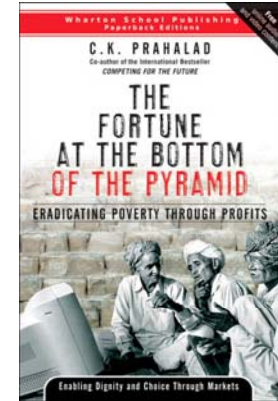


## The Bottom of the Pyramid: Entrepreneurship, “The Missing Middle,” and Market Development in Less Developed Countries

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<http://www.bus.wisc.edu/realestate>

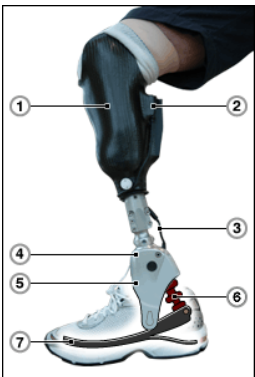
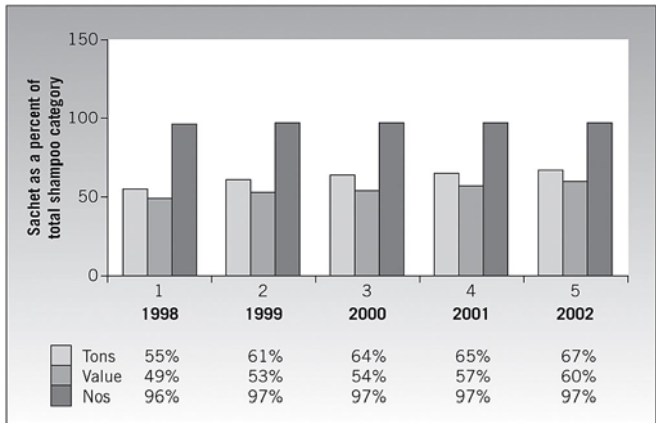
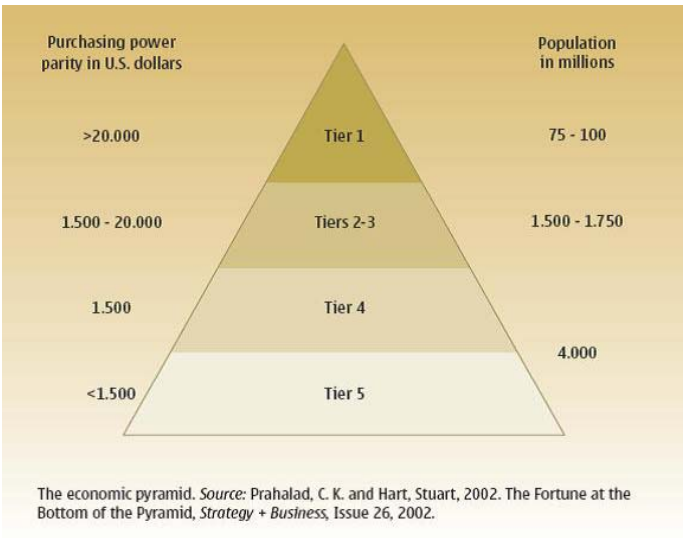


### Today's discussion

- Summarize the BOP argument
- What does the BOP look like?
- Critiques of Prahalad and BOP
- How do we escape the BOP?
  - Well, there will always be a bottom quintile of any distribution. Rather, how do we make the BOP more like the TOP?
- Final remarks

### Summarize the BOP argument

- Follow the market: there are 4 billion people below \$1500 per capita GDP.
  - (Data presented are fuzzy, but qualitatively correct).
- Market opportunities exist, but you have to adapt. Examples:
  - Single-serve packages of shampoo (Hindustan Lever)
  - The “Jaipur foot”
  - Affordable housing (e.g. Cemex)
  - Wider retail (e.g. Casas Bahia)
- Reducing corruption, improving governance helps.



Hi tech, but out of reach to many patients around the globe.

