the form of interest income through lending to customers the company knows are credit-worthy through experience doing business with them in the past—rather than formal credit histories. The model is generally employed by companies outside the

Continued on next page

financial sector, though some may have credit arms or subsidiaries. Some companies focus on their direct customers. One company lends to its customers' customers as well, based on the experience its customers have had with those people in the past (and leveraging their existing relationships to help incentivize repayment). The model is predicated upon limited access to other sources of credit at similar rates or for similar purposes.

Last-Mile Grid Utilities: Extends grid coverage to more distant and often lower-income neighborhoods through a combination of financing, technology, and customer service innovations that help cover capital expenditures, minimize technical and commercial losses, and ensure customers pay on time. The model is based on a clear value proposition to the consumer: greater quality, reliability, convenience, and in many cases, lower cost compared to previously available, often informal utility options.

Smallholder Procurement: Turning geographically dispersed smallholder farmers into reliable sources of quality supply through efficient aggregation methods and customized packages of support services that build capacity and loyalty. Common support services include agricultural extension, business development, access to agricultural inputs, and credit. Sometimes, buyers choose to focus on higher value crops capable of earning a premium in the marketplace to help cover the cost of such support.

Value-for-Money Degrees: Makes university education accessible to all through a combination of innovations that increase affordability and value for lower-income students. To increase affordability, these universities use standardized curricula that can be taught by part-time instructors, accessible physical and virtual campuses that reduce students' transportation

costs, modular programming that matches cash flows, and access to student loan financing. To create value, they offer course content and career services tailored to the job market.

Value-for-Money Housing: Makes home ownership possible for lower-income buyers through a combination of high value for money and facilitated access to mortgage financing. A home is the biggest investment most people ever make and they have to be convinced it is worth the commitment, which can feel risky. Value-for-money housing balances aspiration (with a focus on quality, special features, and the community environment) and affordability (with home sizes and layouts in different price ranges, and features that reduce the ongoing cost of ownership). Because the model hinges upon access to financing, it often involves helping homebuyers—often the first in their families—navigate the mortgage application process.

e-Transaction Platforms: Many low-income people lack access to financial services as a result of the high transaction costs and complex logistics involved in reaching them. Technology companies are beginning to address these challenges through electronic transaction platforms, creating opportunities to serve low-income customers and bringing them benefits spanning convenience, efficiency, security, market access, and integration into the formal financial system. IFC is investing in a diverse set of technology companies that are helping to create the complex infrastructure for a cashless society to function. These companies have different business models. However, at a fundamental level, they display some interesting similarities—like leveraging existing retail outlets and networks, building outlets' business and technology skills, raising consumer awareness and helping them understand the value proposition behind cashless transactions.

Note: IFC's portfolio also includes a significant number of clients in the microfinance sector; this report does not cover the microfinance model because it is already well documented.

The model descriptions in this report are designed as useful references for business managers and entrepreneurs seeking to start, scale, or replicate similar models. At the same time, we believe—and our clients have told us—that there is significant value in learning across models. At the end of the report, we summarize four key insights that influence IFC’s work with clients on inclusive business models:

Creating value for the BOP is paramount: To succeed and remain sustainable over time, a business model must create value for the company and its partners at every step of the chain. But *how* to create value for the BOP can be less obvious. It can be all too easy for people to assume they know what those less fortunate want or need. If good intentions take the place of actual inquiry, they keep companies from truly understanding the suppliers, distributors, retailers, and consumers they are trying to serve. Better information and the experience that comes from “learning by doing” can help companies develop the understanding they need to develop truly compelling value propositions. While cost reduction and cost sharing can help, willingness to pay (in the case of consumers) or invest (in the case of suppliers, distributors, and retailers) is the foundation of any successful inclusive business model.

Inclusive business models are almost always high-touch: They involve significant effort to turn, for example, subsistence farmers into productive and reliable suppliers; neighborhood shops into high-performing retail and distribution channels; and cash-strapped and skeptical people into repeat consumers who are telling their friends. For the most part, BOP markets and sources of supply do not just exist waiting to be tapped—they need active cultivation. The high-touch models required are resource-intensive. Companies must have or be willing to build a significant local presence, including infrastructure, staff, and systems, and they must have a relatively long-term commitment to the market. They must also be capable of generating enough revenues to reach commercial viability.

Many successful inclusive business models are “whole pyramid” models, not just “base of the pyramid” models: Inclusive business models are almost always high-touch, but low-income consumers need relatively low price points. High operating margins can be the answer—but BOP business opportunities offer them relatively rarely. Much more often, IFC sees companies that are making high-touch inclusive business models work by engaging BOP segments as part of much broader markets or supplier bases. “Whole pyramid” approaches enable companies to leverage existing infrastructure, achieve economies of scale, and cross-subsidize. For companies engaging low-income producers, the whole pyramid approach can also help diversify the supply base and manage risk.

Public funding can be used strategically: Because of the development impact inclusive business models can have, funding can be available from governments, multilateral and bilateral donors, and private foundations. Public funding is no substitute for a business case, but it can make an existing business case stronger. One strategy is to use public funding to deepen the market at the base of the pyramid, reaching even lower-income groups than it would have been possible to serve on a purely commercial basis. Another strategy is to use public funding to defray the cost of high-touch activities—like building product literacy among consumers, business skills among small-scale distributors and retailers, and access to financial services throughout the value chain—that are necessary for business growth, and that also generate positive externalities.

IFC hopes this report will point inclusive business leaders worldwide in useful directions in response to the challenges they face, and we remain on call for those ready to take their next steps. At the same time, we hope this report will add to existing literature in the field, helping to build our collective knowledge about how to achieve financial sustainability and scale in inclusive business.

IFC is open for inclusive business.

IFC's Perspective

Why is inclusive business important to IFC?

➤ **Because inclusive business hits IFC's "sweet spot" of growth and inclusiveness.**

IFC's mission is to create opportunity for people to escape poverty and improve their lives, and we pursue it by investing in the private sector.² At a fundamental level, it is the private sector that drives economic growth—a basic ingredient in poverty alleviation. At the same time, the private sector can expand access to goods, services, and livelihood opportunities for the poor, helping to ensure that growth is inclusive. We are particularly interested in investments with this dual rationale—investments in what we call inclusive business (see "What is inclusive business?" on page 6).

Inclusive business models expand access to goods, services, and livelihood opportunities for those at the base of the pyramid in commercially viable, scalable way.

➤ **Because inclusive business is critical for companies seeking to grow.**

The world's leading companies expect emerging markets to generate approximately 70% of global economic growth over the next few years.³ Those that benefit the most will be the ones that turn underserved populations into dynamic consumer markets and diverse new sources of supply. Companies with inclusive business models are doing both. And in the process, they are developing product, service, and business model innovations with the potential to tip the scales of competitive advantage in more established markets

as well—a phenomenon McKinsey & Company has called "innovation blowback."⁴

➤ **And most importantly, because inclusive business is critical for the world's poor: the four billion people living at what is known as the base of the economic pyramid.**

By definition, people living at the base of the pyramid have limited incomes. On top of that, they often lack access to clean water, electrical power, good roads, modern communications, health care, education, financial services, consumer goods, and other products and services at the levels of quality and affordability that wealthier people enjoy. In fact, in highly underdeveloped markets, they often pay more, in absolute terms, for inferior products—a phenomenon known as the "BOP penalty." It is time to begin seeing those living at the BOP not as subjects of charity but as creative and resilient entrepreneurs and value-conscious consumers.⁵ This is something many IFC clients have recognized for a long time. Around the world, IFC clients are engaging the BOP as producers, distributors, retailers, and customers, offering them greater dignity, opportunity, and choice in their lives and futures.

2 IFC is the largest multilateral source of loan and equity financing for the private sector in developing countries, established in 1956 to complement the work of the World Bank, which lends to the public sector. IFC is a development institution with a triple A rating. We raise funds in the international capital markets and invest on commercial terms because we believe markets are powerful drivers of choice, economic opportunity, and poverty alleviation.

3 The Economist. 2010. "The World Turned Upside Down." *The Economist*, April 17, 2010.

4 Seely Brown, John, and John Hagel III. 2005. "Innovation Blowback: Disruptive Management Practices from Asia." *McKinsey Quarterly* 2005, Volume 1.

5 Prahalad, C.K. 2004. "The Fortune at the Bottom of the Pyramid: Eradicating Poverty through Profits." Upper Saddle River, NJ: Wharton School Publishing.



WHAT IS INCLUSIVE BUSINESS?

A \$13 billion telecommunications company operating in eight countries. An early-stage venture using discarded rice husks to generate electricity. A 160 year-old commodity trading company. A financial institution making loans to coffee cooperatives in Ethiopia or business school students in Colombia. A tech-savvy hospital, and a wholesaler serving five-shelf village stores with five-can deliveries of Coke.

Welcome to IFC's portfolio of clients with inclusive business models.

An inclusive business model is like any business model. First and foremost, it has to be commercially viable. To qualify for investment from IFC, it also has to be able to scale. The key differentiator is that an inclusive business model has to expand access to goods, services, and income generating opportunities for people living at the base of the pyramid.

The "base of the pyramid" concept has become popular shorthand for describing those living below a given income or spending threshold. But many debate where these thresholds belong. Some default to traditional \$1 or \$2 a day poverty lines. Others point out that \$5 or \$8 a day is still poor by any objective measure.

The real question, however, isn't the right income threshold—but what such a threshold really captures. Income is just one parameter for poverty, and an imperfect one at that. The seminal World Bank study "Voices of the Poor," based on interviews with 20,000 people living in poverty around the world, found that the poor themselves define their situations in a far more multidimensional ways:

- "There is nowhere to work." (Ecuadoran woman)
- "We need water as badly as we need air." (Kyrgyz woman)
- "Whoever goes to the health clinic healthy comes out sick." (Egyptian villager)

IFC thinks about poverty in the multidimensional way the poor themselves define and experience it—in terms of income and of access to goods, services, and economic opportunities. Too often, the poor lack access to products and services at the prices and levels of quality that others rely on. Whether they are slum dwellers, rural villagers, small-scale farmers, informal laborers or micro-entrepreneurs, they are denied clean water, electrical power, good roads, modern communications, health care, education, financial services, consumer goods, and—perhaps most important—steady sources of income.

People living at the base of the pyramid can obviously be found in the least-developed countries of sub-Saharan Africa and East Asia and the Pacific. But, perhaps surprisingly, even more live in larger, middle-income countries like China, India, Indonesia, and Brazil. In fact, as of 2007-8, three quarters of the world's poorest people—those living on less than \$1.25 a day—lived in middle-income countries.⁶ Inclusive business models are important regardless of country. They are important wherever the poor themselves are to be found.

⁶ Sumner, Andy. 2010. "The New Bottom Billion: What if Three-Quarters of the World's Poor Live in Middle-Income Countries?" Brighton, UK: Institute of Development Studies.

Why is IFC important to inclusive business?

➤ **Because IFC is one of the biggest investors in inclusive business in the world.**

With over \$5 billion invested in more than 200 companies in nearly 80 countries in the last five years, IFC is a driving force behind the proliferation and scale of inclusive business models worldwide. IFC is also one of the few inclusive business investors with a global presence (see “Where does IFC Invest in Inclusive Business?” on pages 10–11).



