

MicroFranchises as a Solution to Global Poverty

Kirk Magleby, November 2005

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“I must create a system, or be enslaved by another man’s.” William Blake, English artist and poet.

Prospectus

Fast food restaurant chains, icons of profligate American consumer culture, may actually represent a key solution to one of the world’s most daunting challenges.

Global poverty is generally regarded as the most serious problem on the planet. Poverty is best understood as slavery enforced through institutionalized, hierarchical exploitation.

Three schools of thought exist today about how best to solve poverty:

- 1) Macro economic structural adjustments such as debt relief, increased development aid and trade rules that favor developing nations.
- 2) Improved governance and business climates through transparency, reduced corruption, respect for the rule of law, property titles and formal business registration.
- 3) Micro economic enterprise solutions such as Microfinance, engaging people at the base of the income pyramid as business partners and customers, and building sustainable enterprises by introducing appropriate disruptive technologies, innovative business models and cross-sector partnerships.

Macro economic structural adjustments have not worked for decades and are not likely to work in the immediate future because they fundamentally misconstrue the underlying causes of poverty. Governance solutions require revolutionary social and political change. Enterprise solutions to poverty are achieving notable results around the world. Most flourishing pro poor enterprises use network business models that are quite different from traditional corporate command and control hierarchies. The most successful network business model on earth is franchising which demonstrates remarkable strengths as a poverty intervention. Proliferating very small businesses and social enterprises as MicroFranchises will help dramatically reduce global poverty.

Poverty is Global Menace #1

Poverty is the worst malignancy on earth. Many of the *causes célèbres* in the world today – AIDS and other infectious diseases,¹ terrorism,² environmental degradation, illiteracy, malnutrition, human rights abuses, human trafficking, narcotics trafficking, illegal immigration, ideological intolerance, tyranny, genocide, debt slavery – have their roots in this seminal evil, the brutal daily indignities of mind-numbing poverty. Billions of our fellow brothers and sisters barely survive on the equivalent of 1, 2 or 3 dollars per day.³ Tens of thousands die every day from the preventable effects of this environmental, social and economic pathology that Gordon B. Hinckley labels “the greatest pandemic of the world”.⁴ Gandhi called poverty “the worst form of violence.”

In an encouraging show of solidarity in January 2005, the world’s glitterati ensconced at the World Economic Forum in Davos and the world’s advocates assembled at the World Social Forum in Porto Alegre agreed on a common cause: poverty is our greatest problem. Jeffrey Sachs’ moving articulation of the poverty scourge was on the cover of *Time*.⁵ Buoyed by the vocal “Make Poverty History” campaign coming from the EU⁶, Tony Blair gave the issue prime billing at the 2005 G8 Summit. Kofi Annan chose Mark Malloch Brown, formerly head of the United Nations Development Programme, as his new chief of staff in part because global poverty has been such a large issue at the 2005 UN General Assembly. Poverty will top the agenda at the WTO Ministerial Round in Hong Kong later in the year. Opinion polls around the world show the issue rising to the

¹ “The best antidote for AIDS, or any other disease, is prosperity.” James Glassman, *Scripps Howard News Service*, syndicated column, August 2005.

² Thomas L. Friedman, one of the most astute contemporary observers of the global condition, says in a number of articles that terrorist extremism results from a “poverty of dignity.”

³ *Global Poverty Report: Multilateral Development Banks and International Monetary Fund Report to the G8*, Okinawa Summit, July 2000.

⁴ Gordon B. Hinckley, remarks at the Enterprise Mentors International 15th anniversary banquet, Salt Lake City, October 2005.

⁵ Jeffrey Sachs, “How to End Poverty,” *Time*, March 14, 2005. The article summarizes Jeffrey Sachs, *The End of Poverty: Economic Possibilities for Our Time* (New York: Penguin Press, 2005).