<http://news.bbc.co.uk/1/hi/magazine/6153748.stm>



**Wouldn't you like to own this?**

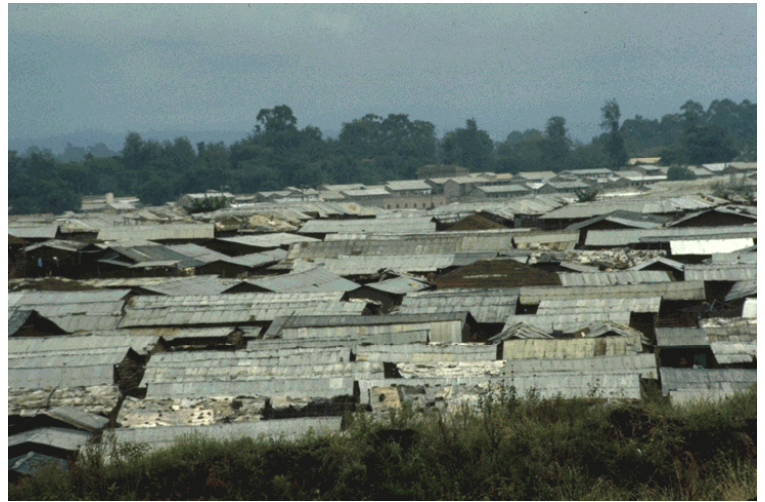


**Or would you rather own this?**



**What does the BOP look like?**

- A few photos
- A little data







**Rough Comparison of Bangladeshi and U.S. Textile Factory Wages**

	Hourly Wage Textile Manufacture	Hours/ Week	Weeks/ Year	Rough Est. Annual Wages	Country's GDP Per Capita 2000	Ratio, Wages/ GDP PC
Bangladesh	0.17	40	52	354	380	0.93
United States	10.96	40	52	22,797	34,260	0.67

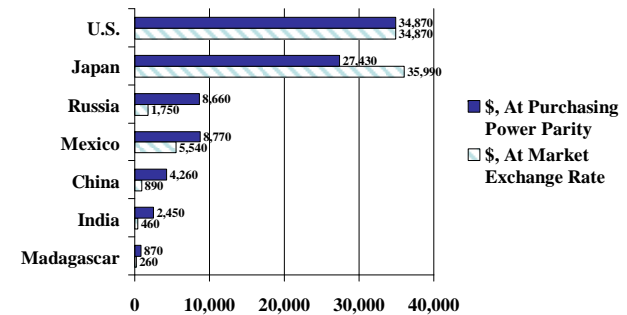
<http://www.womenstudies.wisc.edu/WSRC/index.htm>

To hit the U.S. ratio of textile wages/GDP PC, Bangladeshi wages would be 12 cents per hour.

## Economic Development is Not Just About Gross Domestic Product

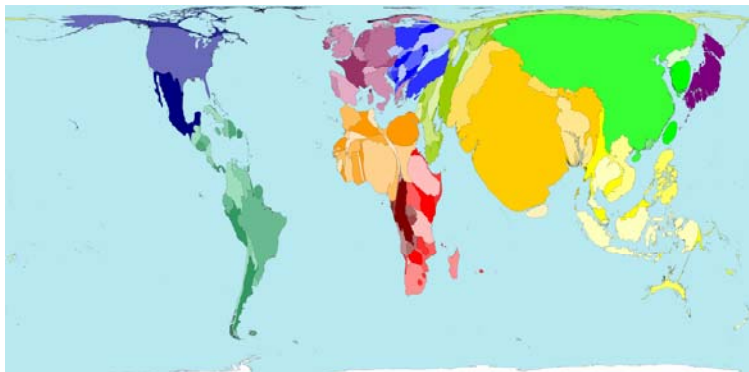
- Development comprises many dimensions
  - GDP, income, purchasing power
    - Level *and* distribution
    - Poverty reduction
  - Education
  - Health, mortality
- But if you have to pick one thing to start with as a measure, GDP per capita is not a bad place to start.
  - Most other measures of development are positively correlated with GDP p.c.
  - An important exception: the distribution of income is more or less uncorrelated with GDP p.c.

