

# Chapter 5

## Theoretical Aspects on Bottom of the Pyramid in Emerging Economies: An Overview of Microfinance in Latin America

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### ABSTRACT

*Despite the growing body of literature on the Bottom of the Pyramid (BoP), much remains unclear and more research is needed in a number of areas as this chapter will highlight. Firstly, the broad literature is reviewed which includes looking at definitions and different strands of research undertaken in the field. The chapter then presents three key sectors that the authors believe have the most potential to aid poverty alleviation, while proposing that other types of studies can be conducted for other sectors that are more likely to lead to consumer satisfaction. Points of departure are offered, before discussing microfinance and then latterly in the context of Latin America. The chapter uses secondary data to show key countries and institutions serving the BoP, and to highlight important aspects that merit further attention. Implications for policy makers and practitioners are offered, and this is followed by a number of directions for future research.*

### INTRODUCTION

The concept of the Bottom of the pyramid (BoP) first introduced by C.K. Prahalad has led many scholars to undertake research on the low-income consumers and underserved communities, and this has become a promising area of study. This chapter aims to uncover two important objectives: firstly, to review the

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concept of BoP, and secondly to map out a number of microfinance institutions that serve this segment in the region of Latin America. We begin this chapter with a review of BoP from its inception, and the controversy surrounding the definition, before delving into the literature on the BoP, including Prahalad's work and the main theoretical developments. Attention then turns to microfinance and the BoP in emerging markets, before focusing more specifically on Latin America as an important region of study. The chapter then using secondary data maps out the microfinance companies serving the BoP, and the Latin American countries in which they operate. This will allow scholars undertaking research on this area to more easily identify which companies and countries merit further and more narrow research at different levels, including a firm and individual level. Finally, we conclude with policy implications and future research directions.

## **BOTTOM OF THE PYRAMID: PRAHALAD AND BEYOND**

The Peruvian economist Hernando de Soto (2000) calculated that up to half of the total economic activity undertaken in emerging markets takes place outside the formal economy. The scholar further states that the total unregistered assets among the world's poor accounts for US\$9 trillion, a point acknowledged by Prahalad (2010). London and Hart (2004) have consequently suggested that within such an informal context, governments and firms should primarily build relationships based on social, rather than legal contracts. The work of these scholars has set the foundations and contributed significantly to research on how firms in emerging economies should look in a constructive manner at the people living at the bottom of the socio-economic pyramid.

There are different ways to define the bottom of the pyramid, and initially Prahalad and Hart (2002) in their seminal paper outlined the BoP as people living with an annual income of less than US\$1,500 measured on purchasing power parity (PPP) basis. However, much debate has centred on this PPP threshold and this is due to the lack of rigour. The World Bank and other scholars use different thresholds and so there is clearly a lack of consistency, which is neatly pointed out by Karnani (2007). The World Resource Institute (WRI) and its partners have proposed a new definition and this threshold is based on an annual income of US\$ 3,000 PPP in 2002 U.S. dollars, which is \$3,260 when adjusted to 2005 U.S. dollars (London, 2007). According to the WRI threshold, the total amount of people living at the BoP across Africa, Asia, Eastern Europe, Latin America and the Caribbean accounts for nearly 4 billion people (Hammond, Kramer, Katz, Tran, & Walker, 2007).

Nevertheless, it remains very opaque, and it is complex to establish a consistent BoP definition when purely based on an income basis. An important issue to point out is that the national context in various emerging economies is different, with certain regions of the world exposed to higher levels of extreme poverty (people living on less than US\$1.25 per day). At the same time there are studies that apply a rather general definition of BoP that is well above the US\$ 3,000 annual income (Hart, 2005). Furthermore, there are important differences when we take into account rural poverty contexts (often the case with African countries), and urban poverty (often the case with the Latin America region). This distinction is fundamental, and well explained by Kolk, Rivera-Santos, and Rufin (2013) who point out that "the spending power on consumer goods in the shantytown of the three largest cities in Venezuela is between 5 and 10 times higher than that of the whole Indian rural BoP population" (p.15). It is the case also that some studies tend to segment the BoP and just focus on one specific tier (either taking the lowest or highest). These limitations illustrate how difficult it is to arrive at a universal definition for the BoP.

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