The Hidden Pitfalls of Inclusive Innovation
By Raghav Narsalay, Leandro Pongeluppe, & David Light
A few years ago, a large multinational corporation developed a new food product designed for low-income people in emerging markets. The product was highly nutritious and low-priced. To win the trust of people in remote rural communities, the company recruited a sales force of local women, who in turn developed recipes using the product and helped teach community members how to prepare those dishes. A yearlong trial confirmed the product’s potential: consumers found it easy to use and less expensive than common alternatives. Success seemed all but guaranteed.

But company executives decided not to continue investing in the project after the trial period. They determined that the product wasn’t reaching new customers at a fast-enough pace—in other words, the business wasn’t scaling up. Product managers had tried to do all the right things, but it wasn’t enough.

Other companies attempting to develop innovative products for the poor have faced similar challenges. For example, a large consumer products company developed an inexpensive water purifier. The company tried building a commercially viable venture targeting low-income customers, but it was unable to get enough people to make repeat purchases of the water purifier, and so was unable to
grow the business. In the end, the company turned the venture into a nonprofit. Another company has developed an affordable refrigerator, but it too is finding it difficult to sell enough of them to make it a sustainable business.

Such derailments of “inclusive innovations”—high-quality yet affordable goods and services designed for and sold to low-income people—are not uncommon. Companies often recognize the value of these projects but falter in the execution. In 2011, for example, 98 percent of the Indian manufacturing executives we (at Accenture) surveyed said that inclusive innovation would be critical to their company’s future success, yet only 30 percent reported that developing inclusive products and services was an indispensable part of their business.

To discover why some inclusive innovation projects fail—and why others, against the odds, succeed—we researched inclusive business initiatives (IBIs) in 17 multinational companies in five developing countries—Brazil, China, Ghana, India, and Nigeria—and a banking institution from Australia that targeted remote rural areas. The initiatives, each with annual sales of at least $100 million (with the exception of Esoko Networks Ltd.), were in eight industry sectors and included such companies as Nestlé, Haier, Siemens, Nokia Telecommunications, Hindustan Unilever, SAIC-General Motors-Wuling, and Tata Motors. (Because of confidentiality agreements we are not able to identify all the companies mentioned in this article.)

Our study revealed that IBIs face many special hurdles as they begin to ramp up their operations. Some of these obstacles are well known, including inadequate physical infrastructure—such as utilities, IT networks, public transportation, and health care facilities—a lack of effective regulatory bodies, and useful market data. These obstacles are challenging, but visible and familiar, and many IBI leaders are prepared to overcome them.

What often blindsides IBI leaders, however, are pitfalls that are less obvious yet equally (or even more) dangerous. We identified five pitfalls that frequently knock IBIs off course before they can gain traction: lacking support from the top, focusing on the wrong performance metrics, failing to recruit talented executives, using old business models, and partnering with the wrong organizations. Our study of initiatives that successfully achieved scale also produced insights into how to avoid each of these hazards.

PITFALL 1: LACKING SUPPORT FROM THE TOP
CEOs and other top corporate executives often give verbal support to inclusive innovation and the economic and social benefits it offers. Doing so provides good public relations for the company and gets them invited to prestigious confabs such as Davos and the Clinton Global Initiative, where they can hobnob with business executives, political leaders, and NGO executives from around the world. But in practice, top managers can be extremely tough on IBIs, and their support is often lukewarm at best.

Because of this tepid support from on top, ordinary problems that typically occur in the development of any new product or service can take on extraordinary importance and derail an IBI early in its journey. For example, while top managers in many companies do not blink an eye when allocating funds for product design and development aimed at middle-class customers, they develop cold feet as soon as they hear that the proposed spending is for products meant to be sold to low-income customers. And even if IBI teams succeed in clearing this barrier, they face another hurdle from the innovation lab heads, who are often not willing to spare their human and financial capital to work on what they see as highly risky ventures, unless they are prompted by top management or the board to behave otherwise.

Top managers are wary of IBIs for many reasons. Some are concerned that the project will lose money, others that it is a distraction from the core business, and still others that it requires the company to become involved in building support infrastructure (such as electricity and IT) that is beyond its expertise.