## GNP Per Capita: Selected Countries, 2001



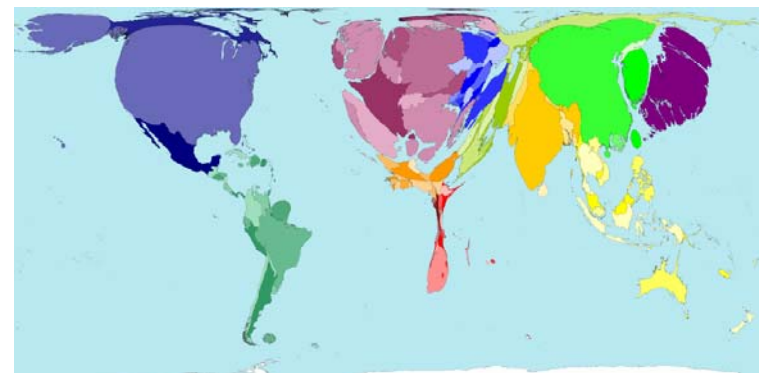
Source: World Bank

## World Population



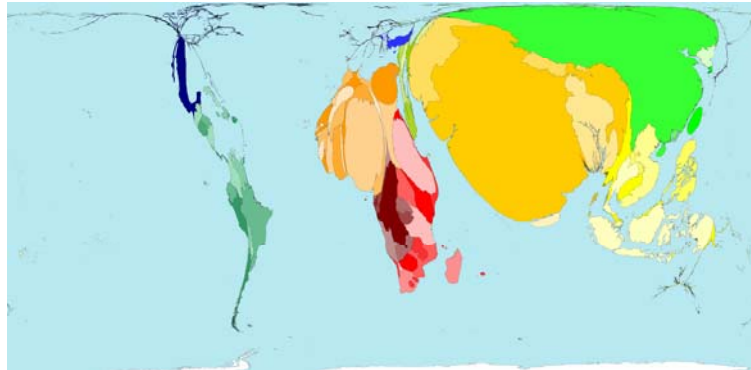
<http://www.worldmapper.org/>

## Total GDP at Purchasing Power Parity Exchange Rates



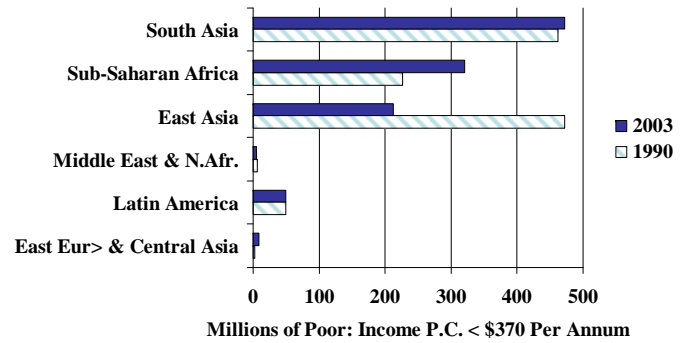
<http://www.worldmapper.org/>

### World population under \$2/day



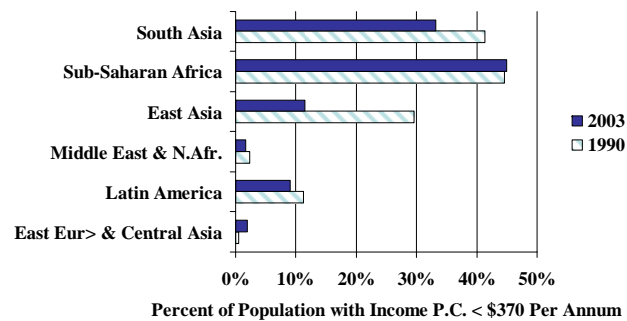
<http://www.worldmapper.org/>

### Poverty in the Developing World: 1990 and 2003



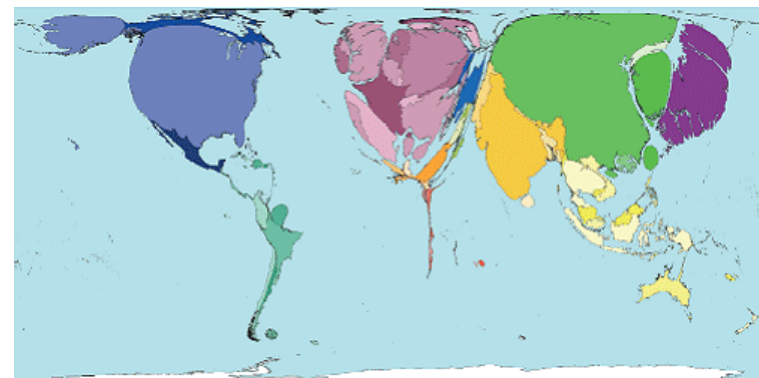
Source: World Bank Global Econ Prospects 2007