⁶ www.makepovertyhistory.org. This is the white band campaign being promoted by Oxfam and others who advocate a dubious “debt, aid, trade” agenda. US equivalents are www.onecampaign.org and www.one.org.

top of public consciousness. A whole global chorus echoes the words of Peter J. Robertson that poverty is “the single most important issue” on earth in the 21st century.⁷

Poverty is Slavery

The recent issue of *National Geographic* that elicited the most response from readers featured a cover story on “21st Century Slaves.”⁸ The photos in that article showing untouchables in Indian brick pits reminded many of Cecil B. DeMille’s epic portrayal of the Biblical account of the Israelites in Egypt. John Roach commented, “An estimated 27 million people around the world are enslaved: people trapped, controlled by violence, paid nothing, and exploited for labor.”⁹

These 27 million physically enslaved people are the most extreme victims of global poverty, but the 4 billion people on earth who live on less than \$4 per day are:

- People trapped
- controlled by local despots and malevolent institutions
- paid very little
- exploited for labor

Human beings do not wish to be poor anymore than they wish to be crippled, senile or malnourished. Large scale poverty does not exist because people are stupid, lazy or incompetent. Factors like religion, a history of colonialism or the so-called “work ethic” do not explain the vast imbalance in access to resources. Billions of people languish in poverty and hopelessness because social, cultural and economic forces beyond their control marginalize and oppress them.¹⁰ This chronic, systemic deprivation is called “institutional” or “structural poverty.” Amartya Sen calls it “unfreedom.”¹¹ Muhammad Yunus calls it slavery.¹² Unconscionably, the impoverished masses on our planet are slaves to a system that exploits human beings as chattel¹³ and denies people the opportunity to realize aspirations or achieve potential.¹⁴

⁷ Peter J. Robertson, Vice President, Chevron Texaco. Presentation at the WRI Conference “Eradicating Poverty through Profit: Making Business Work for the Poor”, San Francisco, December 2004. This is the conference Scott Shuster christened “BOP I.” Assessing the importance of this gathering as a defining moment for our generation, Shuster said, “We have been to Woodstock.” Most commentators agree that a new paradigm for international economic development is imperative since past policies and approaches have generally “failed to significantly reduce poverty or expand the middle class.” Colin McMahon, *Chicago Tribune*, October 31, 2005.

⁸ Andrew Cockburn, “21st Century Slaves,” *National Geographic*. September 2003. Photos by Jodi Cobb.

⁹ John Roach, *National Geographic News*, May 17, 2004.

¹⁰ “[Poverty] is like being in jail, living under bondage waiting to be free.” Cited in Deepa Narayan, Robert Chambers, Meera Kaul Shah, Patti Petesch, *Voices of the Poor: Crying Out for Change* (New York: Oxford University Press, 2000)

¹¹ Amartya Sen, *Development as Freedom* (New York: Alfred Knopf, 1999).

¹² Muhammad Yunus, *Banker to the Poor: Micro-Lending and the Battle against World Poverty* (New York: Public Affairs, 1999).

¹³ Nelson Mandela, speaking to the G7 in London in February 2005, compared the fight against poverty to the fight against slavery and apartheid.

¹⁴ C.K. Prahalad uses the term “aspirational poor” and advocates “enabling dignity and choice through markets.” C. K. Prahalad, *The Fortune at the Bottom of the Pyramid: Eradicating Poverty through Profits* (Upper Saddle River, NJ: Wharton School Publishing, 2004). The *Human Development Index* published by the United Nations Development Programme is about “enlarging people’s choices.” Muhammad Yunus (...continued)

Exploitation Causes Poverty

A young Brazilian, Marco Figueiredo, recently visited his native country after living for many years in the US. His comment upon returning from Brazil was telling. “I was aghast at the corruption and exploitation that exist at every level of Brazilian society. Even very poor people try to take advantage of those less fortunate.”¹⁵ Nations with a large impoverished underclass tolerate and encourage a pernicious hierarchical pecking order of exploitation¹⁶ that is institutionalized in the very fabric of society.¹⁷ Poverty perpetuates itself across generations since it is in the short term self-interest of the ruling or empowered class at all levels to preserve the status quo.¹⁸ In the absence of effective democratic or egalitarian institutions, the law of the jungle dictates that the strong will exploit the weak.¹⁹ LDS Scripture explains succinctly the root of this vast social malaise: “We have learned by sad experience that it is the nature and disposition of almost all men, as soon as they get a little authority as they suppose, they will immediately begin to exercise unrighteous dominion.”²⁰ Stuart Hart calls the poor “victims of corruption and active exploitation by predatory suppliers and intermediaries.”²¹ Slavery, feudalism, colonialism, totalitarianism and underdeveloped nations are the inevitable result.

