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PROOF

## Part II

# Institutions and Foreign Investment



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# 3

## The Entry of Multinational Companies to the Base of the Pyramid: A Network Perspective

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### Introduction

One of the markets that has attracted the attention of business leaders and consequently international business researchers in recent years is the base of the economic pyramid (BOP) (Hammond and Prahalad, 2004; Hart and Christensen, 2002; Lodge, 2006; Lodge and Wilson, 2006; London and Hart, 2004; Prahalad, 2009; Prahalad and Hammond, 2002; Seelos and Mair, 2007). This market, which comprises people with a daily income of less than \$2 a day, has mainly been ignored by multinational corporations (MNCs) up until now (Hammond et al., 2007). However faced with saturated markets at the top of the economic pyramid, MNCs are increasingly diverting their attention to the BOP and developing strategies to enter this market and sell their products or services to this segment. Recent studies illustrate that corporations have to revise the way they do business in order to fit the specific characteristics of the BOP (London and Hart, 2010). One of the factors found to distinguish successful from unsuccessful MNCs in this market is the building of relationships with non-traditional partners such as non-governmental organizations (NGOs) (Teegen, Doh and Vachani, 2004). While the role of NGOs has been corroborated in several international business studies (Doh and Teegen, 2002; Parker, 2003; Teegen et al., 2004; Teegen, 2006), and specifically at the BOP (London and Hart, 2004; Prahalad, 2009), we still know very little about how NGOs help MNCs to enter the BOP (Perez-Aleman and Sandilands, 2008). To explain the relationship between MNCs and NGOs and its effect on the former's entry to the BOP market, this research adopts a network perspective. While the business network approach has been extensively employed in the fields of industrial marketing (Ghauri, 1999; Hakansson and Snehota, 1995) and international business (Forsgren et al., 2005; Johanson and Vahlne, 2003), there

are few studies applying this theoretical perspective to the study of MNCs and social actors (Hadjikhani and Ghauri, 2001). Therefore we extend the boundaries of network theory to analyse the relationship between MNCs and NGOs at the BOP.

This chapter is organized as follows. First, the literature related to the characteristics of the BOP, the challenges facing MNCs at the BOP and the collaboration of MNCs and NGOs at the BOP are briefly reviewed. Then we elaborate the network perspective and its dimensions that will be used in this study. After that the research method is described and the findings of the research presented. The chapter concludes with managerial implications, research limitations and future research directions.

### **MNCs, the BOP and NGOs**

Though MNCs benefit from a superior ability to confront a variety of challenges, evidence shows that being a large MNC does not necessarily guarantee success at the BOP. Specifically, the concept of doing business with the poor calls for additional focus and significant changes in business models (London and Hart, 2004). At the BOP, companies will not have access to the usual infrastructure and support systems. In contrast to the top of the economic pyramid, where corporations are concerned with willingness to consume (Hammond and Prahalad, 2004; London and Hart, 2004; Prahalad, 2004), consumers in low-income markets are often willing to use products but lack sufficient money to pay for them (Seelos and Mair, 2007). The income constraints of the poor present a severe challenge to MNCs, in terms of how they design their products and manage costs (Seelos and Mair, 2007). At the same time, MNCs are expected to bring world-class products, with corresponding quality and safety standards, to less developed economies. However providing high quality at a low price is not possible using traditional ways of doing business (Prahalad, 2009). A further challenge to the MNCs comes from the numerous, geographically dispersed villages without proper transportation infrastructures, which demands innovative strategies for the distribution of products and services (Velayudhan, 2007). The promotion of products also needs to be different, as illiteracy among many of the consumers in BOP markets constrains the use of print media (Velayudhan, 2007).

In addition, companies have to find solutions that will empower the poor and offer sustainable changes in their lifestyles (London et al., 2009), as poor communities will be more likely to embrace the products of those firms that not only serve them well but also improve their standard of living (Wood et al., 2008). Due to these characteristics of the BOP market, researchers have revealed that corporations addressing four particular aspects will be most successful in this market, namely awareness, affordability, availability and acceptability of products or services (Anderson and Billou, 2007).

