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How the environment affects opportunity recognition by entrepreneurs at the bottom of the pyramid

Abstract

There is an army of bottom of the pyramid entrepreneurs (BOPE) who have the potential to transform developing economies, if they can identify and exploit business opportunities. BOPE could have unidentified resources that could lead to the recognition of radical new opportunities. This study paper asks how environmental factors and identification of resources affect Opportunity Recognition by BOP entrepreneurs in developing economies. To investigate this research question we conduct a literature review and plan semi-structured interviews of existing and nascent entrepreneurs in the largest and arguably the poorest country in Africa, the Democratic Republic of the Congo. In this paper we review the context of BOPE and describe the methodology we will use to gather and analyse data. Finally, we describe our access to suitable respondents for this study and how it will be conducted.

How the environment affects opportunity recognition by entrepreneurs at the bottom of the pyramid

In 2001 45% (2.7 billion) of the world's population of approximately 6.1 billion lived in 'moderate poverty' on less than US $ 2 per person per day (World Population Summary, 2012). With the reported success of microfinance, increasingly we are looking towards entrepreneurship to help lift developing countries out of poverty (Alverez, 2012). While some large corporations are identifying and exploiting business opportunities at the 'bottom of the pyramid' (BOP) (Prahalad, 2007), there is an army of bottom of the pyramid entrepreneurs (BOPE) who have the potential to transform developing economies, if they can identify and exploit business opportunities.

Kelliher and Leana reviewed literature on micro-businesses and propose that micro-firms are highly sensitive to their macro environments due to their limited competitive influence, but they also propose that "organisational performance is a consequence of firm-specific resources and capabilities enabled by management competencies, as internal resource availability places a fundamental limit on an organisation's plans, regardless of those resources obtainable on the open market" (2009, p525). This indicates that the BOP entrepreneur (BOPE) is limited by his or her resources, capabilities and management competencies in addition to any limitations imposed by the business environment at the bottom of the pyramid. But BOPEs could have unidentified resources that could lead to the recognition of radical new opportunities.

Opportunity recognition (OpR) is central to entrepreneurship. Shane and Venkataraman define entrepreneurship as the scholarly examination of the way opportunities to create goods and services are discovered, evaluated and exploited (2000). OpR is proposed to have five basic elements (Csikszentmihalyi, 1996): preparation, incubation and insight relate to discovery of the opportunity, and elaboration and evaluation relate to the formation of the opportunity. The preparation stage includes the gaining of experience, expertise and other resources needed to identify the opportunity as relevant and attractive. The incubation stage is the consideration of options and alternatives, and the insight stage is when the potential of the opportunity is consciously recognized. Identification of assets is part of preparation, the first stage of opportunity recognition. Failure to identify available assets could mean failure to identify attractive opportunities.

When a business opportunity has been identified, the opportunity evaluation and elaboration stages (Csikszentmihalyi, 1996) consider if the opportunity is sufficiently attractive to pursue. One technique is to conduct a PESTLE analysis. PESTLE is a review of the political, economic, social, technological and environmental contexts to identify how to best position the nascent enterprise and to evaluate its chances of success. The PESTLE analysis are likely to be quite different in a developing economy, which means that opportunities identified and evaluation of their chances of success are likely to be quite different in developing economies.

Thousands of papers and books have been written about opportunities for corporations to target BOP markets in developing countries (Prahalad, 2007), but are there also opportunities for those living at the BOP with meagre resources? Can BOPE identify opportunities in the challenging PESTLE environment of a developing economy without the financial, human and social assets of large corporate enterprises?

This study paper asks how environmental factors and identification of resources affect OpR by BOP entrepreneurs in developing economies.

To investigate this research question we conduct a literature review and semi-structured interviews of existing and nascent entrepreneurs in the largest and arguably the poorest country in Africa, the Democratic Republic of the Congo (DRC). The study shall gather information about the BOPE's financial, social and human capital assets and their perceptions of the PESTLE factors, which include infrastructure and market conditions, such as demand and competition.

In this paper we review the context of BOPE and describe the methodology we will use to gather and analyse data. Finally, we describe our access to suitable respondents for this study and how it will be conducted.