Eritrean Gebreselassie Tesfamichael says the modern African state is “extractive in its design” with a mission not to serve people, but to “dominate and exploit them.” He continues that despite independence and incipient democracy, “the nature of that state remains intact” and the fundamental African problem is “not lack of resources, but the

talks about “bonsai people,” their growth stunted by a repressive environment, who die without ever knowing what they were capable of. Personal communication with Muhammad Yunus, July 2005.

¹⁵ Personal communication with Marco Figueiredo, March 2005.

¹⁶ Many poor kids peddling candy or trinkets in the streets are being “managed” by parents or grandparents who exploit their own children in a system that Dickens’ Fagin and the Artful Dodger would recognize.

¹⁷ Paul Lyman went to Ukraine in June 2005 as part of an ABA exchange team to consult with Ukrainian judges. “How do you work with a system where poorly paid judges expect bribes?” he wisely questions.

¹⁸ Washington Post columnist George F. Will describes one entrenched group as “a political class that has treated public office as private property.” He is describing legislators in California, but his observation applies worldwide. George F. Will, syndicated column, February 2005.

¹⁹ Stuart Hart mentions a poignant example of this in his important new book *Capitalism at the Crossroads: The Unlimited Business Opportunities in Solving the World’s Most Difficult Problems* (Upper Saddle River, NJ: Wharton School Publishing, 2005). Conversing with Muhammad Yunus, Hart learned that the famous Grameen phone ladies in rural Bangladesh were price gouging customers. They exploited a “shantytown monopoly” (C.K. Prahalad’s terminology) because they owned the only telephone in their village. So, Grameen Village Phone, acting as the democratizing egalitarian institution, immediately introduced a second telephone in each village to assure price competition. This is typical franchisor behavior. Franchisors control site selection. Franchisees generally grow by acquiring a second location, not by increasing the size of their first location or raising prices. The franchise business model enforces rational pricing to maximize network rather than individual location potential. If unit economics become too favorable in one location, the franchisor will locate another store nearby to absorb the demand. If unit economics become too unfavorable, the franchisor will often close a nearby location to give the struggling store additional market territory. Franchisors tend to limit individual unit upsides, but at the same time they mitigate downsides. Both effects are very important in the developing world if an ethos of *liberté, égalité, fraternité* is ever going to replace the systemic exploitation of institutional poverty.

²⁰ Doctrine and Covenants 121:39. Examples abound in Robert Guest, *The Shackled Continent: Power, Corruption and African Lives* (Washington, D.C.: Smithsonian Institution Press, 2004).

²¹ Stuart L. Hart, *Capitalism at the Crossroads*.

failure of political leadership.”²² As evidence, he points out that African economic migrants, part of the continent’s vast diaspora, do well enough in healthier societies that they send \$30 billion of family remittances back to their relatives in Africa each year.

Vicious Cycles

Poverty is a cyclical, intergenerational black hole with a strong gravitational pull that is difficult to escape.²³ For example, very poor people often lack access to quality health care which causes disease, disability and premature death, all of which increase poverty. Semi-literate parents struggling on the brink of survival tend to undervalue their children’s education, limiting future social mobility. Children without adequate interior lighting in the home tend to read poorly and infrequently. The middle-aged and elderly poor, suffering from common presbyopia but unable to afford reading glasses, are often forced to give up livelihoods prematurely as their close up vision blurs with age.²⁴

Characteristics of the Poor

Middle and upper income people often mistakenly assume that the poor are not like them. They see unsanitary hygiene or unrefined manners and conclude that people in a lower socio-economic status must think differently or at least be apathetic. On the contrary, very poor people are just people in acutely constrained circumstances who are often dispirited because they know a better life exists but they feel powerless to progress toward it. The poor are survivors. They are adaptive.²⁵ They are fashion, brand and value conscious. Given the chance, they learn readily and adopt modern technology enthusiastically. The poor can be tenacious when they sense an opportunity. Given a favorable environment, they quickly become informed consumers and efficient producers in the global economy. C. K. Prahalad calls the poor victims of a “huge asymmetry” of information, choice, access to resources, capacity to enforce contracts, dignity and self-esteem.²⁶ The lives of the poor may be different from ours, but their innate abilities, needs and aspirations are not.