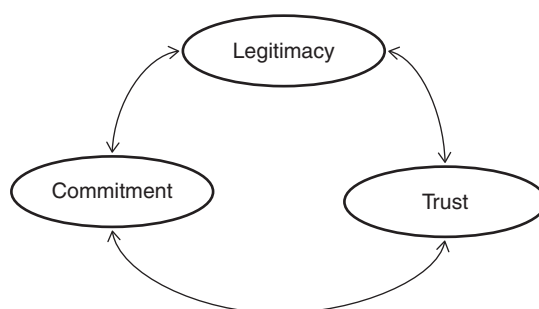
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As a result of these specific BOP conditions, many corporations have found collaboration with NGOs to be a helpful solution to the challenges embedded in this market (Hammond et al., 2007; London and Hart, 2010). London and Hart (2004) study a number of corporations at the BOP and highlight that successful firms have established relationships with non-traditional partners, including NGOs. Simanis and Hart (2009) examine product development at the BOP and report that innovation in this market should involve local NGOs. Perez-Aleman and Sandilands (2008) elaborate on how MNC-NGO partnerships benefit the poor and facilitate the inclusion of poorer producers in global supply chains. Doh and Teegen (2002) point out the role of NGOs in defining the institutional environment and influencing the interaction between businesses and other entities.

### Theoretical background

The theoretical perspective of this research goes beyond the business networks of MNCs and focuses on their non-traditional partners. This is in line with prior studies revealing that corporations are embedded in business networks as well as social-political networks that have proved crucial to the success of firms (Hadjikhani et al., 2008; Hadjikhani and Ghauri, 2001; Keillor and Hult, 2004). To explain the business relationships between MNCs and NGOs and how they impact on MNCs' entry into the BOP market, this research builds its argument upon three concepts: commitment, trust and legitimacy (see Figure 3.1).

The concepts of commitment and trust have been widely used by business network researchers (Hausman, 2001; Walter and Ritter, 2003). In addition, some researchers have suggested that legitimacy is a useful concept for examining the relationships between corporations and social and political partners (Hadjikhani et al.; O'Higgins and Morgan, 2006; Walter and Ritter, 2003). This is mainly because of the differences in the nature of relationships among



*Figure 3.1* Dimensions of the relationship

Source: based on Hadjikhani et al., 2008.

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business networks and socio-political networks. While technological and/or financial interdependency is the key reason for collaboration between business partners, they may be less relevant when corporations work with socio-political entities (Hadjikhani et al., 2008).

Legitimacy is defined as the perceived need to gain society's acceptance by complying with dominant norms, values and beliefs (Suchman, 1995). Accordingly, legitimacy is a socially constructed position of a firm recognized by its networks. Since legitimacy has become a critical issue for MNCs (Kostova and Zaheer, 1999), they are increasingly seeking new forms of legitimacy (Palazzo and Scherer, 2006) by entering into domains that have traditionally been considered the realm of governments or NGOs (Matten and Crane, 2005). By collaborating with them, and incorporating their expectations, MNCs can improve their legitimacy (DiMaggio and Powell, 1983) and as a result obtain and maintain the required resources (Oliver, 1991). At the BOP, MNCs can enhance their legitimacy by demonstrating how their initiatives can create mutual benefits for corporations, NGOs and ultimately the BOP population.

Commitment is defined as believing that an on-going relationship with another party is so important that the partners will make as much effort as possible to maintain it (Morgan and Hunt, 1994); that is, committed MNCs and NGOs believe their relationship is worth investing in, to ensure that it endures for a long time. Through their interactions with NGOs, MNCs can obtain information and experience about the BOP market and use that knowledge to enter the market themselves (Johanson and Vahlne, 1977). When MNCs increase their collaboration with NGOs, their perceived risk of investing in the market declines and their market commitment increases. The commitment of MNCs can be measured by the size of their tangible and intangible investments and their actions towards NGOs or other actors connected to them (e.g. BOP community) (Scott, 1994). Specifically, MNCs demonstrate their commitment when they invest in developing products or services for the BOP population and when they accept the long-term nature of their investment.