Literature Review

In this section we review literature on the business environment at the BOP and its effects on asset identification and opportunity recognition by BOPEs.

The World Bank's "Voices of the Poor," based on research with over 20,000 poor people in 23 countries, identifies a range of factors, which poor people identify as part of poverty. These include:

- Precarious livelihoods
- Excluded locations
- Physical limitations
- Gender relationships
- Problems in social relationships
- Lack of security
- Abuse by those in power
- Dis-empowering institutions
- Limited capabilities
- Weak community organizations.

Entrepreneurial performance is contingent upon environmental variable such as dynamism, munificence, complexity, competitiveness and other industry characteristics (Lumpkin & Dess, 1996). When the environment is more competitive, opportunities are more likely to be exploited, resulting in better performance. When the environment is munificent, however, there is less motivation to exploit new opportunities. Hence the environment at the bottom of the pyramid could in some ways be conducive to greater OpR.

Our review of the business context is structured by the PESTLE analysis. The PESTLE analysis is a review of the political, economic, social, technological, legislative, environmental and ethical forces affecting a business' which recognizes that the business's environmental factors are critical to business success.

Political Factors: Economic Development in reverse - The impact of civil unrest on the economy

Many countries are in poverty because they have experienced or are experiencing some form of manmade disaster, such as civil war. Studies indicate that the occurrence of armed conflict is on the rise since World War II (Ground, 2006, Collier et al, 2003). Ground (2006) estimates that armed conflicts have increased from fewer than 20 per year in 1946 to more than 30 per year in 2003, although the number has reduced from a peak of over 50 per year in 1992. This research indicates that internal conflicts, from civil unrest to civil war, are by far greater in number than external conflicts, such as war with neighbouring countries.

Collier and colleagues propose that civil war can be conceptualized as "development in reverse" (2003, p. 2). Military actions, such as a war or civil war, typically results in numerous deaths and injuries, dislocation of entire communities from their natural habitat, which they have known as the only means of survival, destruction of infrastructure, including governing bodies, transportation and agriculture, and disruption of business and services. This can lead to wide spread unemployment and sometimes starvation.

Poverty

The World Bank in their (year) report defines extreme poverty as living on less than US $1.25 (PPP) per day, and *moderate poverty* as less than US $2 or US $5 a day (but note that a person or family with access to subsistence resources, e.g. subsistence farmers, may have a low cash income without a correspondingly low standard of living – they are not living "on" their cash income but using it as a top up). It estimates that "in 2001, 1.1 billion people had consumption levels below $1 a day and 2.7 billion lived on less than US $2 a day."[6]

An interesting dichotomy exists in the business environment during and after a civil war. On one hand there are extraordinarily high levels of demand, which could be summarized by saying "everyone needs everything". People need food, medical supplies, housing, security and even luxury items. But high unemployment and disruption of markets means that relatively few consumers or surviving businesses will have effective demand, in other words demand that is backed by the ability to pay. Thus, businesses face high demand and can charge higher prices, if they find customers who have money to pay.

The cost of civil unrest

Besides the massive social costs of civil conflicts in terms of deaths, injury, disease and the impact of refugee populations on neighbouring countries, civil wars have extremely high economic costs. During a civil war society diverts expenditure from butter to guns, creating double losses. There is the lost opportunity cost of what could have been done if the money had been spent on productive economic activity and there is the loss through destruction during and after the conflict. Flight of citizens from rebel and government forces creates massive losses.

During peacetime the average developing country spends about 2.8% of GDP on the military (Collier et al., 2003). During civil war this typically increases to 5%. That increase of 2.2% over seven years of the average conflict leads to a permanent loss of 2% of GDP.

These diverted resources used in conflict create further destruction of infrastructure, businesses, shelters, farms, etc. Rebel forces destroy infrastructure necessary for business, such as telecommunications, airports, ports, railroads, roads and bridges. In addition rebels and government forces loot and destroy businesses and farms. Flight of people and wealth from the area reduces availability of customers, employees and investment. In response people invest less and retreat into more vulnerable and less productive subsistence activities.