But what underlies much of top management’s wariness is the fear of the unknown. Top executives will often be reluctant to pursue experiments that take the company beyond well-tested assumptions about its core customers. Others may be concerned that an IBI will unnecessarily drain resources from the core business and hamper the company’s ability to compete. So when an important supplier fails to maintain the quality of its goods, and the IBI has trouble locating a replacement source—to name one bump that can befall any new business—executives at the corporate headquarters might scuttle the project before the initiative’s leaders have had the chance to fully explore alternatives. If conventional ventures have three strikes before they’re out, IBIs are often allotted just one.

To overcome this fear of the unknown—to turn up the heat on lukewarm support—IBI leaders have a number of approaches at their disposal. One is to turn the company’s board members into venture capitalists. At Unilever’s Indian subsidiary, Hindustan Unilever Ltd. (HUL), the company evaluated six IBIs by making board members responsible for allocating resources—in the form of people, money, and specialized internal expertise—to each of the six project managers. Every quarter, the IBI project managers would pitch their case for continued funding to the board, and all ventures were assessed against milestones pegged to growth of the business. Teams usually moved to the next round of funding only after they had achieved a scale that hit the milestone.

This competitive, entrepreneurial environment kept all the board members heavily involved in the IBIs, even though they accounted for only a small part of the company’s overall business. Board members also provided guidance to project teams and used their contacts to open doors within and outside the company. Of the six original IBIs, two survived the three-year test period—a solid result, due in part to the support from the board.

Fear of the unknown can also be overcome by launching an IBI as a corporate social responsibility (CSR) initiative rather than as a business initiative. Taking this approach lowers or eliminates the bar on growth and profitability, giving managers time to develop the initiative.

Consider, for example, an IBI by Alibaba.com, China’s largest e-commerce company. In 2006, a few small-town furniture makers launched online storefronts on Alibaba’s platform, with the aim of accessing larger markets such as Beijing and Shanghai. Seeing a
means power and Shakti Amma to help them market the products and also to teach them how to reach. But the project’s success came about only through patience and persistence.

For example, when Haier wanted to roll out 6,000 Goodaymart stores in rural China, it first had to invest an enormous amount of time and money to build the capacities of the local entrepreneurs who would operate the stores so that they could deliver a standard customer experience. And before an IBI can even begin to start doing business, it must first orbit the rapid expansion in online storefronts based in the small town. By 2010, more than 2,000 shops were online, and the town now hosts more than 180 furniture factories and about 20 logistics firms. Perhaps most important, the town’s furniture has become a recognizable brand among high-income consumers in China’s urban markets. Although rural IBIs still have a limited impact on Alibaba’s bottom line, the scalability of these initiatives has convinced the company’s leadership of the long-term value of rural-to-urban e-commerce.

PITFALL 2: FOCUSING ON THE WRONG PERFORMANCE METRICS

IBIs are often expected to mature as commercial businesses at the same rate of speed as other ventures, and so are often judged by performance metrics that emphasize revenue and profit growth. But company leaders seem to forget that a great deal of time and effort must be put into creating the necessary infrastructure, often under challenging circumstances, before an IBI can even begin to start doing business.

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PITFALL 3: FAILING TO RECRUIT TALENTED EXECUTIVES

IBIs are extremely challenging to manage and need talented executives to lead them. Yet attracting talent to an IBI is often difficult. IBIs are typically portrayed within companies as risky ventures with a high probability of failure. And even when an IBI succeeds, it is unlikely to have a material impact on the company’s financial performance. So under most circumstances, it’s a rare person who is willing to risk her career on such a gamble.

To counteract such challenges, top management must treat IBIs as they would any other strategic project for the firm. YES BANK, in Mumbai, India, has consistently taken this approach, and so has been able to assemble top-notch teams to develop its IBI initiatives.

Take, for example, the development of a new service aimed at low-income workers called YES MONEY. One day while walking to the office, the chief financial inclusion officer of YES BANK saw long lines of people standing in front of a state-run bank branch. When he spoke to some of the people standing in line, he learned that they were migrant laborers who were waiting to remit their earnings back to their families living in rural villages. After further
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often ends up being one of the many partners the NGO or government organization is working with in the same or similar areas. Instead of being treated as collaborators, the corporations become rent generators for the NGOs and government organizations. In some cases, the large NGOs and government organizations are themselves perceived to be authoritarian and dominating players and are detested by locals.

That’s why the best partners for large corporations are often small, local NGOs and entrepreneurs who are deeply embedded in the community and have earned their trust. In Brazil, major paper producers, including Votorantim, Klabin, and Suzano, are engaging communities through local NGOs and using these relationships to advance sustainability practices at a grass-roots level. For example, Klabin’s Forestry Incentive Program, first introduced in 1987, aims to increase the incomes of rural residents by developing sustainable forests that Klabin can harvest for timber.