### Poverty in the Developing World: 1990 and 2003



Source: World Bank Global Economic Prospects 2007

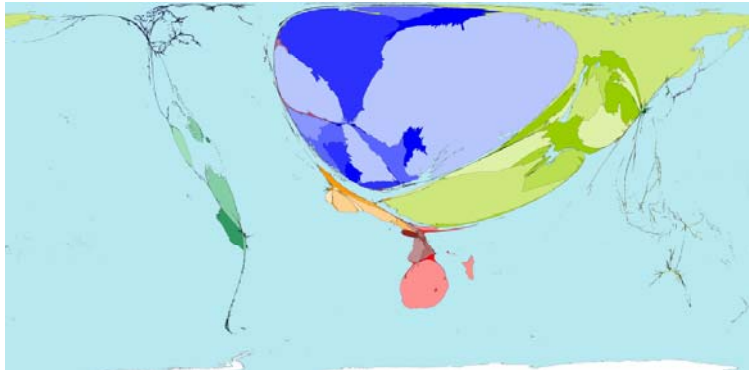
### Growth in Aggregate PPP GDP 1975-2002



<http://www.worldmapper.org/>

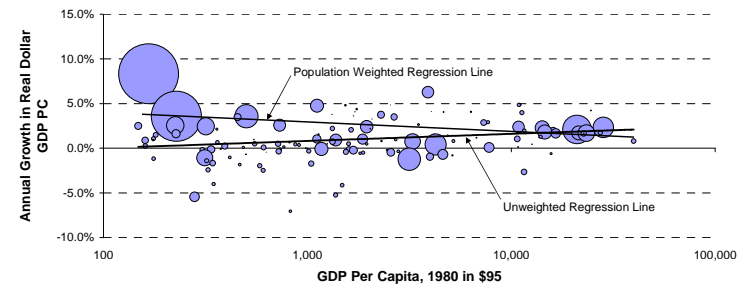


## Declines in PPP GDP, 1975-2002



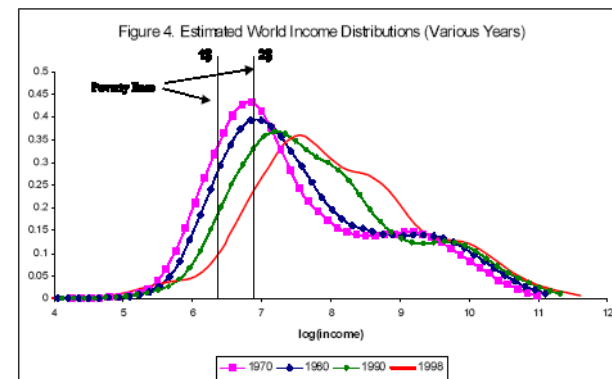
<http://www.worldmapper.org/>

**GDP Growth and Initial Conditions**  
Growth in Real U.S. \$, 1980-2000



## Stylized facts about world income distribution

- With countries as unit of observation, convergence is weak at best.
- Within many countries (U.S., Mexico, China), income inequality has been growing.
- With individuals as unit of observation, world income distribution has been (slowly) converging.
  - Debate exists over extent, methodology, but qualitative consensus is solidifying.



Source: Xavier Sali-i-Martin

## Critiques of Prahalad and BOP

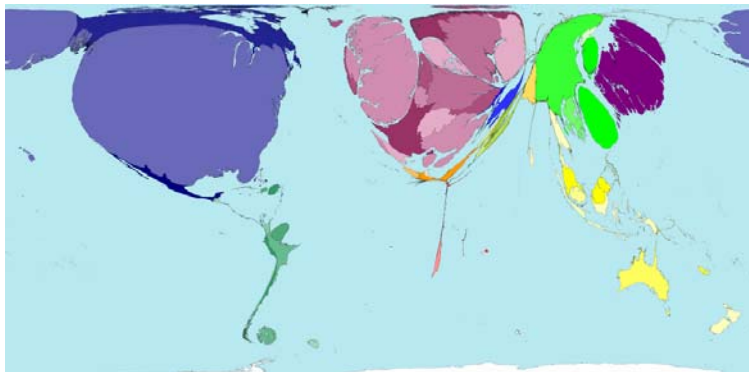
- See Aneel Karnani, “The Mirage at the Bottom of the Pyramid” for a prototype.
- The essential critique is that the BOP discussion focuses on *consumption*, rather than *production*.



