Spotlight: Can entre*preneurs* save the world?

A *new alliance* for global *change*

Working together, corporations and social entrepreneurs can reshape industries and solve the world's toughest problems. This article was first published by Harvard Business Review in 2010

By Bill Drayton and Valeria Budinich

Idea in Brief

The time is ripe for collaboration between for-profit businesses and mission-driven individuals and organizations. By forming "hybrid value chains" the for-profit and citizen sectors can together remake global economies and create lasting social change. Businesses offer scale, expertise in operations, and financing. Social entrepreneurs offer lower costs, strong social networks, and a deeper understanding of customers and communities. Example: Local citizen groups helped to persuade Amanco, a maker of water-conveyance products, that small farmers in Mexico represented a significant market opportunity. They partnered with the company to organize farmers into loan groups, promote irrigation technologies, and even install systems. The social entrepreneurs are helping the farmers get financing so that they can afford Amanco's products. This newly created drip irrigation market is worth about $56 million a year – and farmers are enjoying higher yields.

WE ARE witnessing a sea change in the way society's problems are solved, work is performed, and businesses grow. Collaborations between corporations and social entrepreneurs can create and expand markets on a scale not seen since the Industrial Revolution. These markets will reach everyone, but especially the 4 billion people who are not yet part of the world's formal economy. They will offer new and remarkable products and services in sectors as diverse as education, transportation, and finance.

You may be skeptical of this claim, and with good reason. The citizen sector—the term we use to define the millions of groups established and run by mission-minded individuals across the globe who are attempting to address critical social needs—has long been regarded as understaffed and inefficient. But that has changed. We work with some 3,000 social entrepreneurs worldwide, and over the past 30 years we've seen the citizen sector catch up with business as it has increased its productivity, size, and reach. Its organizations are attracting talented and creative leaders, and their work is changing the game in critical industries and areas such as energy and health care.

For-profit organizations today have an opportunity to collaborate with citizen-sector organizations (CSOs) on large-scale problems that neither group has been able to solve on its own. The power of such partnerships lies in the complementary strengths of the participants: Businesses offer scale, expertise in manufacturing and operations, and financing. Social entrepreneurs and organizations contribute lower costs, strong social networks, and deep insights into customers and communities.

But to work together effectively, they must focus on creating real economic as well as social value. We believe they can do so by forming what we call hybrid value chains (HVCs), which capitalize on those complementary strengths to increase benefits and lower costs. This trend has been developing for years, and we've participated in pilot projects that have delivered impressive results and promise extraordinary growth. HVCs can now be found in many industries all over the world. Collaboration between corporations and CSOs has reached a tipping point: It is becoming standard operating procedure. Indeed, we believe that if you're not thinking about such collaboration, you'll soon be guilty of strategy malpractice.

The *vibrancy* of the citizen *sector*

Before we explore the inner workings of hybrid value chains, it may be helpful to look at how we got here. In the 1700s business became entrepreneurial. Upstarts devising faster and more-efficient ways to produce goods ushered in the Industrial Revolution. They introduced innovation after innovation, ultimately changing the world. After remaining flat for a millennium, per capita income in the West rose by an average of 20% in the 1700s, 200% in the 1800s, and 740% in the past century. But while the for-profit sector enjoyed sweeping progress, the citizen sector languished. It faced little outside market pressure and relied heavily on funding from governments that, as monopolies, feared competition. CSOs felt little push to innovate; as a result, they fell far behind in productivity, performance, pay rates, confidence, and reputation.

By 1980 the imbalance between the business and social sectors of society had become intolerable. (We had great TVs but lousy education.) New opportunities emerged across the world (except where governments got in the way), and the citizen sector restructured itself to become entrepreneurial and competitive. It rapidly increased productivity and scale, lowering the cost of goods and services it provided relative to business's offerings.

Since then, the citizen sector has been creating jobs about three times as fast as have other employers in the Organisation for Economic Co-operation and Development countries. In Brazil the number of CSOs rose from about 36,000 to nearly a million over the past 20 years. In the United States their number has grown by more than 300% since 1982. Today millions of these groups attract talented individuals who long for challenging and lucrative work that is consistent with their personal values and goals.