IFC'S INVESTMENT APPROACH

IFC is a development institution. But we invest on commercial terms, because we believe that market discipline is a powerful driver of consumer choice and sustainable economic growth. We expect our investments to generate financial returns, which demonstrate that our clients are generating value for their customers efficiently. We also expect our clients to adhere to strict social and environmental standards, which ensure that they are not generating value for customers and investors at the expense of other stakeholders.

IFC's inclusive business clients go through the same financial, social, and environmental due diligence all our clients go through. They also generate similar

returns. One study of operationally mature investment projects showed returns of 6.7% on loans and 19.1% on equity.⁷ The average loan size for an inclusive business client in FY10 was \$23.8 million, and the average equity investment was \$11.5 million. IFC also offers risk-sharing facilities and partial credit guarantees.

While the average investment size is relatively large, IFC occasionally makes smaller investments, too—both directly and through funds. Facilities with streamlined approval procedures can make it easier to invest directly in smaller firms, reducing the transaction costs involved. Funds fulfill a similar function. IFC has invested in a number of funds focused on inclusive business, including Aureos, IGNIA, and Leapfrog.

⁷ Calculations for real (i.e., non-financial) sector clients with inclusive business models whose investments were committed between FY00-FY10 and were operationally mature enough as of FY11 for financial return data to be available. The sample of clients meeting these criteria is still small.



- **Because IFC can provide targeted advisory services when clients face fundamental challenges in expanding reach and impact at the BOP.**

IFC realizes that, as critical and as difficult as it can be to get financing on the right terms, financing is one of many challenges inclusive business models face. Some challenges are so fundamental that companies cannot tackle them alone—because they do not have the expertise or because there would not be enough of an immediate return. In cases like these, IFC advisory services can help clients build the capacity of BOP suppliers, distributors, and retailers; educate consumers about valuable new products and services; and facilitate access to financing all along the value chain. The costs are shared among the client, IFC, and its donor partners, in proportion to the balance of private benefit and public good created.

INTEGRATED INCLUSIVE BUSINESS INVESTMENT AND ADVISORY SERVICES



TRIBANCO
(Brazil)

- \$25 million in long-term debt financing
- \$21.3 million in equity
- Financial literacy program development
- Training monitoring and evaluation framework
- Documentation and visibility



ECOM
(multiple countries)

- \$80 million in long-term debt financing
- Farmer training
- Partnership brokering
- International replication
- Documentation and visibility



AIRTEL MADAGASCAR
(previously Zain; Madagascar)

- \$25 million in long-term debt financing
- Village Phone Program design
- Partnership brokering
- Documentation and visibility

➤ **Because IFC has developed considerable knowledge of what makes inclusive business models work.**

In the process of providing investment and advisory services to clients around the world, IFC is developing increasingly detailed knowledge of the solutions companies can use to do business with those living at the BOP, profitably. IFC is now working to share this knowledge, by facilitating direct exchange among companies and through publications like this one. It is our hope that learning from the experiences of others will help IFC clients and their peers accelerate the journey to inclusive business success.

Why this report?

IFC knows it can take time to overcome the challenges to inclusive business success, and we aim to help companies accelerate that journey. The need for experimentation and iteration may never be eliminated entirely, but adapting proven models—learning from the experience of others—is quicker and easier than starting from scratch.

As a result, we have decided to publish an overview of a number of the inclusive business models in our portfolio, summarizing and analyzing patterns in the solutions they are using to succeed. IFC has invested in all of the models summarized here.⁸ This means that extensive financial, environmental, and social due diligence was done; that the financial projections showed a sufficiently high commercial return; and that all projects have been monitored on a quarterly basis for financial, environmental, and social results. Mature investments in companies with inclusive business models show returns very similar to those of IFC's portfolio as a whole. IFC has a significant repository of data on both the financial returns and development outcomes of inclusive business models.

We hope this report will point business leaders worldwide in useful directions in response to the challenges they face, and remain on call for those ready to take their next steps. At the same time, we hope it will add to existing literature in this field, helping to build our collective knowledge about how to achieve financial sustainability and scale in inclusive business.

⁸ IFC has also invested significantly in microfinance, beginning with an \$85 million facility for Internationale Projekt Consult (IPC) in June 2000. This report will not cover microfinance because the model is already well documented.

Where does IFC invest in inclusive business?



MITIENDA MEXICO

Wholesale distribution

Provides 1,300 small, rural retailers affordable door-to-door delivery of individual items within 48 hours—along with extended payment terms and business training to improve sales.

IFC's investment: \$2.5 million in equity



DUOC UC CHILE

Higher education

Educates more than 63,000 students, 64% of them from Chile's lowest three income segments and 70% the first in their families to receive higher education.

IFC's investment: \$30 million in long-term debt financing, \$19 million guarantee



CEMAR BRAZIL

Electric utility

Brings electricity to approximately 1.7 million people in the low-income state of Maranhão, including 230,000 new connections under the government's Light for All program.

IFC's investment: \$80 million in long-term debt financing

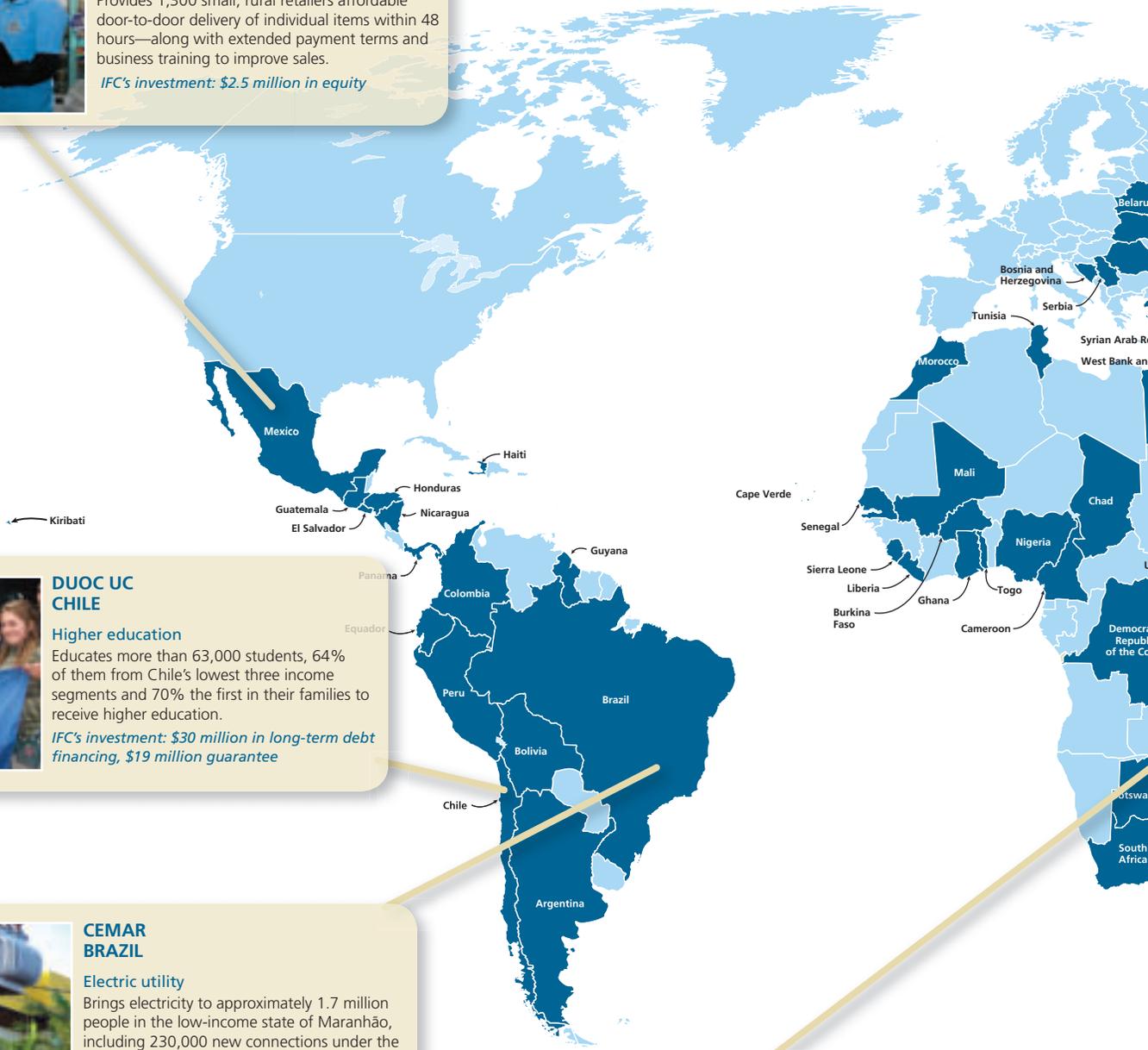


BAKHRESA GRAIN MILLING MALAWI

Agribusiness

Supplies small bakeries and pop-and-mom retail outlets with packaged wheat flour along with technical skills and business training to improve their productivity and sales.

IFC's investment: \$5 million in loans





NIB INTERNATIONAL BANK ETHIOPIA

Agriculture finance

Provides 62 cooperatives made up of 45,000 smallholder coffee farmers with working capital loans to produce high-quality, washed coffee that earns a premium in the export market.

IFC's investment: Up to \$10 million 3-year renewable risk-sharing facility



MANILA WATER PHILIPPINES

Water utility

Provides water and wastewater services to 6.1 million people in Manila. Customers pay 20 times less per cubic meter than they did for trucked water, and 99% of them have 24-hour access.

IFC's investment: \$60 million in loans and \$15 million in equity



PT. SUMMIT OTO FINANCE, INDONESIA

Financial services

Provides more than 1.6 million low- and middle-income consumers with motorcycle financing, increasing their mobility and therefore their access to markets and services.

IFC's investment: \$45 million in long-term debt financing



SUVIDHAA INDIA

Payment technology

Offers low-income customers the means to pay online for a variety of virtual products and services, through 42,000 retail outlets reaching four million people in 28 states.

IFC's investment: \$5 million in equity



DIALOG TELEKOM SRI LANKA

Mobile telecommunications

Provides mobile phone service to approximately 6.3 million people, including underserved remote populations. Nearly 40,000 typically small-scale retailers stock Dialog products.

IFC's investment: \$50 million in long-term debt financing and \$15 million in equity

OVERVIEW OF

Inclusive Business Models in IFC's Portfolio

In this section, we describe seven inclusive business models that are well established within IFC's portfolio (microfinance is also well established within the portfolio, but we do not cover it here as the model has been so extensively documented elsewhere). For several of the models, we also include boxes on complementary business models we see emerging within IFC's portfolio. We hope to provide further detail on some of these complementary models—and additional models that emerge—in future reports.

These model descriptions are designed as useful references for business managers and entrepreneurs seeking to replicate or scale similar models. Each description includes:

- A visual and narrative overview of the model;

- A diagram summarizing key business challenges and solutions along the value chain;
- Text discussion of key solutions, in rough order of importance; and
- A list of selected external success factors at play.