The Conflict Trap – the downward spiral of poverty and civil unrest

In addition, high military expenditures and capital flight continue for years after the conflict. Post civil war incomes are typically 15% lower, which means that about 30% more people will be living in absolute poverty (Collier et al., 2003). Moreover, countries in the first decade of post-conflict peace have a 50% chance of further conflict (Collier et al., 2003). Countries with stagnant, low or medium economic growth and those in the first decade of post-conflict peace can reduce their likelihood of conflict through greater economic development (Collier et al, 2003).

Conducting business in a ‘non-permissive environment’ is extremely difficult. This can create the downward spiral, called the Conflict Trap (Collier et al., 2003), which deepens the civil unrest and increases the likelihood of additional conflict. Loss of business activity contributes to civil unrest due to high unemployment and lack of basic necessities (Collier et al, 2003).

Business Development in reverse

In addition to economic development in reverse, there is growing awareness that the extreme changes to the business environment created by natural or manmade disasters causes existing businesses to revert to the nascent business development stages (Zolin & Kropp, 2007a; Zolin & Kropp, 2007b) in a process similar to ‘emergency entrepreneurship’ (Johannisson & Olaison, 2007). So, in addition to economic development in reverse this process can be likened to ‘business development in reverse’.

Microfinance and Financial inclusion

The success of microfinance has influenced many to look towards entrepreneurship to help lift developing countries out of poverty (Alverez, 2012).

But recently there has been growing scepticism of the ability of the microfinance sector to progress to the economy beyond a certain point: The microfinance community globally is starting to move up the chain and there is now starting to be a debate about private equity in micro-finance. For example there is only so much that you can do on a $100 loan. In order to build more substantial business, you need adequate capital along with the skills required.

Over the next 10 years, the microfinance (Financial inclusion) community has to evolve to create collaborative partnerships with well established players in the financial sector. An example of this will suffice in a triangular relationship between major banks, a Financial Inclusion Enterprise(FIE) and the governments, in which the bank provides seed funding, and the government meets the overhead costs, while the FIE administers the funds to targeted beneficiaries. The returns from the bank funds are at or below commercial rates. The banks participate in this partnership as part of their Corporate Social Responsibility (CSR).

Results from the microfinance industry indicate that microfinance alone does not solve the problems of poverty (Dalglish & Tonelli, 2011). In fact, access to microfinance without training in business can actually lead to poor results leaving recipients worse off than before. One microfinance strategy is to replace financial capital with social capital. This allows new enterprises to start with backing from friends and family instead of cash. Unfortunately this strategy can increase poverty if the enterprise fails because the whole family, social network or village can be plunged into a worse financial position.

Remittances: Positive or negative impact?

Remittances are funds sent by expatriates to their families and friends in the home country. According to Kiiru, (2010) there are risks and possible negative effects of remittances. A worrying scenario is that higher income of households through remittances can remove pressure from governments to implement political, economic, social and environmental reforms. Further there are questionable effects that have been observed, for example inequitable growth at the community level. People from very poor households are seldom in a position to afford to send a family member to study or work abroad.

Based on findings from a study in Pakistan, which shows that the well to do households usually receive more remittances, Ratha (2003) argues that remittances increase the income gap. Prospective land and property purchases by remittance recipients can lead to higher prices for land, which affects poor households in the agriculture sector. There is also a tendency and risk for recipients of remittances to develop a culture of dependence, which does not favour self-initiative (Bagasao, 2004).

Social: Health, Education and Welfare Factors

Quiggin (2007), Explains that the foundation of social issues is based on the fact that members have an obligation to each others' needs. This entails "being there for each other". As a member of society there are expectations that help ensure individuals family and the community will be available as and when needed. As society becomes more diverse, driven by consumerism, social solidarity should not be assumed to exist automatically. There must be concerted efforts to help in providing assistance when need arises.

Access to health care remains one of the greatest challenges particularly in developing countries. There are problems associated with provision of health care, they include accessibility and affordability. Owing to lack of adequate public intervention health care expenses for common or moderate serious illnesses and injuries could be huge and uncertain. In most cases this is beyond the capacity of individuals, families and the community.