Klabin initially partnered with government organizations to provide funding and technical assistance to local producers with an eye toward improving forest sustainability. The initiative provided farmers with resources and know-how useful for building sustainable forests, but Klabin found that many local producers still chose to use older and less sustainable methods. To bring these farmers on board, Klabin needed to inspire a change in behavior. It did so in 2005 by partnering with a local NGO named APREMAVI (Association for the Preservation of the Environment and Life). APREMAVI had built and maintained long-term relationships with local producers and thus was able to convince them that sustainable forests and Klabin’s initiative would help secure their industry’s long-term success.

Klabin is also working with APREMAVI to convince local producers of the value of having their forests certified by the Forest Stewardship Council. The goal is to get all local producers certified so Klabin can become the only large paper company in Brazil that processes 100 percent certified timber. More than 17,000 farmers now receive sustainability-related incentives in the states of Paraná and Santa Catarina. The collaborative program covers 124,000 hectares of cultivated forests, and 198 million seedlings have been distributed to farmers since the program began.

Partnering with small local NGOs, however, is not easy. They frequently don’t have the expertise or the capabilities necessary to participate in a for-profit business venture. In fact, concerns about profitability are typically foreign to the DNA of their organizational cultures.

To create mutual trust with small NGOs and local entrepreneurs, companies must rethink how they partner. NGOs and local suppliers want to feel they are being taken seriously—not just being used to make inroads for a large corporation. One of the most effective ways for an IBI to reassure them is to set up an internal group to help transfer important expertise and best practices—in both directions—with their external partners.

NATURA, one of Brazil’s largest manufacturers of beauty, skin-care, and cosmetic products, created this kind of trust by establishing an Eco-Relations Management department. With employees in the field and a back-office staff, the department is responsible for managing partnerships with NGOs and local entrepreneurs and for training them to improve their operational efficiency. The department’s leader reports to the company’s supply chain director and sustainability director.

NATURA’s team remains in constant communication with NGO partners and local suppliers to ensure that the aspirations of NATURA, the NGOs, and the local communities are always in alignment. The company even asks NGO staff members to accompany its teams of agricultural scientists, environmental engineers, anthropologists, and biologists on visits to local communities. As one senior executive noted, “the company does not send a buyer to interact with the community, but someone who understands the social logic.” This approach has helped the company gain local communities’ trust and develop purchasing channels that dovetail with the communities’ social structure and cultural expectations.

By 2011, NATURA had established relationships with 32 rural low-income communities comprising more than 3,000 households. These communities supply NATURA with raw materials and knowledge about the medicinal or cosmetic properties of local plants in exchange for direct payment and investment in local infrastructure, such as roads, schools, and hospitals. Adopting this approach helped NATURA launch a new line of cosmetics, NATURA Ekos, by drawing on local knowledge.

A NECESSARY DEVELOPMENT

Overcoming the hidden pitfalls facing IBIs is hardly a trivial matter. And yet the stakes for doing so could not be higher. Over the next few decades, billions of people who are now low-income will, because of economic growth, move into the middle class. According to estimates from the Organization for Economic Cooperation and Development, the global middle class will surge from 1.8 billion people in 2011 to 4.9 billion by 2030, with Asia accounting for 85 percent of that growth. And the purchasing power of that group is expected to rise from $21 trillion to $56 trillion during that same period.

In the meantime, those aspiring consumers need products that people in the rest of the world take for granted: the means to access clean water, as provided by HUL’s Pureit water filter; the ability to save or transfer money and obtain loans, thanks to the efforts of financial firms like YES BANK; and the opportunity to obtain inexpensive, reliable, and functional transportation such as that provided by the joint venture of GM-SAIC-Wuling in China.

Companies that figure out how to meet the needs of people moving out of poverty toward the middle class will be well positioned to serve those same customers decades into the future. Indeed, in our survey of Indian manufacturers, more than two-thirds of the executives surveyed said they believed that those businesses that embrace inclusion will ultimately outperform those that do not.

The ability to overcome the hidden pitfalls of inclusive business initiatives is more than a CSR effort or a nice-to-have organizational skill. For companies that recognize the opportunity to provide the poor with goods and services that are both affordable and high quality, it’s rapidly becoming a necessary core competence.

NOTES

1 2014 annual report of YES BANK