Take David Green, who helped start Aurolab, an India-based nonprofit that produces intraocular lenses to restore sight to cataract patients. It has managed to reduce the price of lenses from $300 to $10 or less, by using emerging technology and restructuring its manufacturing costs. Aurolab is the manufacturing division of Aravind Eye Hospitals, which charge patients for the lenses on a sliding scale depending on their income. It has captured about 8% of the global intraocular lens market and sells about 1.5 million such lenses each year in 109 countries. Green, working with Ashoka, the International Agency for the Prevention of Blindness, and Deutsche Bank, has also launched The Eye Fund, a $15 million loan fund that will enable eye-care groups to grow far faster than they otherwise could, significantly speeding the reduction of blindness.

Or consider Rodrigo Baggio, who created a chain of computer schools serving hundreds of slums across Latin America and Asia. He persuaded one organization after another to donate, warehouse, and transport their used computers, and thousands of slum dwellers to set up and run the schools. These schools now boast some 700,000 graduates.

We could go on and on. But our point is that many social entrepreneurs are already out there changing the world—and businesses have largely been overlooking them. It was previously safe to ignore the citizen sector, because this segment of the economy was relatively small in scale and low in productivity. That's no longer true. The companies that work with and learn from the sector and its leaders will reach large new markets. They will also gain competitive advantage from new business models and first-mover benefits.

The time is ripe for collaboration because the two sectors are now equally innovative. Together they can promote changes as powerful and widespread as those produced by the Industrial Revolution.

Hybrid *value chains*

Hybrid value chains represent a systemic shift in the way businesses and CSOs interact. They are collaborations that redefine value in gamechanging ways, with each side clearly understanding (and willingly accepting) the risks and rewards.

Consider the housing industry. Currently, one-sixth of the world's population lives in slums and squatter cities. That's a billion people who are shut out of the formal housing market. If you're a cement company, a tile maker, a brick manufacturer, a banker, a developer, or a utility, just think: What would it mean for your business if you could unlock the potential of a trillion-dollar housing market? Until recently, that was nearly impossible, because the business world acting alone—with its existing cost structures and limited understanding of local markets—could not reach those customers. Nor, for their part, had governments or CSOs figured out how to serve them. But look what happened when a forprofit ceramic tile maker partnered with a South American CSO.

Colcerámica (a Colombian subsidiary of Corona, one of the largest building-materials retailers in South America) wanted to learn more about the low-income market for ceramics and home products. We introduced the company's executives to Haidy Duque, a cofounder of Kairos, which grew out of a humanrights organization that works with people displaced by armed conflict. They collaborated on market research and developed a business plan.

Colcerámica provided the product — its Iberica tile line — and the technical and business know-how (sales and marketing techniques, for instance). Kairos, in return for fees, recruited and >

managed a female sales force. That model generated income for previously unemployed women and pushed the product into the hands of potential customers, rather than waiting for a storefront to pull them in. It reduced Colcerámica's distribution costs by a third, so the company could afford to pay a percentage of its profits to the women sales promoters and community partners. Other local CSOs performed administrative functions in return for a percentage of revenues, which they reinvested in community projects.

→ What would it mean for your business if you could unlock the potential of a trillion dollar housing market?

The program, now called Viste Tu Casa (Dress Your Home), launched in January 2006. In 2009 its sales reached nearly $12 million as it expanded to five of the six largest cities in Colombia, in partnership with five CSOs. It has helped more than 28,000 families improve their living conditions, and 179 saleswomen are each earning $230 a month. In India, Ashoka is working with mortgage companies, for-profit housing developers, and local citizen-sector groups to create a thriving housing market—delivering affordable new apartments for the "informal" members of the local workforce. These consumers often have a steady source of income but lack proof of stability and therefore are ineligible for mortgage loans. India's housing deficit has been conservatively estimated at about 24.7 million homes—perhaps the largest potential housing market in the world. And that doesn't include what will be needed as more than 700 million Indians move from villages to cities. Within this new-construction HVC, CSOs can serve as demand aggregators, bringing groups of consumers to for-profit developers, or as full design and investment partners. More than 2,500 homes are being built, with the promise of another 7,500 within the next 18 months—representing more than $100 million in sales.