²² Gebreselassie Yosief Tesfamichael, economist, international development consultant and former finance minister of Eritrea, “In Africa, Just Help Us to Help Ourselves,” *Washington Post*, July 24, 2005.

²³ “The downward trajectory of poverty is continually reinforced.” Marc Lopatin, Kurt Hoffman, Chris West, Karen Westley, Sharna Jarvis, *Enterprise Solutions to Poverty: Opportunities and Challenges for the International Development Community and Big Business* (London: Shell Foundation, 2005).

²⁴ Graham Macmillan, Director, Scojo Foundation. Presentation at the 8th annual BYU Economic Self Reliance Conference, MicroFranchise track, Provo, UT, March 2005. David S. Landes makes a similar point about eyeglasses as an enabling technology for industrialization in his insightful *The Wealth and Poverty of Nations: Why Some are so Rich and Some so Poor* (New York: Norton, 1998).

²⁵ Dr. Craig Marsden, a veteran of many medical and service missions with Chasqui Humanitarian (now Ascend, A Humanitarian Alliance), tells a delightful story from the high Andes. A team of humanitarian volunteers worked with local villagers to install a municipal water system. They had carefully purchased supplies because the village was rather remote. Near the end of the project, they discovered that they were short one PVC union joint. The North Americans all stood around distraught. The project was on hold until someone went back to town and purchased the right part. A local Peruvian, though, grabbed a small length of PVC pipe with a pair of pliers and lit a llama dung fire. By simultaneously heating and rotating the small length of pipe around another pipe end, the clever fellow in about 15 minutes produced a crude but entirely serviceable union joint.

²⁶ C. K. Prahalad, *The Fortune at the Bottom of the Pyramid*.

OnSat, an Internet connectivity firm best known for wiring the Navajo Nation, installed solar power and a satellite based Internet connection in a remote village in Honduras that had never even had electricity before. An interactive computer lab in the local school became an instant hit. A few months later, an educational psychologist visited the village to do an impact assessment. Administering a standard IQ test, she discovered 2 geniuses among the village youth.²⁷ Latent talent abounds in every community.²⁸

Some Historical Perspective

Following Bretton Woods²⁹ and World War II, individual “care packages” alleviated some suffering and the massive Marshall Plan helped rebuild war torn nations. Successful economic development in Europe and Japan gave impetus to ambitious attempts to solve world poverty. Donor nations built massive infrastructure, supplied materials, equipment and services, “adopted” children for \$25 per month, and sent legions of Peace Corps volunteers followed by waves of eco-tourists. Development projects set up schools, health care facilities and innovative grassroots financial institutions. Numerous policy initiatives attempted to improve local business climates through governance reforms. The Cold War ended and market oriented societies demonstrated their unequivocal superiority over command economies.³⁰ A global economy developed for the first time in history. The ubiquitous profit motive unleashed globalization and technological revolution, twin forces so powerful we are still trying to comprehend their impact.³¹

Meanwhile, poverty persists. “54 countries are poorer now than they were 15 years ago,” was Carly Fiorina’s recent assessment.³² James A. Harmon acknowledges that we had a “very simplistic view” of the developing world throughout the 60’s, 70’s and 80’s.³³ Richard Sandbrook rues the fact that most development aid is administered through large foreign contractors who come into a country and leave behind only “decaying infrastructure” after their contracts expire.³⁴ Beautifully paved roads have rotted back to dirt and once new hospitals are crumbling. Few sponsored children achieve self-reliant

²⁷ David Stephens, CEO, OnSat. Presentation, BYU eBusiness Day Conference, Provo, UT, October 2004.

²⁸ It’s assumed that Africa has a huge capacity deficit; indeed, it’s often depicted as a blank slate. Nothing could be further from the truth. Even in the worst circumstances, the people of Africa retain precious social, cultural, economic and human assets.” Gebreselasie Tesfamichael, “In Africa, Just Help Us to Help Ourselves,” *Washington Post*, July 24, 2005.

²⁹ Bretton Woods, NH was the site of a 1944 conclave that created the World Bank, the IMF, and other important international economic management institutions.