## The critique has some force, but remember...

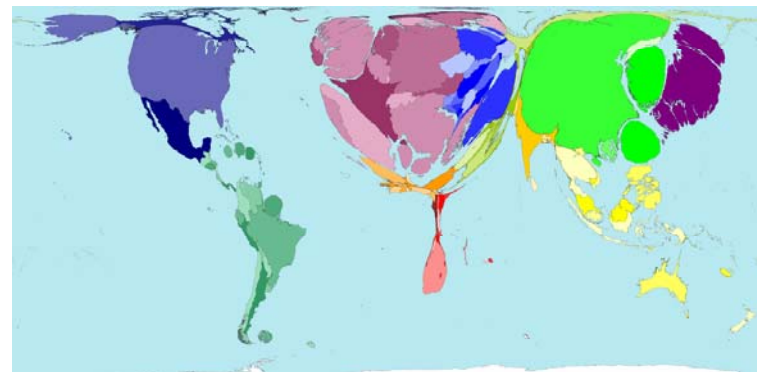
- We are all simultaneously producers, and consumers.
- There are two ways to raise real standards of living: increase output, and lower prices.
- There are costs to informality, *per se*.
- There is some evidence that greater access to markets (e.g. imports from abroad) has dynamic effects on an economy.
- Some goods labeled “consumption” are at least partly “investment.”

How 12 MM cell phones were distributed in 1990



<http://www.worldmapper.org/>

How 940 MM cell phones were distributed in 2002



<http://www.worldmapper.org/>

## What are we selling here? Does it matter?

- Cigarettes or cell phones?
- Shampoo
- Housing
- Prosthetics
- Baby formula
  - Nestlé still wrestling with this controversy?
- MNC marketing: threat, or menace?
  - Why are many economists so blasé about marketing?  
Why does Naomi Klein's *No Logo* give us the giggles?
  - See <http://www.wnyc.org/news/articles/4390> for pros and cons.
  - Are we underestimating the power of our colleagues in the Marketing Department?

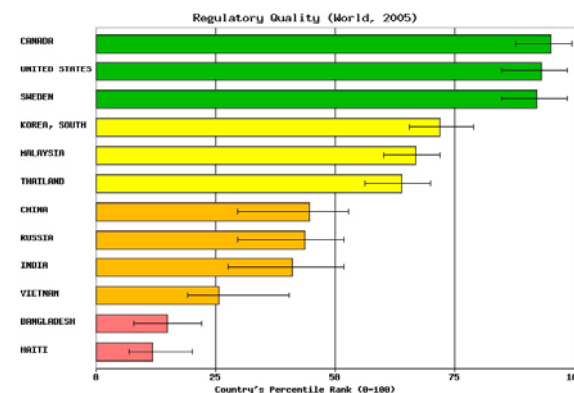


Dani Kaufmann

## How do we escape the BOP?

- Well, there will always be a bottom quintile of any distribution. Rather, how do we make the BOP more like the TOP?

## Survey measures of “regulatory quality,” selected countries



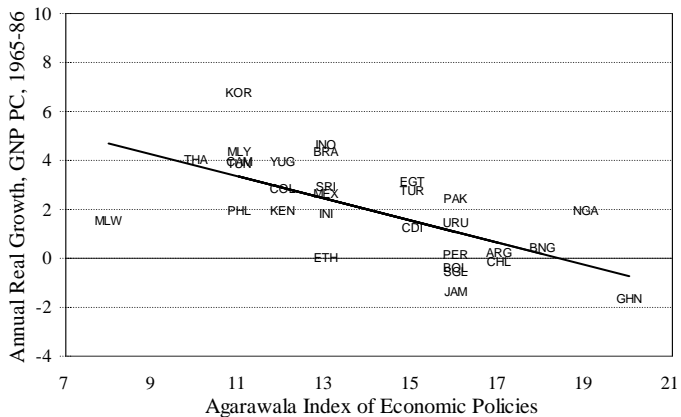
## Why Do Some Countries Grow Faster Than Others?

- Some things that matter *a lot*:
  - Economic policies and incentives and institutions
  - Education (*esp. if incentives are correct*)
- Some things that matter less than you might think, or *under some conditions but not others*:
  - Whether you *start out* rich or poor
  - The level of investment (!)
  - Natural resources (!)
  - Foreign assistance
  - *Generally, if you have the policy environment right, and educate your people (boys and girls) **then** these things will help.*

## Measuring Economic Policies

- We use an index based on work by Ramgopal Agarwala. Index is based on policies re:
  - Exchange rates
  - Interest rates
  - Labor pricing (e.g. minimum wages)
  - Trade (tariffs, etc.)
  - Agricultural pricing
  - Infrastructure pricing
  - Inflation