In terms of education there is uncertainty whether children will complete school once enrolled. Students from disadvantaged backgrounds have limited access to basic life necessities this may include food, water, sanitation adequate shelter not to mention security. Their set of circumstances translates to limited life opportunities. This is evident later in life when they venture into business.

Welfare typically refers to the provision by society for the support of some member s of the society, such as disabled individuals, single parents or families. Outside communist economies, few developing societies can afford to provide for individuals or families, no matter how dire their circumstances.

Technical Factors

With respect to significant global challenges, with the changing business environment, one also needs technology. For example entrepreneurs have to adapt to modern financial services which rely heavily on the internet for transactions. Sometimes using the latest technology can have advantages, such as with the introduction of the mobile phone, which made the installation of phone lines unnecessary. Also, when factories or production facilities are built they can employ the latest technology.

Environmental and Ethical

Debates rages about the ethics of the environmental costs of developing economies. If developed nations have a standard of living that developing nations would like to emulate, but can the world withstand the impact of the environment? Is it ethical for developed nations to enjoy the use of natural resources but deny them to developing nations?

Opportunity recognition

OpR is one of the most important abilities for successful entrepreneurs (Ardichivili, Cardozo & Souray, 2003).

In the private sector, opportunities are couched in terms of meeting market needs through creative combinations of resources to deliver superior economic value (Schumpeter, 1934; Kirzner, 1973; Casson. 1982; Ardichvili, Cardozzo, & Ray, 2003). Schumpeter (1950) proposed that an economy is fuelled by new products, processes, markets and management. Opportunities represent a way of generating profits from adding value or creating a new product, service, process or exploiting a new technology (Ardichvili, Cardozzo, & Ray, 2003). Opportunities "emerge from a complex pattern of changing conditions" (Baron, 2006, p.107).

Opportunity identification or recognition is a core element of the entrepreneurial process (Shane & Venkataraman, 2000; Venkataraman, 1997). OpR is distinct from, and occurs prior to opportunity evaluation and development (Ardichvili, Cardozzo, & Ray, 2003). Entrepreneurs create and deliver value for stakeholders by recognizing opportunities (Ardichvili, Cardozzo, & Ray, 2003). OpR is a first step in the process, but due to the non-permissive environment OpR might be reduced at the BOP because BOPE may focus on survival instead of opportunity development.

Individuals who are more entrepreneurial tend to be better at identifying opportunities (Ardichvili, Cardozzo, & Ray, 2003; Shane and Venkataraman, 2000). Although research to date has tended to focus on OpR being associated with entrepreneurs who start-up and develop entrepreneurial businesses, entrepreneurship is not solely about creating new businesses (Cooper & Dunkelberg, 1986; Ucbasaran, Westhead, & Wright, 2001; Ucbasaran, Lockett, Wright, & Westhead, 2003). Entrepreneurship is a creative process (Vesalainen and Pihkala, 1999) that can apply to large as well as small organizations (Knight & Cavusgil, 1996; Lewis & Zolin, 2004; Pinchot & Pelham, 1999). Thus, OpR is just as relevant to existing BOP firms as it is to the founders of potential nascent BOP firms.

OpR involves cognitive processes by which "individuals conclude that they have identified an opportunity" (Baron, 2006, p.107). These processes involve the perception, discovery, and creation of opportunities (Christensen, Madsen, & Petersen, 1989; Conway and McGuinness, 1986; Singh, Hills, & Lumpkin, 1999: in Ardichvili, Cardozzo, & Ray, 2003). OpR also has been viewed in terms of pattern recognition. Here, the individual recognizes opportunities using prototypes or exemplar models based on knowledge of exemplars already stored in memory (Baron, 2006). Hence exposing potential BOP entrepreneurs to successful business models could trigger OpR.

OpR can involve an active search for opportunities (e.g., Shane, 2003; Hill, Lumpkin, & Singh, 1997; Hills & Shrader, 1998; Gaglio and Katz, 2001; Kirzner, 1973). Search involves proactive behavior involving the scanning of the environment for potential opportunities. Sometimes, however, opportunities arise from situations and appear before entrepreneurs without their actively searching for them.