Some readers will find multiple models useful. For example, we have clients implementing hybrid Micro Distribution and Retail and Experience-Based Customer Credit models, and expanding successful Last-Mile Grid Utility models by experimenting with Off-Grid Utility models. Regardless, our clients tell us there is much to be learned looking across models. The most significant cross-cutting insights are summarized in the next section.

INCLUSIVE BUSINESS MODELS SUMMARIZED IN THIS REPORT

Micro Distribution and Retail: Reaches BOP end consumers who tend to make small, frequent purchases close to home by leveraging and effectively serving existing retail outlets in the neighborhoods where those consumers live. Such outlets are often small, with little space for excess inventory, and run by staff with little business training, scarce working capital, and no access to finance. They need small, frequent deliveries and the ability to buy on credit. They may need custom assortments and/or small-sized products (e.g. airtime cards in small denominations) or pay-per-use services (e.g. minutes of shared mobile phone use) that match BOP consumers' limited, sporadic cash flows. Many companies using the Micro Distribution and Retail model also provide business skills training and other forms of support to help such retail outlets increase sales, recognizing the link between the outlet's business success and the company's own.

Experience-Based Customer Credit: Generates additional revenue in the form of interest income through lending to customers the company knows are credit-worthy through experience doing business with them in the past—rather than formal credit histories. The model is generally employed by companies outside the financial sector, though some may have credit arms or subsidiaries. Some companies focus on their direct customers. One company lends to its customers' customers as well, based on the experience its customers have had with those people in the past (and leveraging their existing relationships to help incentivize repayment). The model is predicated upon limited access to other sources of credit at similar rates or for similar purposes.

Last-Mile Grid Utilities: Extends grid coverage to more distant and often lower-income neighborhoods through a combination of financing, technology, and customer service innovations that help cover capital expenditures, minimize technical and commercial losses,

Continued on next page

and ensure customers pay on time. The model is based on a clear value proposition to the consumer: greater quality, reliability, convenience, and in many cases, lower cost compared to previously available, often informal utility options. *Complementary Model: Off-Grid Utilities*

Smallholder Procurement: Turning geographically dispersed smallholder farmers into reliable sources of quality supply through efficient aggregation methods and customized packages of support services that build capacity and loyalty. Common support services include agricultural extension, business development, access to agricultural inputs, and credit. Sometimes, buyers choose to focus on higher value crops capable of earning a premium in the marketplace to help cover the cost of such support. *Complementary Models: Smallholder Financing, Agricultural Market Information Systems for Smallholders*

Value-for-Money Degrees: Makes university education accessible to all through a combination of innovations that increase affordability and value for lower-income students. To increase affordability, these universities use standardized curricula that can be taught by part-time instructors, accessible physical and virtual campuses that reduce students' transportation costs, modular programming that matches cash flows, and access to student loan financing. To create value, they offer course content and career services tailored to the job market. *Complementary Model: Inclusive Student Financing*

Value-for-Money Housing: Makes home ownership possible for lower-income buyers through a combination of high value for money and facilitated access to mortgage financing. A home is the biggest investment most people ever make and they have to be convinced it is worth the commitment, which can feel risky. Value-for-money housing balances aspiration (with a focus on quality, special features, and the community environment) and affordability (with home sizes and layouts in different price ranges, and features that reduce the ongoing cost of ownership). Because the model hinges upon access to financing, it often involves helping homebuyers—often the first in their families—navigate the mortgage application process. *Complementary Model: Inclusive Mortgage Financing*

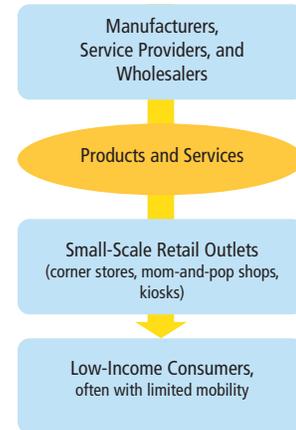
e-Transaction Platforms: Many low-income people lack access to financial services as a result of the high transaction costs and complex logistics involved in reaching them. Technology companies are beginning to address these challenges through electronic transaction platforms, creating opportunities to serve low-income customers and bringing them benefits spanning convenience, efficiency, security, market access, and integration into the formal financial system. IFC is investing in a diverse set of technology companies that are helping to create the complex infrastructure for a cashless society to function. These companies have different business models. However, at a fundamental level, they display some interesting similarities—like leveraging existing retail outlets and networks, building outlets' business and technology skills, raising consumer awareness and helping them understand the value proposition behind cashless transactions.

INCLUSIVE BUSINESS MODEL:

Micro Distribution and Retail

MODEL OVERVIEW

The **Micro Distribution and Retail** model reaches BOP end consumers who tend to make small, frequent purchases close to home by leveraging and effectively serving existing retail outlets in the neighborhoods where those consumers live. Such outlets are often small, with little space for excess inventory, and run by staff with little business training, scarce working capital, and no access to finance. They need small, frequent deliveries and the ability to buy on credit. They may need custom assortments and/or small-sized products (e.g., airtime cards in small denominations) or pay-per-use services (e.g., minutes of shared mobile phone use) that match BOP consumers' limited, sporadic cash flows. Many companies using the Micro Distribution and Retail model also provide business skills training and other forms of support to help such retail outlets increase sales, recognizing the link between the outlet's business success and the company's own. Within its portfolio, IFC has seen food and beverage, consumer products, and mobile telecommunications companies use this model.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing products and services BOP consumers want in formats that match their cash flows	Ensuring product accessibility at the BOP and maximizing the performance of the distribution channel		
Solutions		<p>5 Matching customers' cash flows</p> <ul style="list-style-type: none"> • Small package size • Shared access 	<p>1 Expanding reach</p> <ul style="list-style-type: none"> • Leveraging existing retail outlets • Employing specialized, independent distributors <p>2 Customized delivery</p> <ul style="list-style-type: none"> • Frequent, small drops • Custom assortments <p>3 Access to finance</p> <ul style="list-style-type: none"> • Inventory purchase on credit <p>4 Capacity-building</p> <ul style="list-style-type: none"> • Training • One-on-one coaching 		

1 Expanding reach: BOP consumers are often located in widely dispersed rural villages or geographically segregated urban slums, with mobility limited by the cost of transportation. Companies using the Micro Distribution and Retail model are reaching these consumers where they are, cost-effectively, by *leveraging existing retail outlets* rather than building their own retail chains. Existing retail outlets not only have the advantage of proximity; they also have existing relationships with local consumers and may even offer them credit. IFC client Dialog Telekom PLC, a mobile telecommunications network operator in Sri Lanka, distributes phone cards and SMS-based airtime top-ups through nearly 40,000 mostly small-scale retailers across the country.

The typical Dialog retailer operates a primary business, such as a grocery store, and stocks Dialog products among a range of others. IFC client Alquería, a dairy company, distributes UHT milk through 125,000 small-scale retailers in Colombia. Such retailers account for 75% of the company's sales, whereas supermarkets account for only 25%.

To reach small-scale retailers in the hardest-to-reach areas, including far-flung rural villages and crowded urban settings with narrow streets, companies using the Micro Distribution and Retail model often employ *independent distributors with specialized methods*. Alquería works with 690 such distributors. IFC client Coca-Cola Sabco, The Coca-Cola Company's East African bottler, works with 2,200.

- 2 Customized delivery:** Small-scale retail outlets serving the BOP have little storage space and limited working capital; it is simply not viable for them to have a lot of inventory on hand. As a result, the Micro Distribution and Retail model involves *frequent, small deliveries*. Coca-Cola Sabco's independent distributors might deliver a single case of product, or less, every day. Companies using this model may also deliver *custom assortments* of different products tailored to the needs of a particular store and its shoppers. For instance, IFC client MiTienda—a wholesale distributor in rural Mexico serving shops less than 10 square meters in size—sends agents out at least once a week to observe sales patterns and help customers order assortments that match demand. The company will deliver even single units of product.
- 3 Access to finance:** Because small-scale retailers have little working capital and limited or no access to financial services, the Micro Distribution and Retail model often relies on extended payment terms—allowing them to *purchase inventory on credit*. For example, MiTienda offers seven days. IFC client Moderna, a miller and marketer of wheat flour targeting small-scale bakeries in Ecuador, also offers seven days. Brazilian wholesaler Grupo Martins has been able to offer longer-term financing for store renovation by establishing a financial services subsidiary, IFC client Tribanco.
- 4 Capacity-building:** In the Micro Distribution and Retail model, sales growth happens in two ways. One is increasing the number of retail outlets in the network. The other is increasing the volume of sales at each outlet. As a result, the model almost always includes some form of capacity-building for outlet owners and staff, who have typically had little to no marketing, sales, inventory or cash management, or other business training. Such capacity-building can take different forms, including classroom or virtual *training* and *one-on-one coaching*. Leveraging a local-language version of IFC's SME Toolkit, Dialog has trained more than 5,100 retailers in Sri Lanka. Moderna in Ecuador has trained approximately 10,000 individuals at 5,000 bakeries not only in business skills, but also in fundamentals like self-esteem. Ten technical assistants follow up with one-on-one coaching through more than 400 client visits per month. Coca-Cola Sabco offers one-on-one coaching as well, at both the retailer and the independent distributor levels, through Resident Account Developers and Area Sales Managers on staff.

It is important to note that capacity-building helps small-scale retailers increase sales not only of a company's own products, but of all the products those retailers sell. The additional income helps to cement retailer loyalty—critical in markets where many companies are competing for shelf space.

- 5 Matching BOP consumers' cash flows:** The BOP consumers that small-scale retailers serve have low incomes that can also be lumpy and unpredictable. They often need to buy small amounts of product when they have the money. As a result, the products offered through the Micro Distribution and Retail model may come in *smaller package sizes* than one might see in larger supermarkets targeting consumers with greater disposable incomes, who can afford to have more of the equivalent of inventory on hand. Dialog, for example, along with Idea Cellular in India, Bharti in Madagascar, and other IFC clients in the mobile telecommunications sector, offers pre-paid airtime cards in very small denominations. Some products may even be offered as *shared access services*, which permit consumers to “pay as they go.” Bharti, which has taken over from Zain in Madagascar, offers shared phone service for those unable to afford their own handsets through existing retail outlets that are part of the Village Phone Program.

EXTERNAL SUCCESS FACTORS

Fragmented retail landscape: The Micro Distribution and Retail model applies in fragmented retail markets characterized by large numbers of small outlets. The dense, urban slums and sparsely populated rural areas where the BOP tend to live are often not conducive to “big box” retail. And in some places, consumers simply prefer small shops. They may value the relationships they have there, or the store owner's willingness to let them pay next week. Where larger and smaller retail formats co-exist, it is important for companies to understand what kinds of products are flowing through what kinds of channels, and why.

High levels of product literacy: The Micro Distribution and Retail model works best where people are already familiar with the product or service category, know how it works, and why it is valuable to them. Micro distributors and retailers earn thin margins, and cannot be expected to spend too much time educating customers about products and services that are new, complex, and difficult to understand.