Agriculture is another market that profits from hybrid value chains. Consider drip-irrigation systems in Mexico, where more than 2 million small farmers live on less than $2 a day and work, on average, fewer than five hectares (about 12 acres) of land. Most companies believe it isn't cost-effective to serve such low-income consumers. But Ashoka and local citizen groups persuaded Amanco, a maker of waterconveyance products, otherwise. Viewing these farmers as a significant market opportunity, it is reengineering its business model to increase the value of small individual transactions. CSOs are critical to this effort: They organize farmers in loan groups, promote irrigation technologies, and even install systems. They also help the farmers gain access to consumer financing so that they can afford Amanco's products. This newly created drip-irrigation market is estimated to be worth $56 million a year. The customers have become moreefficient farmers and enjoy higher and morecertain yields of multiple crops, sometimes tripling their prior income.

A *Win-Win-Win* proposition

Businesses that enter into HVCs can expect three kinds of return on their investments:

Profits.

HVCs unleash many opportunities for growth. For example, on the basis of their joint research, Ashoka and the consulting firm Hystra estimate that a $553 billion market exists for safe, clean, and affordable energy for low-income consumers. Moreover, if a business can construct an HVC to profitably serve lower-income consumers, it can often provide those services to higher-income consumers as well.

Knowledge.

Companies that pioneer HVCs will run up the learning curve, leaving competitors behind. And as they gain experience, they can carry their new knowledge into different environments. In "How GE Is Disrupting Itself" (HBR October 2009), Jeffrey R. Immelt, Vijay Govindarajan, and Chris Trimble write: "Success in developing countries is a prerequisite for continued vitality in developed ones." GE is pushing to "reverse innovate" products in emerging markets because they can "create brand-new markets in the developed world—by establishing dramatically lower price points or pioneering new applications." When designed correctly, HVCs, too, can be a prime source of such disruptive offerings.

Talent.

HVCs require entrepreneurs who can spot opportunities, devise creative solutions, and collaborate with a diverse group of partners. They give companies a chance to identify and encourage talented leaders. They also attract progressive thinkers and increase commitment to employers, because working on this new frontier of business is exciting, socially relevant, and challenging.

CSOs will gain at least as much, beginning with access to cheaper capital. McKinsey estimates that philanthropic capital actually costs those seeking it anywhere from 25% to 40% of what they get, once the expense of pursuing grants is factored in. Capital from for-profit finance firms typically costs 2% to 5%—and, surprisingly, business sources are much more patient. Customers, too, benefit greatly from an HVC. They get lower-cost access to high-quality products, from building materials to medical diagnostic kits.

→ It's time the finance industry developed smart ways to invest in the world and those who want to change it.

CSOs, especially early actors, will take market share from other CSOs that can't provide the same goods or services. This will allow them to scale up, driving costs down further. The profits from an HVC can be reinvested in the group's work or used to subsidize those who can't pay full price for the service or product. CSOs will attract and retain talented people who want their work to make a positive difference on a large scale. And, last but not least, CSOs will vastly improve the lives of the people they sought to help in the first place. Not every situation calls for an HVC, of course. Three kinds of opportunities are particularly ripe for this form of business strategy:

When the *citizen sector* is large and *growing* fast.

Ashoka estimates that the global low income health care market is now worth $202 billion but will grow exponentially because of emerging business and social innovations. The global low-income food market is even more immense: a fast-growing $3.6 trillion. Any entrepreneur's heart would beat faster thinking about all this untapped potential.

When *market values* are *changing* dramatically.

In markets such as energy and the environment, customers are often asked to make big compromises because existing business models are inflexible. HVCs can help organizations figure out ways to lessen those compromises. For instance, in many parts of India people use stoves fueled by kerosene or wood to cook and to heat their homes, at great cost to both their personal health and the environment. On the advice of the late C.K. Prahalad, BP partnered with local manufacturers and two Indian Ashoka fellows, Muthu Velayutham and Prema Gopalan, to manufacture and sell biofuel for stoves. Users' monthly energy costs dropped, as did their exposure to indoor smoke. Although this business is still in its infancy, the goal is to reach 20 million households in rural India by 2020. BP has decided not to continue, because it considers the business outside its core product line, but local Indian companies in partnership with CSOs and rural retailers have stepped in to fill the gap.

When *charitable funding* and "free services" can *be replaced* with genuine markets.

Innovative pricing and new approaches can lead to goods and services that deliver both traditional and new value. Microcredit comes to mind: Thanks to the work of Grameen Bank and similar lending organizations worldwide, microborrowers have been able to create their own businesses—spurring economic growth in their communities—while generating a multibillion-dollar finance industry.