³⁰ See Andrew Bernstein’s provocative article *Capitalism is the Cure for Africa’s Problems*, The Ayn Rand Institute, Irvine, CA, 2003.

³¹ On the enigmatic, disparate effects of globalization, see Thomas L. Friedman, *The Lexus and the Olive Tree: Understanding Globalization* (New York: Farrar, Straus and Giroux, 1999)

³² Carly Fiorina, Former CEO, Hewlett Packard. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. David Rothkopf calls these countries the “foiled aspirant class of states,” and notes that “more than 90 percent ended up regressing deeper into poverty,” David Rothkopf, “Pain in the Middle,” *Newsweek*, November 21, 2005.

³³ James A. Harmon, Chairman, World Resources Institute. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

³⁴ Richard Sandbrook, Senior Advisor, United Nations Development Programme. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

prosperity once donor fatigue sets in and their sponsorship inevitably ends.³⁵ The dependency created by relief aid does not alter the underlying institutional basis of poverty. In fact, it generally exacerbates the problem.³⁶

Malevolent and Benevolent Institutions

Q. Why have Western economic development strategies failed so conspicuously in most parts of the globe? **A.** Western governments, NGOs, donor and aid agencies have not understood the pervasive, suffocating influence of endemic hierarchical exploitation in the developing world. When most institutions in a society are repressive rather than egalitarian, the human spirit simply fails to reach full flower.

The key here is the word “institution.”³⁷ Malevolent institutions (corrupt governments, commercial monopolies, mafias, exploitative slum lords) enslave the poor and foment poverty.³⁸ Infrastructure enhancements (schools, bridges, hydro-electric plants) in Western democracies improve the business climate and create a rising tide that lifts all boats. Those same infrastructure investments in the developing world often end up simply strengthening the hand of the local oligarchs who are the root cause of institutional poverty in the first place.³⁹ Individualistic interventions (temporary relief aid, small personal loans) level the playing field enough to give a few strong people some of the tools they need to escape poverty. It is hard, though, for even resolute individuals armed with a few tools to liberate themselves from the overpowering influence of the oppressive institutions around them.

Poverty is slavery and slaves seldom free themselves. The poor need benevolent, nurturing, liberating institutions so they can begin achieving their potential in a favorable

³⁵ An orphanage is an extreme example of child sponsorship. Many orphanages around the world are radically changing their mission. Rather than warehouse children in institutions, they facilitate foster care in private homes. A disproportionate number of children raised in the hothouse environment of a traditional orphanage quickly fall prey to violence, drugs or the sex trade when they reach the age to be released onto the mean streets of real life.

³⁶ The current global agenda focus on debt relief, increased development aid, and fairer trade is encouraging. As the worst problem on earth, poverty demands attention. These macro economic structural adjustments, though, have not worked for 50 years. See Thomas W. Dichter, *Despite Good Intentions: Why Development Assistance to the Third World has Failed* (Amherst, MA: University of Massachusetts Press, 2003) and Michael Maren, *The Road to Hell: The Ravaging Effects of Foreign Aid and International Charity* (New York: The Free Press, 1997). Giving things away tends to “dampen the human spirit.” Self-empowerment is the “better option.” Personal communication with Muhammad Yunus, July 2005.

³⁷ “Institutions, not resources matter most.” “U.S. Foreign Aid: Meeting the Challenges of the Twenty-first Century,” USAID White Paper, Bureau for Policy and Program Coordination, January 2004.

³⁸ “Good banking is, in the end, no match for bad government.” “Bankable banks,” *The Economist*, November 5, 2005. This article explains why the Latin American Profund, managed by Alex Silva, did not renew its charter in 2005 after a decade in operation.

³⁹ In the late 19th century US, these rapacious, omnivorous capitalists were called “robber barons.” They go by the name “New Russians” in contemporary Russia. In Kenya, they are called the “Wabenzi,” literally “the tribe of the Mercedes Benz.” You’ll hear the term “cacique” in Latin America which carries the connotation of tribal chief. Development professionals in Washington, D.C. talk about the HPVE or “high priest vulture elite.” Robert Guest decries Africa’s “thugocracy” in *The Shackled Continent*.

environment.⁴⁰ In the developed world where the poor feel beleaguered by landlords and credit bureaus, this hand up is often provided by educational institutions, employers, the government, churches, charities, etc. In emerging nations, effective institutional allies for the billions of disenfranchised and dispossessed have been few and far between.⁴¹

What are We Really Trying to Accomplish?