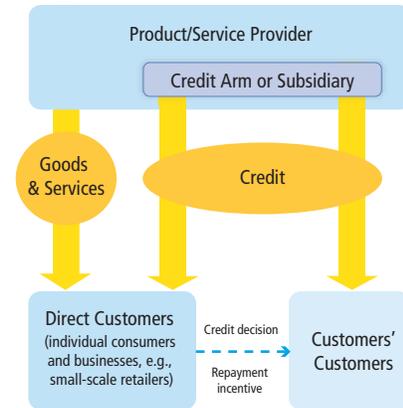


INCLUSIVE BUSINESS MODEL:

Experience-Based Customer Credit

MODEL OVERVIEW

The Experience-Based Customer Credit model generates additional revenue in the form of interest income through lending to customers the company knows are creditworthy through experience doing business with them in the past—rather than formal credit histories. The model is generally employed by companies outside the financial sector, though some may have credit arms or subsidiaries. Some companies focus on their direct customers. One company lends to its customers’ customers as well, based on the experience its customers have had with those people in the past (and leveraging their existing relationships to help incentivize repayment). The model is predicated upon limited access to other sources of credit at similar rates or for similar purposes.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Expanding the product offering for the BOP market	Ensuring accessibility to creditworthy borrowers while minimizing distribution costs	Enhancing borrowers’ willingness to pay	
Solutions		<ol style="list-style-type: none"> Reducing cost <ul style="list-style-type: none"> Leveraging existing customer knowledge Standardization 	<ol style="list-style-type: none"> Expanding reach <ul style="list-style-type: none"> Leveraging established retail networks Capacity-building <ul style="list-style-type: none"> Training One-on-one coaching 	<ol style="list-style-type: none"> Increasing collection rates <ul style="list-style-type: none"> Payment incentives Business training 	

1 Reducing cost: In the process of doing business, companies large and small develop valuable knowledge of customers’ purchasing and payment habits, particularly if they allow customers to buy on credit. Through the Experience-Based Customer Credit model, companies *leverage existing customer knowledge* to offer credit for other uses to those with a history of paying on time. Most companies using this model leverage their own customer knowledge. IFC client Promigas, a natural gas utility in Colombia, used knowledge of which households had paid off their connection fees to extend credit for home improvements and appliances. Grupo Martins, a wholesale distributor in Brazil, used knowledge of which retailers honored their extended payment terms to extend credit for store renovations through a financial subsidiary, IFC client Tribanco. Tribanco took the model a step further, leveraging retailers’ knowledge of their own customers to offer consumer credit, too. For a monthly fee,

Tribanco lets retailers issue store credit cards to customers they have found to be creditworthy.

Companies using the Experience-Based Customer Credit model reduce the cost of service even further through *standardization*. For example, Promigas has a very simple list of requirements that, if met, qualify a borrower for pre-approval.

2 Expanding reach: BOP customers are often geographically dispersed or isolated from large, mainstream retail channels. But because the Experience-Based Customer Credit model targets existing customers with an additional product, companies’ *established retail networks* can be used.

3 Capacity-building: Existing networks need *training* to use existing customer knowledge to offer what is often a very new service: credit. These networks may have been set up to sell utility services, groceries, or consumer goods. To offer

consumer credit cards through its network of customers—small-scale retailers—Tribanco sends trained loan officers to provide them with *one-on-one coaching* on the credit card product, their lending practices, and the financial system at large.

- ④ **Increasing collection rates:** The customer knowledge on which credit decisions in this model are based come from existing relationships which offer built-in *payment incentives* for borrowers. Borrowers don't want to jeopardize those relationships because they still need access to the original product or service that brought them to do business with the company. For example, Tribanco's credit cardholders pay because they want to continue to shop at their local neighborhood stores. Tribanco strengthens these incentives by offering store owners discounted monthly fees if the default rates among their cardholders are low. Where borrowers are businesses, rather than individuals, it may make sense for companies to provide business training as well. If those businesses increase their turnover, they are not only more likely to repay their loans, but also to buy more of the company's original product or service.

EXTERNAL SUCCESS FACTORS

Unmet demand for credit: The Experience-Based Customer Credit model responds to a demand for credit that often goes unfilled either by the mainstream commercial banking sector (focused on larger loans to borrowers with formal credit histories and traditional forms of collateral) or by microfinance institutions (focused on loans for "productive purposes"). Many low-income people need credit on more flexible terms simply to smooth out irregular cash flows. Companies offering Experience-Based Customer Credit address this need, though they have tended to limit the range of products and stores for which credit can be used—whether to stimulate their core business, limit risk, or target social impact.

Regulation: Whether a company can transition from offering extended payment terms to offering credit depends on regulation. In many countries, it is not easy to do without establishing a financial subsidiary, as Grupo Martins has done in Brazil. It can also help if the country has a "positive list" as part of the credit rating system, giving consumers points for having made utility payments on time, for example. Many countries have "negative lists" only, which means customers who pay on time do not appear on any list.

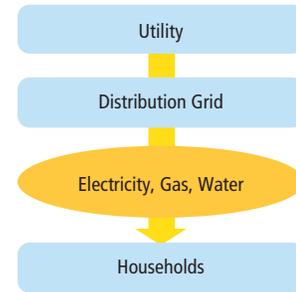


INCLUSIVE BUSINESS MODEL:

Last-Mile Grid Utilities

MODEL OVERVIEW

The **Last-Mile Grid Utilities** model extends grid coverage to more distant and often lower-income neighborhoods through a combination of financing, technology, and customer service innovations that help cover capital expenditures, minimize technical and commercial losses, and ensure customers pay on time. The model is based on a clear value proposition to the consumer: greater quality, reliability, convenience, and in many cases, lower cost compared to previously available, often informal utility options.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing a high-value, low-cost offer	Financing grid expansion and minimizing distribution costs	Enhancing willingness and ability to pay	Strengthening the value proposition and retaining customers
Solutions		<ol style="list-style-type: none"> Adding value <ul style="list-style-type: none"> High quality 	<ol style="list-style-type: none"> Reducing cost <ul style="list-style-type: none"> Efficient distribution technology Public funding 	<ol style="list-style-type: none"> Communicating value <ul style="list-style-type: none"> Customer awareness-raising Increasing collection rates <ul style="list-style-type: none"> Smart metering Sense of ownership Leveraging existing retail outlets Payment incentives Affordable pricing <ul style="list-style-type: none"> Tiered pricing Public funding Access to finance <ul style="list-style-type: none"> Household connection on credit 	<ol style="list-style-type: none"> After-sales support <ul style="list-style-type: none"> Maintenance and repair

1 Adding value: Grid-based water and electricity services are *high quality* compared to alternative sources that low-income households have access to, including water tankers, kerosene, and illegal grid connections. For example, water is clean and does not cause disease; voltage is regulated and does not cause fires that put lives at risk or burn out appliances. Being available in the home, grid-based services are also more convenient, saving customers the time it would have taken to travel to the nearest retail outlet. Even without taking quality or convenience into account, many alternative sources of water and energy are very expensive simply because they are informal, unregulated, and vulnerable to corrupt or exploitative business practices.

2 Communicating value: Whether water, electricity, or natural gas, grid utilities may be new to low-income households. They may have concerns about affordability, meter reliability, or even safety, as in the case of natural gas. In some cases, they may not feel they should have to pay—believing the utility should be a public service. The Last-Mile Grid Utilities

model involves significant *customer awareness-raising* around the value of household-level grid utility service, why it is important to pay, and how it can be affordable. Along with traditional media like television and radio, IFC client AAA—a water utility in Barranquilla, Colombia—employed more than 40 full-time social workers familiar with low-income neighborhoods to build community awareness and acceptance.

3 Increasing collection rates: To help keep service charges low, bill collection rates must be high throughout the system. The Last-Mile Grid Utilities model includes special effort on this front, even among higher-income households, particularly where a culture and history of paying for utilities has to be developed. Companies use various tactics, some technological (like *smart metering*) and some social (like building a *sense of ownership* of the system within the local community). To reduce incentives to tamper with meters or miss payments, Manila Water has built a sense of ownership by involving local communities in the design,

implementation, and maintenance of the system and by hiring community members to manage billing and collection. Companies also **leverage existing retail outlets** such as grocery stores and pawnshops to create convenient payment points and offer positive **payment incentives**. For example, AAA recognizes on-time payers as “super clients” and provides them with discounts at neighborhood stores as well as thank-you letters from the CEO, which have helped them get credit in the absence of formal credit histories.

- 4 **Reducing cost:** Because low-income households have limited ability to pay for service, the Last-Mile Grid Utilities model relies on **efficient distribution infrastructure and technology** to reduce cost throughout the system. Examples include energy-efficient water pumps that reduce electricity consumption; remote monitoring to identify illegal connections and leaks so they can be fixed right away; and better voltage-regulating equipment.

Sometimes, though, efficiency is not enough. The cost of building last-mile grid infrastructure in the very dense, often peripheral urban communities and isolated rural regions where low-income households are found can be too high to recoup without raising rates beyond what those households could afford. When necessary—for example, to meet coverage targets stipulated in their concession agreements—companies can take advantage of public-private partnerships. **Public funding** can be offered outright or on an output basis, where companies receive the money once pre-agreed targets are met. IFC client CEMAR, in the low-income Brazilian state of Maranhão, received public funding for a significant portion of the cost of building last-mile electrical infrastructure under a federal government program to electrify the rural poor. IFC client Manila Water, in the Philippines, received output-based aid enabling it to reduce the household connection cost for the most marginalized consumers by nearly 80%.

- 5 **Affordable pricing:** Low-income households may not be able to pay full cost-recovery rates even for highly efficient systems. While utilities tend to be highly regulated, in many countries companies are permitted to adopt **tiered pricing** structures in which industrial users and/or higher-income households pay higher rates to cross-subsidize lower-income households—enabling the Last-Mile Grid Utilities model to stay viable. IFC client Calidda, for example—a natural gas

company in Peru—charges industrial users more. **Public funding** can also be used to help companies reach lower-income households than it would be commercially viable to reach at standard tariff levels. Such funding can be used to subsidize the lowest-income households directly or to compensate operators for charging below cost-recovery rates.

- 6 **Access to finance:** Low-income households are generally unable to pay large lump sums to connect to the grid, so some companies **provide connections on credit**, letting them pay in installments over time. IFC client Promigas, a natural gas utility in Colombia, connected nearly two million households this way.
- 7 **After-sales support:** A final solution the Last-Mile Grid Utilities model employs—reinforcing customers’ willingness to pay, and enhancing the value proposition overall—is timely **maintenance and repair**. Companies may use technology to increase efficiency. AAA allows customers to report problems by mobile phone, and dispatches service personnel via a central computer system.

EXTERNAL SUCCESS FACTORS

Regulatory environment conducive to private sector investment:

The government plays a critical role in the success of the Last-Mile Grid Utilities model. First of all, the model is only relevant in places where private sector players are permitted to provide what are often considered public services. Because utilities are highly regulated, the specific conditions under which they are permitted to operate also matter. The regulator must strike a balance between rules that incentivize the operator to invest and rules that ensure service coverage and compliance with performance standards. Regulated tariff levels must be set both to cover the operator’s investment and be affordable to the consumer.

Availability of public support to reach the poorest: Given the fundamental importance of the services they provide, utilities are often required—whether by regulation or by stakeholder pressure—to reach even the poorest households, which cannot pay even for very low-cost service. In these cases, the availability of public funding becomes a critical success factor. Such public funding can include grants and low-interest loans for building out last-mile infrastructure, output-based aid and direct end user subsidies to help defray consumers’ monthly bills.