Con*structing* a *hybrid* value chain

From our experience devising HVCs and working with organizations involved in them, we offer the following advice to executives who are ready to build their own:

Ask *hard questions* about how the business is *currently done.*

The value chain concept, developed simultaneously in the 1980s by Michael Porter and a group of McKinsey consultants, replaced a framework called the business system, which essentially created a product, made it, and sold it. The value chain involves choosing, providing, and communicating the value. It forces managers and strategists to examine the relationship between benefits and price. It pushes executives to think deeply about how customers define price: Do they focus on purchase price or lifetime costs? How price sensitive are different segments?

How elastic is demand? These are all critical questions for the would-be creator of a hybrid value chain. Organizations considering one must think holistically about their business strategy and the industry they're in.

Reconceive value *along multiple dimensions* to find new *markets.*

The for-profit Healthpoint Services, incubated at Ashoka, brings together Indian businesses, citizen-sector groups, and for-profit venture capital and social funds to deliver modern, evidence-based health care to rural villages in India. Its clinics, called E Health Points, use telemedicine—video technology and electronic medical records—so that patients don't have to travel for a day or more (and sacrifice income during that time) to reach a doctor.

The clinics keep costs low for patients with a combination of advanced point-of-care diagnostics, generic drugs, and careful local staffing. Consultations are just $1. Many diagnostic tests cost less than 50 cents; none costs more than $4. The clinics also provide clean drinking and cooking water on a monthly subscription basis at a cost of roughly 5 cents a day per household. And when customers come to collect their water, staffers take the opportunity to raise awareness of health issues and early prevention. On the basis of initial success, the finance minister for Punjab has asked that 600 € Health Points be built in that state. >

Models like this can be exported to many countries, including developed ones, turning scarcity into abundance. Healthpoint already has pilots planned in Southeast Asia and Latin America. For its target market, the scarcity was access to services: Most patients in rural areas lacked transportation and needed to work long hours. By putting clinics nearby and using technology to bring doctors to patients, Healthpoint unlocked latent demand, showing that even low-income consumers are willing to pay for quality services.

A *huge market*, and not just at the bottom

What's the value of the untapped markets that might be reached by hybrid value chains? If we consider only low-income consumers, it was more than $6 trillion (in international dollars) in 2005, according to a pioneering study by the World Resources Institute and the International Finance Corporation. Market opportunities in emerging economies have increased sharply since then, because of rising populations and incomes in India, China, Brazil, and elsewhere. A conservative estimate is that these markets have grown 5% annually since 2005. The bulk of the total value comes from:

$ 202 billion market for health care

$ 424 billion market for low-cost housing

$ 553 billion market for energy

$ 3.6 trillion market for agricultural products and food

These markets are all much larger than the oft-touted and explosive one for mobile telephony among low-income populations – and the potential market for HVCs overall certainly exceeds their total value, because HVCs can spread across the economic spectrum. Consider the need for improved education and health care among the urban middle classes in developing countries, or the demand for lower-cost health care, more-nutritional food, and affordable housing in wealthy countries like the United States.

Look for *pricing* and *financing* innovations.

This is a critical point. Just like businesses, HVCs need different types of capital at different stages of their life cycles. They may need up-front seed money, but sooner rather than later, customers will have to pay for the product or service they're receiving. And designers of HVCs will have to come up with appropriate financing solutions. They may work with nontraditional partners—some utility companies, for instance, provide "retail" financing at relatively low risk because they are close to their customers—or they may need to work with the usual suspects in unusual ways: The Indian company Selco brought its $400 solar home-lighting system within reach of customers by working with banks and microfinance institutions to help the lenders understand how solar products increase productivity. Other organizations turn to leasing models.

Commercial microcredit funds are an early (if small) example of how the finance industry profitably provides direct investments in citizensector work. The industry can do so because there are 120 to 150 large, well-established microcredit lenders in whose sec rities these funds can safely invest large sums without incurring significant expense.

Financial institutions will have many attractive opportunities to invest in markets created by hybrid value chains. Indeed, HVCs present a huge opportunity for the finance industry. Here is why: First, because HVCs are *businesses,* they are both stable and easily understood by businesspeople. Second, HVCs with successful financing structures can generate what finance firms love—millions of loans that have low transaction costs and low to moderate risk. (Such financing structures themselves are commonly HVCs: CSOs make the loans and sell them to bankers.)