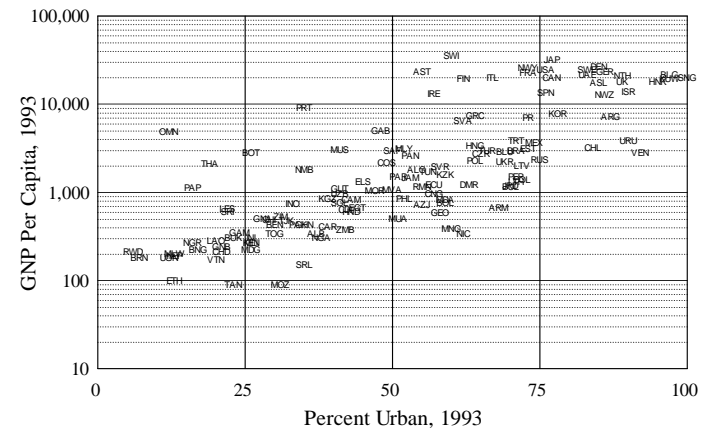
## Growth and Economic Policies



Source: Malpezzi (1990)

— (Linear Fit)

## Urbanization and GNP Per Capita



## (Very) Brief Intellectual History of Economic Development

- 50s and 60s: Accumulating capital, Harrod-Domar growth models, overcoming the “two gaps”
- 70s: Basic Needs, Human Capital
- 80s, 90s: Incentives, property rights; institutions (again!) Market based, enabling approaches
  - Markets matter to the poor
  - Market based approaches vs. “trickle down”
- 2000s: Governance? What else?

## Current controversies

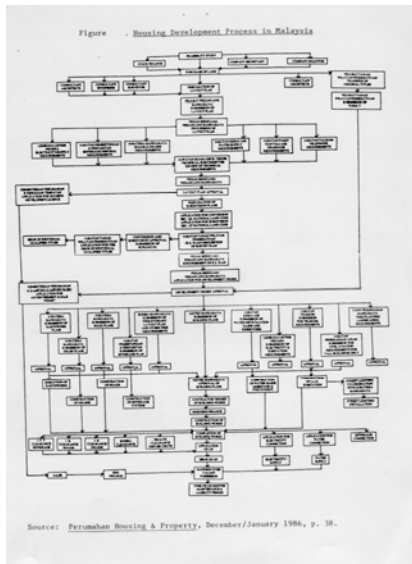
- Natural resources (oil): help or hindrance?
- Education: necessary or sufficient condition?
- Rapid population growth: good, bad, or a wash?
- How important are “shocks” (“good luck?”) compared to policies?
- Institutions vs. geography?
- Corruption: is there a difference between “good” and “bad” corruption, or is it all bad?
- Democracy: cause of development, effect, or both?
- Millennium Development Goals: great leap forward, or pie in the sky?

## Why Do Some Countries Grow Faster Than Others?

- Some things that matter **a lot**:
  - Economic policies and incentives
  - Education (*esp. if incentives are correct*)
- Some things that matter less than you might think, or matter *under some conditions but not others*:
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  - Foreign assistance
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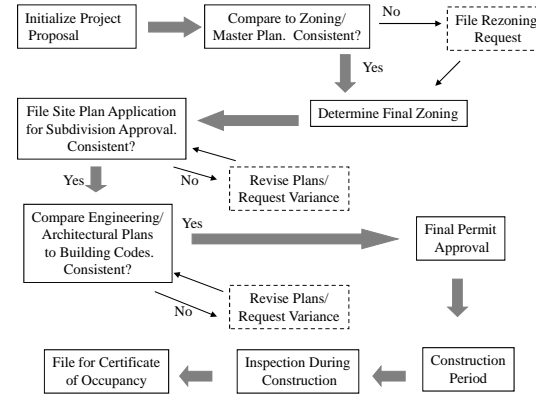
## Case study: Malaysian Housing

- Circa 1989: Malaysia’s formal housing market is producing only for the top end of the market.
  - Houses start at M\$50K
  - No one building for the middle of the market (around M\$25K).
    - Despite high subsidies (free land) for Special Low Cost Housing Program!
  - There are informal/slum dwellings around \$M5K.
- Where’s the middle of the market?
- Is it:
  - Labor cost?
  - Cement prices?
  - Or something else?