Trust, as the driving force behind commitment or an outcome of commitment, is defined as 'the firm's belief that another company will perform actions that will result in positive outcomes for the firm as well as not take unexpected actions that result in negative outcomes' (Anderson and Narus, 1990, p. 45). Trust is fostered when one party is confident of the other party's reliability and integrity, which is related to qualities such as competence, honesty, responsibility, helpfulness and benevolence (Morgan and Hunt, 1994). Han et al. (1993) suggest that perceived mutual trust is a principal characteristic of a good relationship. Rodríguez and Wilson (2002) note that trust is dependent on the goal congruency of the partners. Therefore, to improve the trust in their relationships with NGOs, MNCs have to pursue initiatives that will benefit the BOP population. MNCs use their resources to develop trust in the BOP and

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reach NGOs in order to gain special treatment (Hadjikhani and Ghauri, 2001). Commitment and trust dissuade exchange partners from sacrificing expected long-term benefits of working with existing partners for attractive short-term alternatives (Morgan and Hunt, 1994).

Trust in MNC–NGO relationships can affect the commitment and legitimacy in them. The higher the commitment between an MNC and an NGO, the higher will be the trust in the relationship and the legitimacy of the MNC.

### Research method

This study used a qualitative case study approach to explore the relationships between MNCs and NGOs at the BOP. Yin (2009) proposes using the case study method to understand real-life phenomena in depth, and also to understand important contextual conditions. A multiple case study approach was employed in this research to enhance the generalizability of the findings (Ghauri and Gronhaug, 2010; Stake, 1995). The study was conducted in India as the majority of the world's BOP population live in this country (Hammond et al., 2007) and an increasing number of MNCs are trying to enter the BOP market there. The MNCs selected for the research were all serving the needs of the BOP population through their products or services and had collaborated with NGOs in order to enter this market. In each MNC, we interviewed managers who were directly involved in the BOP projects of the firm. The number of interviewees in each company varied as we used snow ball sampling (Bryman, 2008). The use of multiple interviewees in each case can reduce subjective bias (Eisenhardt and Graebner, 2007). Additionally some of the NGO partners of the MNCs were identified and interviewees carried out. In total 13 interviews were conducted, 11 with MNCs and two with NGOs. Table 3.1 gives some information about the MNCs. The interviews were semi-structured and based on an interview guide addressing the theoretical concepts of this study.

Table 3.1 Overview of interviewed MNCs

Company	Year founded	Year of establishment of subsidiary in India	Field of activity	Revenue of MNC in 2010 (€ billion)	Number of employees in 2010
HR Consult	1960	1992	Human resources consultancy	14.2	27,500
Tel Co.	1985	2007	Mobile telecommunication	51	85,000

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In addition to the primary data collected from the interviews, we used secondary data for identification and corroboration purposes (Ghauri and Firth, 2009). The major sources of secondary data included company websites, company reports, articles from newspapers and magazines, videos of presentations by executives (e.g. press conferences or speeches) as well as other online sources. The collected data were analysed using pattern matching and systematic case comparisons (Yin, 2009, Ghauri and Gronhaug, 2005).

## MNC cases

### HR Consult

As a human resource consultancy, HR Consult provides a range of services, including regular temporary staffing and permanent in-house placements, search and selection, and human resource solutions. It registers the information of applicants who are looking for new jobs and collects a database of job opportunities in corporations. It then tries to match candidates to vacancies in companies, helping job seekers to find the best position and employers to identify the best talent for roles across various levels. The company also offers training to applicants to enhance their employability, and to corporations to improve their productivity.