OFF-GRID UTILITIES

While the Last-Mile Grid Utilities model is more common within the IFC portfolio, IFC is beginning to see promising off-grid utilities emerge. These village-level systems provide safe, affordable water and electricity in places it is uneconomical to reach through the grid—using small-scale, distributed purification and generation technology; local operating partners; and customer education and engagement to generate demand and ensure on-time payment. For example:

- **Manila Water** in the Philippines is experimenting with stand-alone water systems that provide communities outside its network area with clean, affordable water. Partners, usually local governments, operate these systems and customers pay their bills at local shops—with the balances transferred to the company via mobile banking.
- **WaterHealth International** in India develops and markets proprietary, decentralized water purification and disinfection systems that provide affordable

potable water in off-grid communities. Local communities operate and eventually own the systems, once they have paid off the capital cost.

- **Husk Power**, also in India, builds 35-50 kilowatt power plants that run entirely on rice husks, generating electricity through biomass gasification, and connect households using simple distribution micro-grids of insulated wire strung from bamboo poles. While Husk operates some of the systems, it transfers many to local entrepreneurs and stays involved to provide training and maintenance.

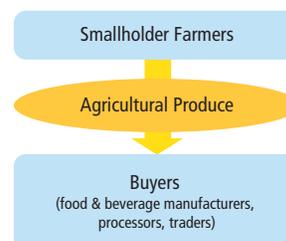
These businesses are new and rapidly evolving; IFC's investments in Husk and WaterHealth are among the earliest stage investments in the portfolio. The technological innovations involved are promising and absolutely fundamental. Further business model innovation will be equally fundamental as these young firms reach toward financial sustainability and scale.

INCLUSIVE BUSINESS MODEL:

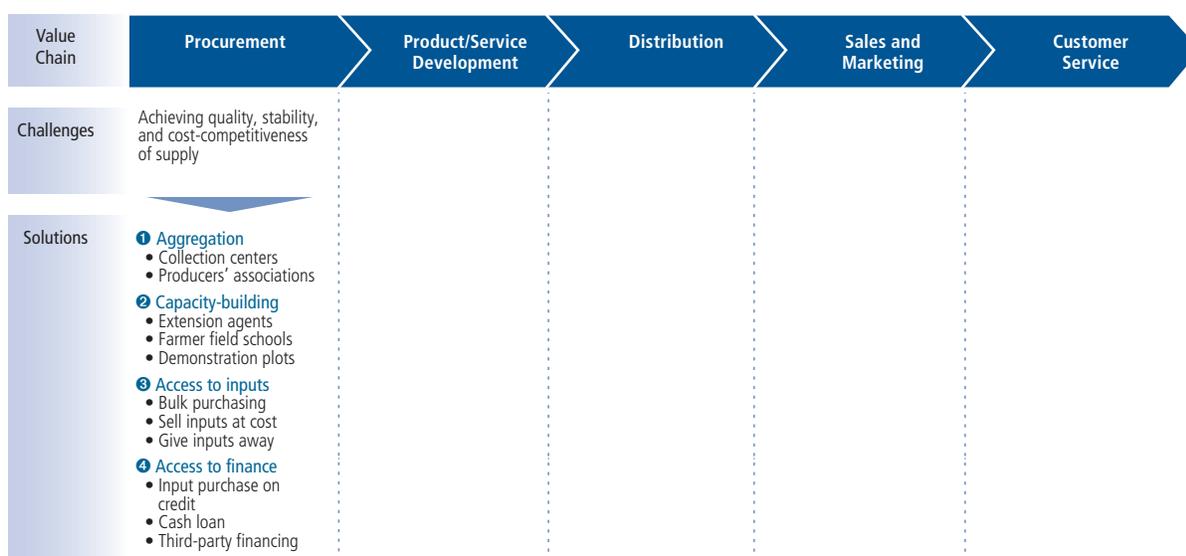
Smallholder Procurement

MODEL OVERVIEW

The **Smallholder Procurement** model turns geographically dispersed smallholder farmers into reliable sources of quality supply through efficient aggregation methods and customized packages of support services that build capacity and loyalty. Common support services include agricultural extension, business development, access to agricultural inputs, and credit. Sometimes, buyers choose to focus on higher value crops capable of earning a premium in the marketplace to help cover the cost of such support.



CHALLENGES AND SOLUTIONS



1 Aggregation: Smallholder farmers are widely geographically dispersed in many markets, where transportation infrastructure can be poor. They also produce small volumes. As a result, the Smallholder Procurement model involves various methods of aggregation to reduce the transaction costs involved. Some buyers use *collection centers*. IFC client Salala Rubber in Liberia uses 14 remote buying stations owned by independent third-party agents who buy on the company's behalf for a commission. Other buyers source from *producers' associations*, like cooperatives, and other intermediaries rather than individual farmers. IFC client Alquería, a dairy producer in Colombia, sources approximately 42% of its milk supplies from more than 5,500 small-scale dairy farmers this way.

2 Capacity-building: Smallholder farmers face a range of constraints, one of which tends to be limited knowledge of the latest and most effective agricultural techniques. Often,

they do things the same way their families have done for generations. Because agricultural buyers need consistent, high-quality supplies, those using the Smallholder Procurement model must build farmers' capacity to produce them—whether through *extension agents* or *farmer field schools*, often utilizing *demonstration plots* to help convince farmers to implement what they learn. Most of the buyers in IFC's portfolio have their own technical assistance staff, but some use partners in addition. IFC client ECOM, a global commodity trader, partnered with the US-based non-governmental organization Rainforest Alliance and French agricultural research center CIRAD to provide coffee farmers in Central America with training to improve productivity, environmental sustainability, and eligibility for product certification. Sometimes, capacity-building spans not only agricultural skills but also the business skills required to transform smallholder farming from a subsistence activity into a viable commercial enterprise.

- ③ **Access to inputs:** Underdeveloped agricultural input markets are another constraint smallholder farmers face. Buyers must often provide or facilitate more affordable access to inputs to make the Smallholder Procurement model work. They may do this through *bulk purchasing*, passing along savings smallholders would be unable to capture on their own, as in the case of Alquería. They may *sell inputs at cost*, as in the case of Salala. They may even find it a strategic investment to *give inputs away*, especially where particular inputs are critical to the nature or quality of product they expect to procure. Salala gives away rubber tree stumps to smallholders ready to replant their farms.
- ④ **Access to finance:** Smallholder farmers generally lack financial reserves they can use as working capital to buy seeds and other inputs, hire laborers, and get their produce to market at the harvest before they ultimately get paid. Access to finance is critical, but because agriculture is notoriously risky and smallholders have little to no collateral, banks tend to shy away. As a result, buyers engaged in Smallholder Procurement must fill this need too. Some offer *input sales on credit* and some, like ECOM and Salala, will actually provide *cash loans* to farmers they know and whose production potential they have thoroughly assessed. Other buyers provide farmers with contracts they can take to the bank, facilitating access to *third-party financing*—though this is relatively rare within IFC’s portfolio. IFC client Jain Irrigation, an irrigation equipment manufacturer and agricultural processor in India, contracts with 4,150 relatively progressive farmers that have shown themselves to be receptive to improved growing practices.

EXTERNAL SUCCESS FACTORS

Comparative advantage of smallholder farmers:

Smallholder Procurement is a resource-intensive model. To be a good choice, it must give companies a comparative advantage—or at least, not put them at a comparative disadvantage. For example, in some markets, companies have no choice but to source from smallholders. Smallholders may be the predominant source of supply for historical or regulatory reasons, for example. Alternatively, crop dynamics may favor small-scale production.

Availability of specialized private sector service providers:

That many buyers engaged in Smallholder Procurement are providing support services like information, technical assistance, and financing themselves—and doing it viably—suggests that there could be business opportunities for specialized private sector providers. Some might target large buyers as customers (of agricultural management information systems, for instance) while others might target individual farmers and farmers’ groups (with financial services, for example). A few such companies can already be observed within IFC’s portfolio (see boxes on page 23).

Availability of cost-sharing partners:

Smallholder Procurement is resource-intensive, but with large rural populations earning their primary livelihoods in agriculture, it has enormous development potential—increased productivity and quality, better market linkages, and higher incomes translate into improved standards of living and greater opportunities for future generations. As a result, in many countries there are donor facilities and programs available to help support smallholders. These programs are increasingly looking to involve large, anchor buyers and can be a source of savings for companies, provided they are market-based and that the transaction costs of participation are sufficiently low.



SMALLHOLDER FINANCING

To be reliable sources of quality supply, smallholder farmers need access to working capital and financing for farm equipment and other capital investments. Yet farming is notoriously risky and agricultural financing can be difficult if not impossible to obtain. As a result, many companies engaged in Smallholder Procurement provide some form of financing themselves—whether it be outright loans or the ability to purchase necessary inputs on credit. Nevertheless, some banks are beginning to venture into the smallholder financing space, often in partnership with donors and other investors willing to share the risk. For example, IFC client Nib International Bank in Ethiopia is leveraging an IFC partial credit guarantee to provide working capital loans to cooperatives of smallholder farmers marketing high-quality, washed coffee. Aggregation to reduce transaction costs—for example, through cooperatives and other farmers' groups—is critical, as is farmers' ability to produce a value-added crop capable of commanding a price high enough both to repay the loan and still leave the farmer better off.

AGRICULTURAL MARKET INFORMATION SYSTEMS FOR SMALLHOLDERS

Efficient agricultural markets depend on timely, accurate information flows. Yet in too many developing countries, smallholder farmers have limited insight into which commodities are in demand, where, in what volumes or at what prices. For their part, buyers may have little visibility into what is available, where, when, or at what level of quality without frequent visits to the field—which can be very time-consuming as a result of distance and poor transportation infrastructure. Their cheapest and most reliable option may be to focus on large domestic suppliers and imports.

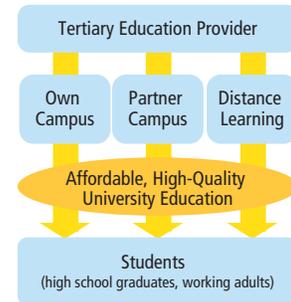
Within the development community, there have been several attempts to take advantage of rapidly increasing mobile phone penetration to narrow the information gap. Most of these donor-driven efforts have been costly and experienced limited take-up. More recently, a number of private sector providers have begun to experiment with market-based, more user-driven approaches. For example, IFC client Esoko in Africa is licensing and developing custom applications of a market information system individual farmers, cooperatives and farmers' associations, government extension providers, commodity traders, and buyers can use to exchange buy and sell offers, agricultural input and crop prices, growing advice, stock counts and locations where seeds and fertilizers are available—all via the Internet and mobile phone. It is relatively early days for Esoko and companies like it, and the business model is still evolving. The model has great potential to help turn smallholder farmers into reliable sources of quality supply for larger traders, processors, and food and beverage manufacturers—enabling those farmers to move from subsistence to commercial agricultural activity.