Creativity, innovativeness, and OpR are conceptually related. Particular personality traits are associated with entrepreneurial individuals who are involved with creativity (Ardichvili, Cardozzo, & Ray, 2003; Shane, 2003). They use their creativity to develop innovative solutions that break new ground (Baron, 2006, Gaglio & Katz, 2001) and in being alert to recognizing opportunities (Baron, 2006). They also appreciate that one does not need to know all the answers to solve a particular problem but that one does need to know where to look and who to talk to in identifying particular solutions. In this regard, entrepreneurial individuals are good at developing and tapping into social networks (Hills, 1995; 1999) to access solutions and to stimulate and synthesize ideas and thinking. Hence, bring potential nascent BOP entrepreneurs together and discussing entrepreneurial opportunities could trigger OpR.

Entrepreneurs generally accept that entrepreneurship involves risk-taking and are willing to take calculated risks in return for potential rewards. Prior knowledge of markets, industries, and/or customers (Shane, 2003) moderates the financial reward-OpR relationship (Shepherd & DeTienne, 2005). Identifying a potential opportunity will implicitly or explicitly involve risk. Entrepreneurs prefer to be associated with opportunities where risk is manageable (Timmons & Spinelli, 2007). If the risk associated with a potential opportunity is perceived to be too high, the opportunity will not be pursued. Strong risk aversion is likely to reduce OpR, while a "managed", slightly positive risk acceptance is likely to enhance OpR. At the BOP there are few livelihood alternatives to entrepreneurship, thus reducing the perceived risks.

Asset Identification

Regulatory focus theory (Higgins 1998) describes how one's internal regulation operates when choosing and pursuing goals. Individuals have a general orientation to achieve positive outcomes or to prevent negative ones. Regulation focus can influence goal pursuit, thereby influencing speed versus accuracy, flexibility in changing plans, and adjusting motivational intensity in response to success versus failure feedback (Higgins, 1998). Regulation focus can also influence goal commitment, counterfactual thinking, and the generation of alternatives (Higgins & Spiegel, 1998).

A promotion regulation focus aims at personal development, aspirations, accomplishment, or achievement of an ideal. Individuals with a promotion focus tend to be more concerned with the absence or presence of positive outcomes and are probably better at recognizing opportunities to achieve objectives (Baron, 2004). Those who apply a prevention regulation focus are more concerned with duties, targeting protection, safety, and responsibility and showing concern for the absence or presence of negative outcomes and more likely to identify opportunities that avoid risk.

Hence the psychological regulation focus of the lead entrepreneur or entrepreneurial team could affect OpR.

Asset Based Community Development

Asset Based Community Development (ABCD) is a "strengths-based" approach to community development (Healy, 2005), which is designed to bring a community together through a process of asset identification to develop community relationships and instil trust, hope and self-efficacy and to develop shared objectives (Kretzmann & McKnight, 1993). Healy (2006) proposes that ABCD has four key principles:

1. Change must come from within the community;
2. Development must build upon the capacities and assets which exist within the community;
3. Change should be relationship driven, and
4. Change should be oriented towards sustainable community growth.

Kretzmann and McKnight (1993) described five steps to ABDC:

1. *Asset-mapping*: Mapping completely the capacities and assets of individuals, citizens' associations and local institutions
2. *Building internal relationships* among local assets for mutually beneficial problem-solving within the community
3. *Asset-mobilization*: Mobilizing the community's assets fully for economic development and information-sharing purposes
4. *Building a vision*: Convening as broadly representative a bgroup as possible for the purposes of building a community vision and plan

5. *Establishing external connections*: Leveraging activities, investments and resources from outside the community to support asset-based, ocally-defined development (p 345).

The key technique of ABCD is asset mapping, a process if identifying primary, secondary and potential building community blocks. Primary building blocks are assets within the community, like its members and their skills, secondary are located within the community but owned outside, like a railway station and potential are wholly outside but may be acquired for use.

Organisational assets

Organizational variables that could influence OpR include the size and structure of the organization, its strategies and strategy-making processes, firm resources, and organizational culture (Lumpkin & Dess, 1996).

Research has shown that entrepreneurship flourishes better in smaller, private organizations, with less hierarchical organizational structures (Burns & Stalker 1961; Lawrence & Lorsch 1967). Hence the micro-firms of BOPE are likely to be more agile and better at spotting fleeting opportunities.