In 2007, HR Consult decided to establish a foundation in India to employ its core capabilities and bring poor people out of poverty by increasing their earnings. In particular, the foundation aims to create sustainable change in the lives of children, women and youths from disadvantaged backgrounds. It focuses on several aspects of poverty but, for the purposes of this research, two will be discussed:

- (1) Providing empowerment and employability for women.
- (2) Building the capacities of NGOs that work at the grass-roots level.

First of all, the foundation aimed to empower disadvantaged women to earn extra money for their families and become more independent and self-reliant. As a starting point, HR Consult identified NGOs that were pursuing the same goal: namely, the empowerment of poor people. The company then invited NGOs to collaborate with it in offering entrepreneurial education to poor women. The aim of these simple training courses was to help the attendees to learn how to start a micro-business. Each year, the company donates part of its profits to the foundation. This has enabled the foundation to help micro-finance NGOs to provide loans to these disadvantaged women so that they can start their own businesses.

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Finally, building upon its database of available job opportunities, and the needs of different industries, HR Consult is offering training programmes to enhance disadvantaged groups' employability and marketable skills. These programmes are aimed at improving the skills and knowledge of youths and women to enable them to work for companies.

The foundation realized that, in order to scale up its initiatives, it would need the support and collaboration of NGOs. It therefore started another initiative to improve the visibility, connectivity and capacity of local grass-roots NGOs. It has created a facilitative platform where NGOs, companies and individuals with common social concerns can come together for mutual learning, sharing and the collective espousal of social causes. The programme is aimed at providing visibility, connectivity and capacity to NGOs working at the grass roots level. Currently, it has a strong network of 256 NGOs, 300 individuals and 14 corporations.

Since HR Consult is not pursuing any profits from these activities at this stage, and has aligned its goals with those of the NGOs, it is finding it easy to attract the trust of local NGOs. The investment of the company's resources, such as giving employees the opportunity to volunteer, offering free training to poor women and donating money to micro-finance NGOs, demonstrates the firm's commitment towards changing poor people's lives. Similarly, the NGO capacity-building initiatives have contributed significantly to strengthening the relationships between HR Consult and the NGOs. Finally, since HR Consult's activities at the BOP have enabled NGOs to achieve their goals of reducing poverty, and poor people to earn money and improve their lives, the company has gained legitimacy in the eyes of the NGOs and poor communities, and thus gained their support.

#### **Tel Co.**

Tel Co. is a global telecommunications company headquartered in Europe. It is one of the world's largest mobile companies in terms of revenue and number of subscribers. It operates in over 30 countries and has partner networks in more than 40 others.

As a mobile network provider, the activities of Tel Co. at the BOP are related to investing in disadvantaged areas to build mobile network infrastructure. The company also offers a variety of schemes aimed at making telephone conversations fairly affordable. However despite the low call rates, poor people were still unable to use mobile technology because they could not afford to purchase even the simplest handsets. Therefore the company decided to address this barrier by introducing a new affordable handset. In addition, to enable the poor to benefit from the advantages of mobile phones, and in order to increase

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its sales, Tel Co. invited micro-finance NGOs to work with it and offer loans for purchasing handsets. In the words of one of the managers:

We are working with micro-finance organizations that are also NGOs. They give people financing or rural consumer financing for very small purchases such as Rupees 300, Rupees 500; they get Rupees 50 per month or Rupees 20 per month as a kind of pay back. So we do have that kind of arrangement in some places where these groups exist, where we get them to fund the purchase of our handsets or our service, and we educate them through this.

Another challenge was the distribution of mobile phones and a system for adding credit to them. For this, the company decided to seek the help of NGOs, asking them to put them in touch with poor women from their self-help groups. The company then trained these women in commercial operations. They now work as representatives for the firm and sell mobile services in their villages. This strategy has led to the opening of many mini-stores to provide mobile services in a number of widely dispersed areas.