INCLUSIVE BUSINESS MODEL:

Value-for-Money Degrees

MODEL OVERVIEW

The **Value-for-Money Degrees** model makes university education accessible to all through a combination of innovations that increase affordability and value for lower-income students. To increase affordability, these universities use standardized curricula that can be taught by part-time instructors, accessible physical and virtual campuses that reduce students' transportation costs, modular programming that matches cash flows, and access to student loan financing. To create value, they offer course content and career services tailored to the job market.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing a high-value, low-cost offer	Ensuring accessibility while minimizing distribution costs	Enhancing willingness and ability to pay	Strengthening the value proposition, retaining customers, and fueling positive word of mouth
Solutions		<ol style="list-style-type: none"> 1 Adding value <ul style="list-style-type: none"> • Income generating potential • High quality • Accreditation 2 Reducing cost <ul style="list-style-type: none"> • Standardization • Bulk purchasing 3 Matching customers' cash flows <ul style="list-style-type: none"> • Modular product 	<ol style="list-style-type: none"> 3 Expanding reach <ul style="list-style-type: none"> • Evening hours • Convenient locations • Virtual distribution 	<ol style="list-style-type: none"> 4 Communicating value <ul style="list-style-type: none"> • Word of mouth 5 Access to finance <ul style="list-style-type: none"> • Third-party financing • Purchase on credit 	<ol style="list-style-type: none"> 7 After-sales support <ul style="list-style-type: none"> • Career services

1 Adding value: The cost of higher education can be a significant proportion of the student's—or his or her family's—income, requiring significant lifestyle change to accommodate in the household budget. The Value-for-Money Degrees model targets many students who are the first in their families to receive a higher education, and they have to believe it is worth the investment. Specifically, they have to believe it offers *income generating potential*—that they will obtain higher-paid jobs after they graduate. Curricula are designed and continuously adjusted to prepare graduates for the demands of the local job market, sometimes in consultation with large firms and trade organizations. Courses are often taught by working professionals who bring practical knowledge and job connections. *High quality* is important, and many universities offering Value-for-Money Degrees seek official government *accreditation* as a signaling device. IFC client Duoc UC, for example, has received the maximum seven-year accreditation from the Chilean National Accreditation Commission.

2 Reducing cost: On the money side of the value for money equation, it is important to reduce the cost of higher education as much as possible to match students' and their families' ability to pay. Universities offering Value-for-Money Degrees keep staff costs down through *standardized curricula* that allow working professionals to teach part-time by reducing the amount of time they have to spend preparing for class in order to achieve the required level of quality. *Bulk purchasing* saves students on school supplies. As its student numbers grew, IFC client Anhanguera in Brazil was able to negotiate lower prices on the books used in its courses. The company has now reached a scale where it can publish and sell books to students more cheaply on its own.

3 Expanding reach: Low-income students often have limited mobility and work full- or part-time. Education has to be accessible in terms of location and schedule. As a result, the Value-for-Money Degrees model uses *evening hours*, *conveniently-located campuses* where students live and work (or can quickly and easily travel by public transportation), and *virtual distribution*, or online learning.

Anhanguera educates about 650,000 students a year in physical locations and another 100,000 or more online. IFC client Uniminuto, in Colombia, is working with international partners—like Mexico’s Tecnológico de Monterrey—to expand its online offering.

- 4 **Communicating the value:** While low-income people recognize the value of higher education in terms of securing higher-paying jobs in the future, the prospect of making such a big financial commitment now can be hard for those without consistent cash flows or significant savings to fall back on. *Word of mouth* from current or former students is a powerful way of reassuring prospective students and unlocking pent-up demand. Uniminuto actively facilitates word of mouth through regular open houses where this exchange can occur.
- 5 **Matching customers’ cash flows:** Recognizing that lower-income students’ cash flows can be more sporadic, universities may offer *modular programming* that allows students to earn their degrees one course at a time—exiting when necessary with certificates that are valuable in the job market and can be built upon when they have the money to return to school.
- 6 **Access to finance:** Low-income students and their families cannot afford to pay outright for an investment as big as an education. The Value-for-Money Degrees model depends on student access to *third-party financing* from the government or the private sector. IFC client Maurício de Nassau in northeast Brazil, for example, works with the government’s PROUNI and FIES student loan programs. One hundred and seventy-five Brazilian universities work with IFC client Ideal Invest (see box on page 26). Where outside options are not sufficient, universities like Uniminuto allow students to *purchase on credit* through their own financing subsidiaries.
- 7 **After-sales support:** Further strengthening the value proposition of Value-for-Money Degrees is the customer service provided by university *career services* departments. Duoc UC has a job portal, leverages professors, and offers students ongoing opportunities for interaction with industry through internships, contests, conferences, and collaborative projects to enable students to secure jobs upon graduation. Such career services are very important in fueling word of mouth, building brand image, and motivating students to invest now for better futures.



EXTERNAL SUCCESS FACTORS

Job market demand for professional skills: The Value-for-Money Degrees model works best in markets where there is high demand for skilled labor and insufficient supply. Students will not invest if they do not believe they will be able to earn more money once they graduate.

Large volumes of high school graduates: While this model can start small, it is most successful when it achieves scale. Regions with large numbers of high school graduates qualified for tertiary studies—perhaps as a result of government investment in primary and secondary education in the past—are good candidates for this model. India, China, Indonesia, the Philippines, and Egypt are examples.

Availability of student financing and scholarships: Given the level of investment involved, the Value-for-Money Degrees model is most successful where student financing is available—whether through government or the private sector. This is one reason IFC’s current Value-for-Money Degree clients come from Brazil, Chile, and Colombia where subsidized state loan programs, scholarships, and private sector providers are present.

Availability of long-term corporate financing: Investing in new campuses, building a student body, and expanding corporate reputation takes time. In IFC’s experience supporting this model, four to five years are required for a campus to become financially self-sustaining. That means a company needs affordable, long-term financing to stay the course.

Regulatory support for private universities: Strong and transparent regulation can help grow the market for Value-for-Money Degrees. Countries must be open to private sector provision, first of all, and must simplify the process through easy-to-navigate bureaucracy. Good regulators also develop recognized quality criteria. Chile, for example, has a National Accreditation Commission that enables providers to strive for high ratings in order to improve their value proposition vis-à-vis their competitors. Accreditation helps students know how to value their investments, and frees providers to focus on content quality rather than marketing.

INCLUSIVE STUDENT FINANCING

Student financing is critical to the growth of the Value-for-Money Degrees model. While some governments offer student loan programs, private sector lenders are also beginning to develop the market opportunity. IFC client Ideal Invest, in Brazil, is one example. Since 2006, the company has financed over 17,000 students' higher educations. Its current portfolio is more than \$65 million.

Financial institutions reduce the risk involved in student lending through a number of different mechanisms, including partnering with particular universities whose graduates they believe will have good repayment prospects, and lending incrementally—one semester's loan at a time. Partner universities may also help make loans more affordable to even lower-income students by covering part of the interest, in return for the lenders' role in bringing in new students. One challenge is to persuade prospective borrowers that higher education is a wise investment. In this respect, student lenders are as dependent on universities offering Value-for-Money Degrees as those universities are on them.

INCLUSIVE BUSINESS MODEL:

Value-for-Money Housing

MODEL OVERVIEW

The **Value-for-Money Housing** model makes home ownership possible for lower-income buyers through a combination of high value for money and facilitated access to mortgage financing. A home is the biggest investment most people ever make and they have to be convinced it is worth the commitment, which can feel risky. Value-for-Money Housing balances aspiration (with a focus on quality, special features, and the community environment) and affordability (with home sizes and layouts in different price ranges, and features that reduce the ongoing cost of ownership). Because the model hinges upon access to financing, it often involves helping homebuyers—often the first in their families—navigate the mortgage application process.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing a high-value, low-cost offer		Ensuring ability to pay	Strengthening the value proposition, retaining customers, and fueling positive word of mouth
Solutions		<ol style="list-style-type: none"> 1 Adding value <ul style="list-style-type: none"> • High quality • Bundled product 2 Reducing cost <ul style="list-style-type: none"> • Low-cost design • Energy efficiency 		<ol style="list-style-type: none"> 3 Access to finance <ul style="list-style-type: none"> • Third-party financing 	<ol style="list-style-type: none"> 4 After-sales support <ul style="list-style-type: none"> • Customer education and training • Resale support

1 Adding value: A home is the biggest investment most people will ever make. It can feel risky, especially when one's income is low and potentially uncertain. High value for money is what makes it worthwhile. The Value-for-Money Housing model centers upon a **high quality** product that appeals to the homebuyer's aspirations with a focus on location, attractive design, and special features like Internet access or security systems. It comes with legal property title, a big advantage for buyers who may have been living at risk of eviction, and unable to use their homes as collateral, in informal settlements. Moreover, Value-for-Money Housing is often a **bundled product** comprising not just a house, but a community—including shared facilities like parks, courtyards, and community centers.

2 Reducing cost: On the other side of the value for money equation, homes must be low-cost—not only to purchase, but also to own and live in over time. This can be accomplished through a combination of **low-cost home design** and **energy efficiency**. For example, many Value-for-Money Housing developers offer homes starting at a minimum functional size, with layouts geared to make the most of limited space, often within multi-unit buildings so costs like land and trunk infrastructure connections can be

shared among multiple buyers. IFC client VINTE, a Mexican developer, offers units beginning at \$23,000 for 450 square feet, including a kitchen, living-dining area, two bedrooms and one bathroom, in multi-unit buildings. VINTE homes are also designed to reduce gas bills by 75%, and optional rooftop solar cells can reduce electricity bills as well. Striking the right balance between aspiration and affordability is especially important for younger developers in this relatively new business model, who are yet to build a name and reputation and may not have the capabilities or pockets of larger, more established firms.

3 Access to finance: Even with attention to affordability, the magnitude of the investment in a home typically requires financing. For most low-income homebuyers, their mortgage will be the biggest and longest-term loan they have ever taken on. They may be coming from informal settlements, the first in their families to own a home and the first to experience the mortgage process. They may not even have bank accounts. For someone with a low income, who may not be sure about his or her long-term job prospects, the prospect of a mortgage is daunting—and so is the process of getting one. The Value-for-Money Housing model relies on homebuyers' **access to third-party mortgage**

financing, and often facilitates it through customer education and hands-on assistance with the application process. VINTE, for example, helps customers gather and file all the needed documents.

- 4 **After-sales support:** As first-time homeowners, often the first in their families, Value-for-Money Housing customers may not know how to maintain a house to maximize resale value. They may never have participated in community associations or had to abide by community rules and regulations intended to boost the asset values of all the homes within them. To help customers get the most out of their investments, the Value-for-Money Housing model involves **customer education and training** in these areas and efforts to foster a shared sense of ownership over common spaces, which discourages vandalism and enhances security.

Just as it will be many Value-for-Money Housing customers' first time buying a home, it will be their first time selling a home when the time comes. It is in the builder's best interest that homes be resold for good prices, so they acquire a reputation for being good investments. It is also in the builder's best interest that homes be sold to buyers who will be responsible members of the community, since safe, well-maintained communities are critical to builders' brand image. For these reasons, the Value-for-Money Housing model involves **resale support**—for example, putting a home on the market for a fee. Resale support also contributes to customer loyalty, strengthening the up-sell opportunity for builders with bigger, higher-priced homes on offer.