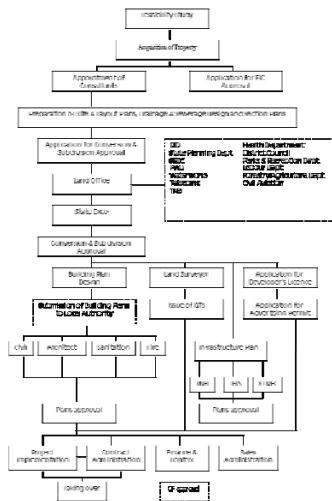


Source: Sen

A Stylized View of Regulation During the Real Estate Development Process

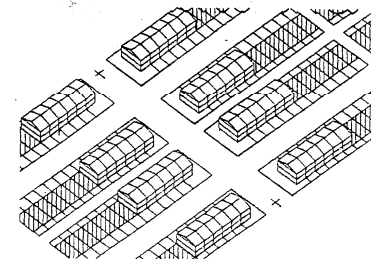
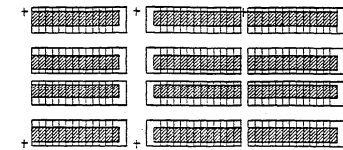


Source: Malpezzi 1998



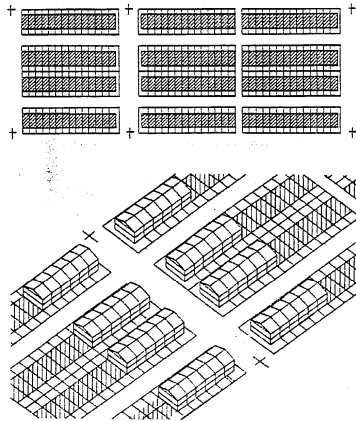
Site Plan Corresponding to SLCHP Guidelines  $\Delta$

44 % of Saleable Land  
20.5 % Community Facilities  
36.5 % Roads  
FAR: 0.23



Site Plan Corresponding to Iteration (3) ▲

55 % of Salable land  
 19.4 % Community Facilities  
 25.6 % Roads  
 FAR: 0.41



### Point of View I: The Economy

- + Market Value of the Unit
- Resource Cost to the Economy

-----  
 Net Economic Cost-Benefit

### Point of View II: The Developer

- Resource Cost to the Economy
- + Land Subsidy
- + Development Period Infrastructure Subsidy
- + Construction Subsidy
- Cost of Land Use and Building Regulations
- Land Acquisition Taxes
- + Sales Price

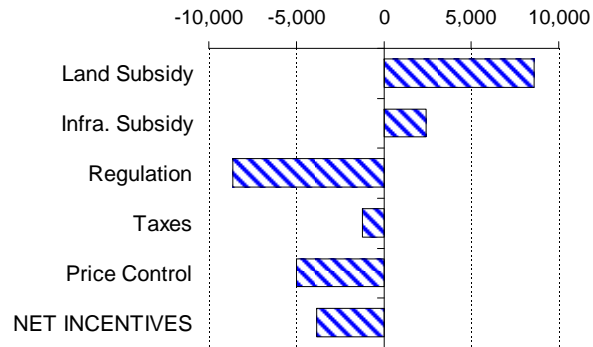
-----  
 Net Financial Cost-Benefit to Developer

### Point of View III: The Consumer

- Sales Price
- Registration Taxes
- Property Taxes
- Extra Transactions Cost of Program Participation
- + Market Value of the Unit
- + Recurrent Infrastructure Subsidies
- + End User Finance Subsidies

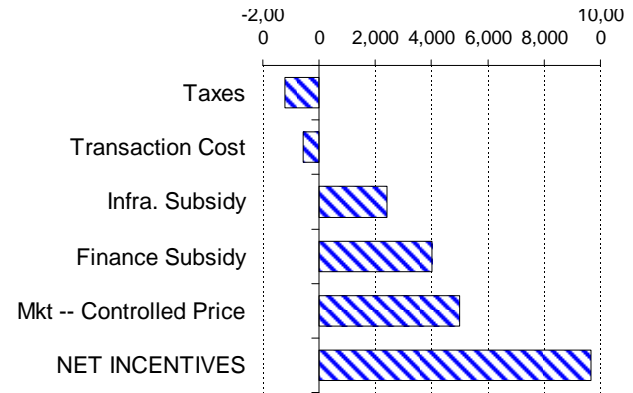
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 Net Financial Cost-Benefit to Purchaser