Third, packaging these loans allows financial companies to give their clients a choice among significant social impacts (from housing to education) and locations (from Brazil to Poland) along with solid returns. At least for early movers, the ability to offer so much choice will confer a competitive advantage.

It's time for the finance industry to develop smart ways for clients to invest in the world and the people who want to change it. Right now, those investors are limited to foundations and various kinds of "impact philanthropy." Individuals and institutions should instead be able to invest in financial products that deliver solid returns and enable people to irrigate their land, rebuild their homes, educate their children, and transport products to market. Investors should be able to weigh their risks and rewards on the basis of financial as well as other returns they value.

Organize to innovate.

Two distinct innovation challenges arise when building HVCs – finding good ideas and developing business models to deliver them at scale. Ideas are everywhere, of course, but they increasingly come from emerging markets. Mukesh Ambani, the chairman and managing director of Reliance Industries, says, "Twenty years from now we will not talk about garages in Silicon Valley. We will talk about projects in rural areas of India, which are then scaled all over the world." The Ashoka-Lemelson Fellows program has identified 100 inventor-entrepreneurs, largely from developing countries, who have launched social enterprises in clean energy, mobile technology, water and sanitation, and many other areas. We've already mentioned that GE and others have learned to reverse-innovate products designed for emerging markets. Keeping a close eye on these markets is a good first step.

Because HVCs are still evolving, there's no single formula for success. But experience has taught us some lessons about the second challenge— developing business models. We know, for instance, that companies wrestle with where to house their hybrid ventures. We recommend not categorizing such efforts as corporate social responsibility, because the CSR arms of most companies focus on doing good and demonstrating impact but are rarely asked to generate healthy returns.

Appoint a leader.

HVCs, which start as constellations of potential players, are not selforganizing. Someone must take the lead and decide who is in and who is out. Because HVCs are a pathway to explosive growth, both partners—corporations and CSOs—will want to assign talented executives to the opportunity. Those people must be patient, persistent, and able to earn the trust of all the actors—that is, they must be empathetic, good at team building, and willing to work directly both across sectors and with unfamiliar suppliers and customers. A corporate intrapreneur or the head of a CSO might lead the team—whoever it is, he or she will have to manage lots of complex moving pieces as the HVC forms.

Give the *team time* and *permission* to fail.

Organizations can afford to tolerate missteps and failures when the goal is to exploit an immense opportunity. Learning what doesn't work will move them one step closer to discovering what does. Of course, results are important—sooner or later the business model needs to show that it can be profitable and scalable. It's critical to strike a balance between being patient and being demanding. Remember Tracy Kidder's marvelous book The Soul of a New Machine, about a project team and its race to develop a new computer? Forming a hybrid value chain is a similar story:

It involves a relentless team of players who are ready to welcome risks and challenges because they believe strongly that what they are doing is not only about profits but also about human progress.

Many people today have the sense that as change accelerates, the world's problems are multiplying faster than solutions. Slums are growing daily; affordable and sustainable energy is elusive; we are failing to provide adequate health care for many citizens. Whatever the issue may be, we believe that the most powerful and profitable answer is often a new form of partnership between business and the citizen sector, which is now composed of millions of competent and competitive organizations, often led by entrepreneurs. The more eyes we have on society's problems–and opportunities– the better our chances of coming up with viable solutions.

The *four criteria* for an *HVC*

Hybrid value chains can transform industries and create whole new ones if they meet these criteria:

1. The business has the potential to be large in scale and to cross borders. The best HVCs will have enormous impact, not only on a company's bottom line but on millions of lives.

2. For-profits and social entrepreneurs work together to create multiple kinds of value. Companies and citizen sector organizations capitalize on their particular areas of expertise to deliver a valuable product or service that neither partner could provide on its own.

3. Consumers—broadly defined—pay for the product or service. This is not charity work or a CSR project. Sustainability and scalability rest on profitability.

4. A system-changing idea provides the basis for new competition. Muhammad Yunus's microcredit idea of 30 years ago has been expanded to include health care and insurance products as well as financial services.

→ Bill Drayton
CEO & Founder of Ashoka

→ Valeria Budinich
Chief Entrepreneur of Full Economic Citizenship Initiative