EXTERNAL SUCCESS FACTORS

Availability of large-scale, long-term corporate financing:

For housing developers, profitability hinges on the economies of scale associated with large developments. Large developments require large amounts of capital up front to acquire land and build homes, and it may be several years before all those homes are sold. In some countries, governments help developers address this challenge by contributing land on the condition that certain percentages of homes be sold or given to the government to transfer to low-income families. Real estate sales are also sensitive to slumps in the economy, and developers must have enough financial reserves to withstand periods of low customer demand.

Availability of mortgage financing: Mortgage financing is a critical enabler of demand for housing, and unfortunately

a critical gap in many countries—especially for low-income people who have limited access to the formal financial sector at all. Countries like Brazil, Mexico, South Africa, India, the Philippines, and Turkey either have or are developing mortgage programs for low-income homebuyers. In some countries, the private sector is beginning to step in (see box below).

Availability of land: If developments are located too far from prospective buyers' jobs, schools, families, and friends, they will stay in low-quality housing for the convenience, time and transportation cost savings, and presence of social support networks. Location is a critical part of any successful project strategy and in some metropolitan areas, availability of land—at a price lower-income homebuyers will be able to afford—is a real challenge.

INCLUSIVE MORTGAGE FINANCING

The Value-for-Money Housing model depends on the availability of mortgage financing for low-income homebuyers. Yet in many countries, mortgages are only available to the wealthy, or there is a gap between private mortgages available to the wealthy and public subsidies available to the very poor. As discussed above, some countries are developing mortgage programs that begin to fill this gap. And in some places, the private sector is coming in. IFC is beginning to see a few such companies within its portfolio. IFC client La Hipotecaria, for example, has issued nearly 20,000 mortgages to lower- and lower middle-income borrowers in Panama and El Salvador.

To serve low-income borrowers successfully, private sector mortgage companies rely heavily on standardized loan origination, approval, and servicing processes made even more efficient through the use of technology. They ensure collection rates remain high through measures to increase convenience—making it possible to pay at supermarkets or through money transfer services, for example—or even make payment automatic, through payroll deduction. Finally, in some countries, they take advantage of government incentives to make mortgages affordable to even lower-income borrowers. In Panama, for example, the government offers tax credits to mortgage companies offering subsidized rates.



INCLUSIVE BUSINESS MODEL:

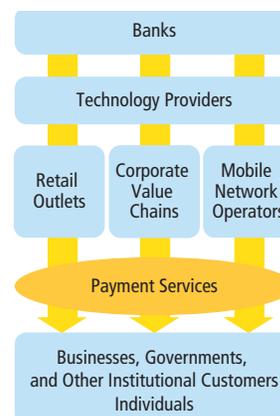
e-Transaction Platforms

MODEL OVERVIEW

Approximately 3.5 billion people worldwide lack access to financial services. A major reason is that financial institutions face high transaction costs and complex logistics to reach the poor, especially in remote areas, due to the cumbersome nature of securely transporting and distributing cash. These challenges are shared by providers of other goods and services that require distribution infrastructure and payment mechanisms to transact with the poor. However, electronic transaction platforms are beginning to address these challenges, creating opportunities to serve low-income customers and move them toward a cashless society. Cashless transactions bring these customers benefits spanning convenience, efficiency, security, access, and integration into the formal financial system.

IFC is investing in a diverse set of technology companies that are helping to create the complex infrastructure for a cashless society to function. For example, YellowPepper offers mobile phone-based “electronic wallets” for unbanked customers to pay for goods and services; Suidhaa offers the means to electronically purchase virtual goods like train tickets or airtime through over 40, 000 retail outlets; and FINO offers, among other services, biometric smart card-based electronic wallets for 23 million customers to receive and spend social benefits distributed by the government of India.

These companies have different business models. However, at a fundamental level, they display some interesting similarities. These similarities are summarized below.



CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing a high-value, low-cost offer	Ensuring product accessibility while minimizing distribution costs	Ensuring willingness and ability to pay	Strengthening the value proposition, retaining customers, and fueling positive word of mouth
Solutions		1 Adding value and reducing cost <ul style="list-style-type: none"> Technology 	2 Expanding reach <ul style="list-style-type: none"> Leveraging established retail networks Leveraging existing retail outlets Leveraging existing constituent networks 3 Capacity-building <ul style="list-style-type: none"> Training One-on-one coaching 	4 Communicating value <ul style="list-style-type: none"> Key message Incentives Customer awareness-raising 	5 After-sales support <ul style="list-style-type: none"> Continuous access to cash

1 Adding value and reducing cost: The e-Transaction Platforms model uses *technology* to provide unbanked and under-banked customers with the means to use money in electronic form, a convenient, low-cost, secure, and transparent alternative to cash. Electronic or e-money technology includes front-end devices like mobile phones, smart cards, and point-of-sale terminals used to access stores of e-money, as well as back-end switching and processing infrastructure that moves e-money and keeps records. With electronic transactions, individual customers save time (previously spent traveling great distances or waiting in long lines) and money (in the form of travel costs and forgone

wages). They are also less vulnerable to robbery and corruption. For institutional customers like banks and businesses, e-transaction platforms reduce the cost of serving low-income customers because shared technology platforms, distribution channels, and even brands offer economies of scale.

This, in turn, expands consumer choice, offering access to products and services that can be distributed virtually but were previously unavailable or difficult to obtain. These include loans, remittances, savings products, insurance, and transportation tickets.

② **Expanding reach:** The e-Transaction Platforms model is high-volume, low-margin and requires a critical mass of customers. As a result, the model involves a number of solutions for getting to critical mass quickly and cost-effectively. One such solution is *leveraging established retail networks* to develop large footprints of agents—people or businesses contracted to sign up customers and facilitate their transactions. YellowPepper, for example, leverages existing networks of mobile phone airtime distributors. IFC client Suidhaa, an e-transactions provider in India, leverages e-government centers. Where established networks do not exist or do not provide enough reach, companies also *leverage existing independent retail outlets* rather than building their own storefronts.

Another solution for reaching critical mass quickly is to target large institutions with significant *constituent networks*—of customers, employees, or citizens. YellowPepper, for example, targets corporations like Coca-Cola and SAB Miller with large numbers of small businesses and customers in their value chains. IFC client FINO, a financial services technology company in India, is working with the Indian government to transfer health insurance and rural employment benefits to millions of low-income beneficiaries.

③ **Capacity-building:** During the shift from cash to e-money, agent capacity-building is essential since they are the face of the e-transaction service to the customer, playing the vital roles of customer education, enrollment, transaction support, and exchange between cash and e-money. A customer's interaction with an agent creates the trust that is critical to adoption and use of e-transactions. The model therefore relies on *training* in the actual service being offered, in customer acquisition, and in general business and finance—which is critical to maintaining the liquidity necessary to help customers exchange cash for electronic value and vice versa, whenever they need to. Several companies using this model—such as Suidhaa and FINO—also provide *one-on-one coaching* to help agents manage their operations.

④ **Communicating value:** Successful e-Transaction Platforms businesses depend on a *key message* that expresses the value proposition in a way customers can easily identify with. YellowPepper's ad campaign offers customers "more time for yourself." E-transaction providers also use *incentives* to encourage customers try out the new service—YellowPepper encourages customer buy-in by preloading an amount of airtime equivalent to the registration fee. However, customers who have no experience with formal financial services need to be engaged by more than

advertising and incentives. *Customer awareness-raising* is key. Agents play a critical role in teaching customers the benefits of shifting from cash to e-money, and sometimes broader and more intensive customer education is required. FINO, for example, holds financial literacy workshops in villages to teach customers about the banking system and financial services in general—and e-banking in particular.

⑤ **After-sales support:** Over time, e-money will become ubiquitous. In the interim, while cash and e-money co-exist, companies in this space need to ensure that customers have *continuous access to cash*. Otherwise, the system loses utility and customers lose trust. When FINO first started, new customers would deposit 100 rupees and withdraw 99 five minutes later to see if they could get their money back. A successful customer experience in this regard ensures customer retention and positive word of mouth, helping to get the next generation of users on board.

EXTERNAL SUCCESS FACTORS

Regulation: Regulatory frameworks determine whether non-financial institutions like mobile network operators and technology companies may provide e-transactions and financial services. In most cases, they require such companies to partner with banks. Proportional regulations enable financial inclusion by permitting e-transactions providers to acquire BOP customers at lower cost. For example, "know your customer" requirements can be relaxed. On one hand, it is costly or impossible to meet them for BOP customers who may lack formal identification cards with proof of address. At the same time, such customers maintain small stores of e-money and make small transactions, posing little risk to the financial system.

Willing partners: Corporations and governments must be willing to adopt e-transactions within their networks for providers to achieve a critical mass of users quickly. Such partners provide access to large numbers of retailers, customers, employees, and other citizens. Also, and especially when required by law, e-transactions providers need to find partner banks that not only want to target BOP customers, but are open to using non-traditional distributional channels to do so.

High penetration of mobile phones: Most e-transactions providers use mobile phones as front-end, user access devices. Mobile phones will continue to be popular: by 2012, an estimated 1.7 billion people in developing countries will have mobile phones, but no access to financial services.



Insights Across Models

Among the seven inclusive business models profiled in this report, we have seen a wide range of solutions used to address key business challenges along the value chain. So far, we have discussed them at the model level, with the goal of presenting readers with the information they need in the most targeted fashion we can. At the same time, we believe—and our clients have told us—that there is significant value in learning across models. Many of the challenges are similar, and it never hurts to have a longer menu of possible solutions to implement or to inspire further innovation. Adding up the individual business model challenges and solutions laid out in the previous section, we obtain the summary below.

SUMMARY OF INCLUSIVE BUSINESS MODEL CHALLENGES AND SOLUTIONS

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges	Achieving quality, stability, and cost-competitiveness of supply	Developing a high-value, low-cost offer	Ensuring product accessibility while minimizing distribution costs	Ensuring willingness and ability to pay	Strengthening the value proposition, retaining customers, and fueling positive word of mouth
Solutions	<p>Aggregation</p> <ul style="list-style-type: none"> Collection centers Producers' associations <p>Capacity-building</p> <ul style="list-style-type: none"> Extension agents Farmer field schools Demonstration plots <p>Access to inputs</p> <ul style="list-style-type: none"> Bulk purchasing Sell inputs at cost Give inputs away <p>Access to finance</p> <ul style="list-style-type: none"> Input purchase on credit Cash loan Third-party financing 	<p>Adding value</p> <ul style="list-style-type: none"> High quality Income generating potential Accreditation Bundled product Technology <p>Reducing cost</p> <ul style="list-style-type: none"> Standardization Bulk purchasing Low-cost design Energy efficiency Leveraging existing customer knowledge <p>Matching customers' cash flows</p> <ul style="list-style-type: none"> Small package size Modular product Shared access 	<p>Expanding reach</p> <ul style="list-style-type: none"> Leveraging established retail and constituent networks Leveraging existing retail outlets Employing specialized, independent distributors Virtual distribution Evening hours Convenient locations <p>Customized delivery</p> <ul style="list-style-type: none"> Frequent, small drops Custom assortments <p>Capacity-building</p> <ul style="list-style-type: none"> Training One-on-one coaching <p>Access to finance</p> <ul style="list-style-type: none"> Inventory purchase on credit <p>Reducing cost</p> <ul style="list-style-type: none"> Efficient distribution technology Public funding 	<p>Communicating value</p> <ul style="list-style-type: none"> Customer awareness-raising Word of mouth Key message Incentives <p>Affordable pricing</p> <ul style="list-style-type: none"> Tiered pricing Public funding <p>Increasing collection rates</p> <ul style="list-style-type: none"> Business training Smart metering Sense of ownership Leveraging existing retail outlets Payment incentives <p>Access to finance</p> <ul style="list-style-type: none"> Purchase on credit Third-party financing 	<p>After-sales support</p> <ul style="list-style-type: none"> Customer education and training Maintenance and repair Resale support Career services Continuous access to cash

Looking at business challenges and solutions across models also reinforces a number of insights that influence IFC in its work with clients on inclusive business models.