### Summary of Developer Incentives



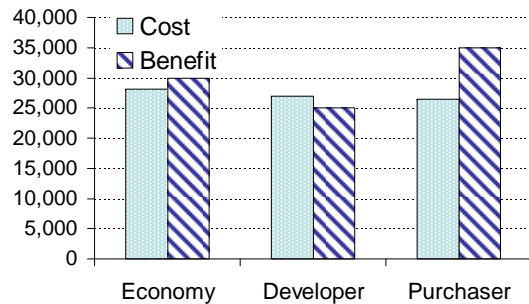
SLCHP Unit, Selangor, Current Stds (from Malpezzi and Mayo 1997)

### Summary of Consumer Incentives



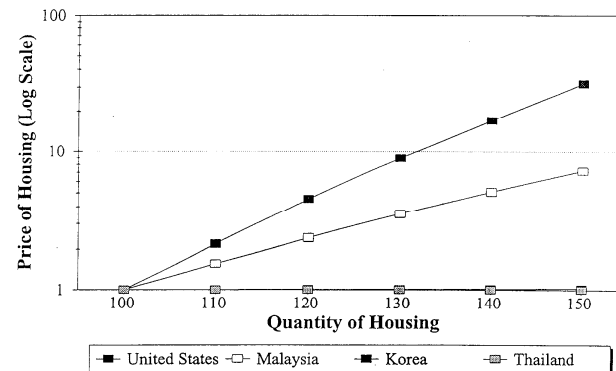
SLCHP Unit, Selangor, Current Stds (from Malpezzi and Mayo 1997)

### Summary of Malaysia Incentives, Test Case



SLCHP Unit, Selangor, Current Stds (from Malpezzi and Mayo 1997)

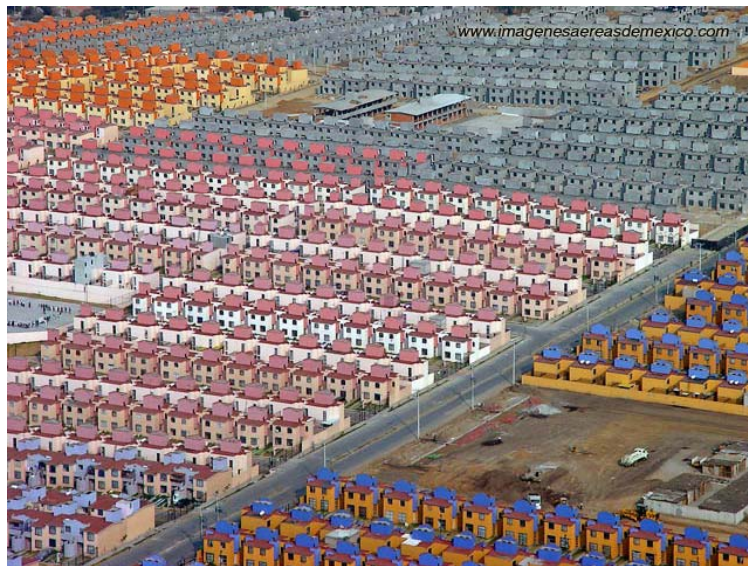
### Estimated Supply Curves Four Countries





**The costs of informality:  
two photos of Mexico, by Ruiz**

<http://homepage.mac.com/helipilot/PhotoAlbum31.html>



**Final remarks – discussion questions about BOP**

- Is the BOP insight only about, say, India or Ghana – or is it also about the U.S. and other developed economies?
- Is “consumption” ever “productive?”
- In many countries, we need to worry about the MOP and even the TOP?
  - If the market doesn’t work for the rich, will it work for the poor?
- BOP – a “silver bullet,” or a part of the puzzle of development?

## Selected References

- C.K. Prahalad, *The Fortune at the Bottom of the Pyramid*. Wharton, 2005.
- Aneel Karnani, "The Mirage of Marketing to the Bottom of the Pyramid," *California Management Review*, 2007.
- Daryl Collins, Jonathan Morduch, Stuart Rutherford, Orlanda Ruthven, *Portfolios of the Poor: How the World's Poor Live on \$2 a Day*. Princeton, 2009.
- World Bank, *Housing: Enabling Markets to Work*, 1993 (Principal authors: S. Angel and S. Mayo)
- S. Malpezzi, Housing in Developing and Transition Economies, *Handbook of Regional and Urban Economics*, vol. 3, 2001

**Email me for a more detailed  
list of references.  
smalpezzi@bus.wisc.edu**