Another challenge that Tel Co. faced at the BOP came from the lack of infrastructure and widespread illiteracy among people in rural areas. Because of the former, the reach of media such as cable TV and satellite was very low. As a result, the company could not advertise its products and services using the methods common in urban areas, mainly TV advertisements. Meanwhile, illiteracy meant that flyers and newspapers would be ineffective. Therefore communication had to be mostly verbal or visual, which required extensive physical reach into rural areas. So, the company developed several short audio-visual films showing a villager becoming an entrepreneur and creating a small company through his access to mobile communication methods. These films were shown at village gatherings, and helped the company build great awareness of its services and the benefits they could bring to the lives of the villagers.

Tel Co. also understood that offering mobile technology is not enough at the BOP, as people are constrained by their low incomes. Therefore, in collaboration with NGOs, the company started to educate people about how they could develop micro-enterprises based on mobile communication. In partnership with its distributors, the company is also taking vans into rural villages and educating rural consumers about how mobile technology can enhance the social and economic lives of the poor. One of the interviewees described the thinking behind this idea:

We go and show the rural people how mobile telephones can make their lives more comfortable, can help them grow in their businesses and help them keep in touch with loved ones living in the towns, and that is something that will help them grow as individuals and in their financial lives.

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In this case, the trust in the relationship between Tel Co. and the NGOs developed through the alignment of their goals and the resulting creation of mutual value. Tel Co. aimed to enter the BOP market by selling its handsets and mobile network to the BOP population and encouraging people to use mobile phones. Meanwhile the NGOs were trying to help women find a way out of poverty, through self-help groups. As a result, when Tel Co. suggested making these women sales representatives, the idea was very much welcomed by the NGOs.

Tel Co. also demonstrated its commitment to the BOP population by investing resources in building infrastructure in rural areas, and bringing the advantages of mobile phones to the poor. The company also invested in training poor women to work as its sale representatives. These contributions, in providing jobs for poor women and improving the lives of those on low incomes by giving them access to mobile phones, has brought about a higher acceptance of Tel Co.'s initiatives at the BOP and legitimacy for the firm.

### Discussion

The case studies in this research highlight the necessity of establishing relationships with actors outside traditional business networks in order to achieve business goals. This is in line with prior studies expressing the need to include social actors in MNCs' networks (Hadjikhani et al., 2008), especially at the BOP (London et al., 2004; London and Hart, 2004). However this research adds to the previous understanding by elaborating on the role that establishing relationships with NGOs plays in helping MNCs to enter the BOP market. A summary of the MNC-NGO relationships and how they facilitated the case MNCs' entry to the BOP is presented in Table 3.2.

The establishment of trust among the MNCs and NGOs also improved the commitment of both. The MNCs' market entry into the BOP created benefits for the NGOs and the BOP, which strengthened the NGOs' commitment to the relationships. This is in line with the findings of Morgan and Hunt (1994), highlighting that in a committed relationship each party will invest in maintaining the relationship. The findings of this research also confirm the necessity of establishing a win-win relationship at the BOP, as suggested by international business scholars in the past few years (London et al., 2010; London and Hart, 2004; Prahalad, 2009).

By contributing to the reduction of poverty and the enhancement of poor people's lives, companies' initiatives at the BOP will be more easily accepted and the organizations will increase their legitimacy (Bowen et al., 2010; Chen and Roberts, 2010). In line with prior understandings, the MNC cases in this research engaged in several initiatives to improve their legitimacy. Both Tel Co. and HR Consult attempted to understand the real needs of the poor people in their target markets and to incorporate the NGOs' aims to improve the lives of

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*Table 3.2* Summary of the MNC–NGO relationships and their role in the BOP market entry of the MNCs In line with prior studies ( Anderson et al., 1994; Rodríguez and Wilson, 2002), the findings of this research illustrate that defining mutually beneficial goals can strengthen trust in a relationship. Both of the case companies in this study pursued this strategy and designed their entry into the BOP in such a way that also allowed NGOs to achieve their social goals, improving the lives of the BOP population. HR Consult provided education and training skills for the poor to enhance their employability chances. Tel Co. offered jobs to poor women whom the NGOs were already trying to help. In collaboration with NGOs, Tel Co. also developed some business ideas based on the use of mobile phones, to improve micro-entrepreneurship among the poor.