➤ **Creating value for the BOP is paramount**

To succeed and remain sustainable over time, a business model must create value for the company and its partners at every step of the chain. Every single model described in this report creates value for its BOP suppliers, distributors, retailers, and consumers.

This may sound like an obvious finding. But *how* to create value for the BOP can be less obvious, and operating on assumption can lead companies astray. It can be all too easy for people to assume they know what those less fortunate want or need. If good intentions take the place of actual inquiry, they keep companies from truly understanding the

markets they are trying to serve. What does the target customer currently buy? Where, why, and at what price? What other needs do these purchasing patterns fulfill—like social interaction, relationship building, or the need to fit in? What are the customer's aspirations and what influences do these reflect? Similar questions can be asked about production patterns on the supply side and business practices in the distribution and retail chain. Better information throughout the value chain can help, and some companies are undertaking innovative new forms of research together with civil society organizations, for example. But often, real understanding comes only with experience.

This kind of understanding enables a company to develop a compelling value proposition, which is critical—whether it is lower cost, higher quality, greater earning potential, better self-esteem, or anything else. For customers, a new product or service must be worth making room for in an

already limited budget. For suppliers, distributors, and retailers, new business opportunity or business practice must be worth risking change in a finely calibrated income generation strategy. While cost reduction and sharing can be critical, willingness to pay (for customers) or invest (for suppliers, distributors, and retailers) is the foundation of any financially sustainable, scalable inclusive business model. It is important to remember that value is a subjective concept. To succeed in inclusive business—and fulfill the development objective of empowering the poor—companies must create value the way the BOP themselves define it.

➤ **Inclusive business models are almost always high-touch**

All of the inclusive business models described in this report are *high-touch*: they involve significant effort to turn, for example, subsistence farmers into productive and reliable suppliers; neighborhood shops into high-performing retail and distribution channels; and cash-strapped and skeptical people into repeat consumers who are telling their friends.

These business models not only offer a strong value proposition; they also take action to raise the target group's awareness and appreciation of it. Suppliers, distributors, retailers, and customers may be unfamiliar with new products, services, and livelihood opportunities or why they should care. They may have active misperceptions. For example, when Promigas started in Colombia, households believed natural gas service was dangerous. In some cases, the BOP may be unaccustomed to paying for a particular product or service, like clean water. And because they have little disposable income, BOP customers often have to cut something else out of the budget to make room for the new offer. Companies are responding to the need to raise awareness and appreciation of the value proposition with solutions like targeted messaging, customer education, word of mouth, targeted messaging, and incentives.

Awareness and appreciation of the value proposition are often not enough; companies must also take steps to build the target group's capacity to act on it. Suppliers may lack market information about what is needed, or the capabilities required to produce to specifications. Distributors and retailers may lack the inventory management skills or marketing savvy to keep shelves stocked so the products consumers want are available when they want them. Consumers may lack the knowledge or skills to use a product or service to its maximum effect, so they get the full benefit of the product and buy it again. This is true in housing and financial services, for example, where product literacy is about keeping the customer out of trouble—like

over-indebtedness—in addition to more than just maximizing the customer experience. Companies are responding to these challenges through capacity-building solutions like training and coaching all along the value chain.

Finally, successful inclusive business models often include financing for suppliers, distributors, retailers, and consumers who lack either the savings for large, up-front purchases (like farm equipment, store renovation, education, or housing) or the working capital for recurring or even day-to-day expenses (like planting and harvesting, purchasing inventory, or making sure food is on the table every night). Companies are responding with solutions like the option to purchase on credit, access to third-party financing, and even, in some cases, cash loans.

The key message is that for the most part, BOP markets and sources of supply do not just exist waiting to be tapped—they need active cultivation.⁹ The high-touch models required are resource-intensive. They are also local. Companies must have or be willing to build a significant local presence, including infrastructure, staff, and systems, and they must have a relatively long-term commitment to the market. Finally, high-touch models must be capable of generating enough revenues to reach commercial viability. The last two insights in this section discuss two different, potentially complementary, ways of doing so.

➤ **Many successful inclusive business models are “whole pyramid” models, not just “base of the pyramid” models**

Inclusive business models are almost always high-touch, but low-income consumers need relatively low price points. How do companies reconcile these two, seemingly conflicting, imperatives? One answer is high operating margin.¹⁰ Some business models actually achieve very high operating margins, for example where incumbents are inefficient or exploitative and charge very high prices, allowing new entrants to come in with cost structures that are much lower and prices that are only slightly so. The difference—or operating margin—is used to cover the cost of stimulating demand, capacity-building, access to financing, and other high-touch aspects of the business. It should be noted that profit margin, minus these operating expenses, may still

9 Karamchandani, Ashish, Mike Kubzansky, and Nishant Lalwani. 2011. “Is the Bottom of the Pyramid Really for You?” *Harvard Business Review* 2011, Volume 3.

10 Simanis, Erik, April 2011. “The Margin Myth: Why Low Margins Sink Businesses at the Bottom of the Pyramid.” Working Paper, Center for Sustainable Global Enterprise, Cornell University.

be low—in keeping with the “high volume, low margin” mantra that has come to dominate the BOP space—and up-front investment costs also factor into the overall financial viability equation.

BOP business opportunities offering high operating margins are rare. Much more often, IFC sees companies that are making high-touch inclusive business models work by engaging BOP segments as part of much broader markets or supplier bases. Many of the successful models in IFC’s portfolio are not just “base of the pyramid” models, they are “whole pyramid” models. The whole pyramid approach enables companies to leverage existing infrastructure, to achieve economies of scale, and sometimes, to cross-subsidize using tiered pricing based on selected indicators of ability to pay—all of which can help them reach low-income consumers with more affordable prices. The business benefits include market share, first-mover advantage, and the opportunity for innovation that could one day offer competitive advantage in higher-income markets as well. For companies engaging low-income producers, the whole pyramid approach (for example, sourcing from larger, more commercial farmers as well as smallholders) can also help diversify the supply base and manage risk.

➤ **Public funding can be used strategically**

Because of the development impact inclusive business models can have, grant funding can be available from governments, multilateral and bilateral donors, and private foundations. Donors often target early-stage ventures, helping them accelerate the journey to financial sustainability

and scale. But inclusive business models that have already reached that point can also benefit, provided they use public funding strategically. Public funding is no substitute for a business case, but it can make the business case stronger.

One strategy is to use public funding to deepen the market at the base of the pyramid, reaching even lower-income groups than it would have been possible to serve on a purely commercial basis. Many governments provide funding for services like electricity and health care directly to end users, offering companies a chance to turn the beneficiaries into customers on the expectation that they will be able to provide more efficient or higher-quality service. An alternative is output-based aid, where governments and other donors release funding to companies when pre-agreed service targets are met. The decision to leverage public funding to deepen markets should be weighed carefully, as such funding may be needed on a more or less permanent basis, and it can be politically difficult to discontinue service in the event it is withdrawn.

Another strategy is to use public funding to help defray the cost of high-touch activities—like building product literacy among consumers, business skills among small-scale distributors and retailers, and access to financial services throughout the value chain—that are necessary for business growth, and that also generate positive externalities. In these cases, the need for public funding diminishes with time as challenges are overcome, knowledge is generated and disseminated, and people’s behavior changes.

Strengthening the Inclusive Business Ecosystem

The model descriptions and cross-cutting insights in this report have been designed as practical references for business leaders seeking to start, scale, or replicate inclusive business models of their own. IFC hopes the report will point companies in useful directions in response to the challenges they face, and remains on call for those ready to take their next steps.

At the same time, this report has practical implications for all those seeking to support business leaders and entrepreneurs in developing inclusive business models.

Bilateral and multilateral donors can play a role through challenge funds, innovation funds, and technical assistance facilities that help attract companies to the inclusive business space, deepen their involvement, and heighten their development impact. These mechanisms warrant further research and evaluation to tease out and replicate best practice. Bilateral and multilateral donors can also help governments create better enabling environments for inclusive business models, as described below.

Governments should be reminded, reading this report, that the policy and regulatory environment matters. Governments can create enabling environments for inclusive business through general measures of legal empowerment for the poor, like strengthening property rights, and through specific measures to encourage business innovation while ensuring consumer protection in specific industries. Because inclusive business models are still evolving in many industries, striking this balance requires real-time dialogue between the public and private sectors. The World Bank Group and other development institutions can help facilitate such dialogue.

Civil society organizations have valuable relationships in low-income communities and insight into how community members live, what they value, and what they aspire to. These organizations have the potential to play important roles in developing products, services, and self-sustaining business models that truly do make their constituents better

off, if better bridges between the private sector and civil society can be built. There is a critical need to build mutual understanding, respect, and new ways of working together on profitable—not just philanthropic—projects. These could include new matchmaking mechanisms, legal agreements, and revenue models that incentivize civil society groups to link existing skill-building programs more tightly to business and market needs, for example, or enable them to share market insight without jeopardizing their greatest asset—community trust.

When it comes to inclusive business models, IFC's comparative advantage is providing large-scale investment and targeted advisory services to individual companies. Yet IFC realizes that it can take an ecosystem to start these models up, bring them to scale, and deepen their reach and development impact.

As a result, IFC also works to build and strengthen the ecosystems on which inclusive business models depend by generating knowledge, facilitating dialogue, and brokering partnerships among companies, donors, foundations, impact investors, governments, civil society organizations, consulting firms, and research institutions. For example, we are working to expand *access to finance for smallholders* in Africa in partnership with banks, foundations, and civil society organizations like Nib International Bank, the Gates Foundation, and TechnoServe in Ethiopia. We are working to build a *sustainable affordable housing ecosystem* in India with developers, housing finance institutions, state and national government bodies, and donors including Dewan Housing Finance Limited, National Housing Bank, and the World Bank. And we are working to support *emerging off-grid utilities models* in India and Africa with early-stage ventures, impact investors, and corporations including WaterHealth, Husk Power, Acumen Fund, the Shell Foundation, and Diageo.

In these and many other opportunities to start, scale, and deepen the development impact of inclusive business models, we invite readers to join us. IFC is open for inclusive business.

For more information, contact
IFC's Inclusive Business Group:

Toshiya Masuoka
tmasuoka@ifc.org

Eriko Ishikawa
eishikawa@ifc.org

+1 (202) 473-9538
ifc.org/inclusivebusiness

IFC
2121 Pennsylvania Ave., NW
Washington, DC 20433, USA
Ifc.org/inclusivebusiness

2011