Due to the substantial environmental turbulence in developing economies, we also believe that organisations with more organic or fluid structures that include more open communication channels and, possibly, more decentralized authority (Burns & Stalker 1961; Lawrence & Lorsch 1967; Miller 1983) will have stronger OpR. These organizations are also likely to have flat structures that emphasize lateral interaction among members (see, Burns and Stalker 1961). Given the extensive turbulence and dynamism associated with the developing economies, BOPEs could be more effective if they were to structure their organizations accordingly to respond in a more entrepreneurial manner.

OpR can also be influenced by the characteristics of the founding entrepreneur or the top management team. In small private sector firms, the top management and the founders may be one in the same. Thus, OpR becomes a measure of the founders' entrepreneurial strategies.

This literature review identified areas for investigation in the methodology that follows.

Methodology

Our research goal is to investigate the effects of environment on asset identification and opportunity recognition at the BOP. To investigate this research question we will conduct interviews with nascent and existing entrepreneurs in the Democratic Republic of the Congo (DRC). These interviews will include an ABCD approach to identify primary, secondary and potential community and assets including individual financial, social and human capital assets.

Financial Assets- Scoping will focus on the ability of entrepreneurs to access affordable financial products. We will determine if finance options exist and are they aware of them.

Social Assets- Scoping will explore the extent to which community networks provide the requisite social networking opportunities to enable the entrepreneur to conduct business. For example by trading among peers does this provide stability or is a recipe for business failure. Can a small business owner deny a close relative essential food items without damaging their kith and kin relationship? And are family members able to provide the support necessary to run a businesses in the event of the main principal being indisposed with common illnesses, such as HIV/AIDS?

Human Capital Assets- Scoping will determine if BOP entrepreneurs have the education and experience needed to implement potential business opportunities. For example, do the entrepreneurs have the financial literacy needed to access financial assets and manage a small business?

Sample selection

To identify existing and nascent entrepreneurs we access them through the AusCongo Network, Inc, a volunteer organisation operating out of Brisbane, Australia with a Community Centre in Mbuji Mayi, the second largest city in the DRC. According to the Parliament of the Commonwealth of Australia Joint Standing Committee on Foreign Affairs, Defence and Trade (2011) Africa is a diverse continent of increasing importance to the world. In geopolitical terms, African countries have increasing influence on international organisations; in resources terms. The continent has vast reserves; in trading terms, while the population represents a huge potential market; and in agricultural terms, Africa's vast underutilised arable lands represent great opportunities to feed the world. Yet Africa also continues to face significant challenges, particularly in poverty, health, governance and economic development. DRC has 32.5 people per square kilometre, with 2,267,048 square kilometres. The DRC is one of the most poverty stricken countries in the world with 71,713,000 people in 2011, an increase of 82% from 39,151 000 in 1990. DRC has a life expectancy of 55 years (compared to 78 in the USA) with an infant mortality rate of 73 per 1,000 births (USA 6). DRC has had a negative net migration rate most years since 1995.

Interview protocol

The Congo is considered part of francophone Africa, where French is the first or second language of the population and although Swahili serves as a national, or official language in DRC, it is not the native language. Hence we will translated the survey into French. The survey is then translated back into English by another translator to ensure the meanings remained true to the initial survey. Since most respondents can not read or write the survey is administered by interviewers who speek both French and Swahilii, which allowes them to explain the questions and ensure they understand the spoken answers. The interviews are recorded and transcribed in French. Since it was a structured interview the responses to each question are analysed to identify the range of responses.

Conclusion

While some large corporations are identifying and exploiting business opportunities at the 'bottom of the pyramid' (Prahalad, 2007), there is an army of bottom of the pyramid entrepreneurs who have the potential to transform developing economies, if they can identify and exploit business opportunities. The BOP entrepreneur (BOPE) is limited by his or her resources, capabilities and management competencies in addition to any limitations imposed by the non-permissive business environment at the bottom of the pyramid. But BOPEs could have unidentified resources that could lead to the recognition of radical new opportunities.

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