	HR Consult	Tel Co.
Initiatives for building trust	<ul style="list-style-type: none"> <li>– Offering non-profit initiatives</li> <li>– Offering solutions to increase the earnings of poor women (training workshops to start a micro-enterprise, developing poor women’s skills to improve their employability) (Alignment of HR Consult’s goals with those of the NGOs)</li> </ul>	<ul style="list-style-type: none"> <li>– Bringing the advantages of mobile phones to poor communities</li> <li>– Offering job creation for self-help group women (Alignment of Tel Co.’s goals with those of the NGOs)</li> </ul>
Initiatives for demonstrating commitment	<ul style="list-style-type: none"> <li>– Dedicating resources to the provision of training workshops for poor women</li> <li>– The donation of money to microfinance NGOs to support the poor in the starting of micro-enterprises</li> <li>– Dedicating resources to building the capacity of NGOs</li> </ul>	<ul style="list-style-type: none"> <li>– Developing the telecommunication infrastructure in rural areas of India</li> <li>– Developing an affordable handset</li> <li>– Training women to establish micro-enterprises</li> </ul>
Enhancement of legitimacy	<ul style="list-style-type: none"> <li>– Reducing poverty by generating incomes for poor women</li> <li>– Enhancing the employability of the poor</li> <li>– Building the capacity of the NGOs</li> <li>– Obtaining support from the NGOs to scale up the initiatives at the BOP</li> </ul>	<ul style="list-style-type: none"> <li>– Empowerment of self-help group women</li> <li>– Providing access to mobile phones in rural areas</li> <li>– Obtaining the support of NGOs for Tel Co.’s initiatives at the BOP</li> </ul>
Consequences of building relationships with NGOs and BOP market entry	<ul style="list-style-type: none"> <li>– The NGOs helped HR Consult to gain access to the BOP communities, offering training workshops and scaling up initiatives</li> </ul>	<ul style="list-style-type: none"> <li>– The NGOs encouraged women form their self-help groups to work as the firm’s sales representatives</li> <li>– The NGOs provided microfinance for the purchase of handsets</li> </ul>

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these people. HR Consult, for example, offered training to improve the earnings of the poor, either through increasing their employability or their chances of starting new micro-businesses. In addition, HR Consult's investment in the capacity of the NGOs, which were then able to help the company to scale up its activities, enhanced its acceptability among both the poor and the NGOs. Tel Co., in addition to offering an affordable handset, sought the collaboration of micro-finance NGOs in giving loans to the poor to purchase these handsets. Changing the lives of the poor by suggesting ways they could earn money using their mobile phones also made the company's activities more acceptable at the BOP.

### Conclusion

This research sought to reveal how the collaboration of MNCs and NGOs at the BOP can contribute to the market entry of MNCs. We adopted network theory and highlighted the necessity of developing trust, commitment and legitimacy in the relationships between MNCs and NGOs, and provided some insights, based on our empirical findings, into how these factors can facilitate the entry of MNCs into the BOP.

The findings of this research contribute to theory by extending the boundaries of business to non-business networks and providing a theoretical understanding of the interaction between MNCs and NGOs at the BOP. Therefore the findings corroborate prior studies emphasizing the necessity of incorporating social actors in the analysis of MNCs' behaviour (Hadjikhani et al., 2008; Hadjikhani and Ghauri, 2001).

This research also has several implications for the managers of both MNCs and NGOs. The findings reveal that entering the BOP market requires different strategies and MNCs should learn to collaborate with NGOs and seek their help and advice. They should first develop trust, illustrate their commitment and improve their legitimacy in the eyes of the NGOs and then the BOP population. NGOs should also appreciate the contribution MNCs can make to improving the lives of the poor and collaborate with them to develop products and services that meet the specific unmet needs of the poor.

This research is not without limitations. Like any other qualitative study, the generalizability of the findings is limited. Future studies can thus focus on the BOP in different countries, and collaborations between MNCs and NGOs in a variety of industries and on a larger scale.

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