To echo Thomas Jefferson, we hold these truths to be self-evident that stifling individual human progress by enslavement through institutional poverty is an ultimate social evil.⁴² It is a fair question, then, to ask what are the ultimate social goods to which we aspire? The goal cannot be to turn every citizen of sub Saharan Africa into a prodigal American consumer. The carrying capacity of our small planet simply precludes that level of global resource utilization. Solving poverty, I propose, means an increase in:

- Freedom, as measured by Freedom House rankings of countries from 1.0 (Free) to 7.0 (Not Free).⁴³
- Transparency, as measured by Transparency International rankings of countries from 10.0 (highly clean) to 0.0 (highly corrupt).⁴⁴
- Human Development, as measured by the UNDP Human Development Index that tracks life expectancy, adult literacy, school enrollment and GDP per capita.⁴⁵
- Equality, as measured by a nation's Gini coefficient, a metric of income distribution inequality between quintiles in a population. Gini ratios are calculated by the World Bank and others.⁴⁶
- Ecological Sustainability, as measured by a country's Environmental Sustainability Index, calculated by a joint project between Yale and Columbia Universities.⁴⁷ Projects and enterprises often use the ISO 14001 standard.

⁴⁰ "People can do miracles for themselves when they have the support of an institution behind them." Personal communication with Muhammad Yunus, July 2005. David Wheeler talks about "good will and trust-based relations" that must be "reciprocated and nurtured" in institutional networks if confidence between people is going to grow. Wheeler, David, et. al., "Creating Sustainable Local Enterprise Networks," *MIT Sloan Management Review*, Fall 2005.

⁴¹ "Institutions Westerners take for granted are entirely absent in most of Africa." John Blundell, "Africa's Plight Will Not End with Aid," *The Scotsman*, June 14, 2004

⁴² A rogue's gallery of ultimate evils according to the author's value system: On June 6, 1944, more human beings lost their lives in Auschwitz gas chambers than on Normandy beaches. In 2004, American medics came upon a critically ill girl in a remote Afghan village. They explained to the father that if he would take his daughter to a medical post about two hours away, the doctors there could save the girl's life. Reminding them that the trail from his house to the medical post passed over rocky ledges that could be dangerous for his donkey to traverse, the father declined the American's offer explaining, "girls are free, but donkeys cost money." On January 30, 2005, one of the 9 suicide bombers dispatched to disrupt Iraqi elections was a Down Syndrome child.

⁴³ www.freedomhouse.org. The Heritage Foundation/Wall Street Journal Index of Economic Freedom www.heritage.org/research/features/index publishes a similar list as a guide for investors.

⁴⁴ www.transparency.org.

⁴⁵ www.undp.org.

⁴⁶ A convenient source for a country's Gini coefficient and per capita GDP adjusted for PPP is *The World Factbook* available at www.cia.gov. For an erudite discussion of the topic, see Branko Milanovic, *Worlds Apart: Measuring International and Global Inequality* (Princeton, NJ: Princeton University Press, 2005).

⁴⁷ www.yale.edu/esi.

- Enterprise Sustainability, adherence to Triple Bottom Line principles as expressed in Cornell University's BOP Protocol (economic profitability, environmental sensitivity, social responsibility).⁴⁸ Another tool gradually coming into greater favor around the world is the comprehensive GRI.⁴⁹

There is a strong positive correlation between all five global indices. Finland and the other Scandinavian countries, for example, are at or near the top of all five metrics, while many of the poorest, least developed countries cluster conspicuously at the bottom of the scale.

Enterprise is the Solution to World Poverty

Every nation that has lifted itself out of poverty in the current generation (Singapore, South Korea, Taiwan) has done it in precisely the same way: economic growth and job creation through successful enterprises. The same pattern holds true in the high growth emerging economies of recent years (Chile, China, India). Developing nations can't medicate their way out of poverty, even though access to health care is a necessary condition. Cubans enjoy excellent health care by world standards, but they are desperately poor. People in the developing world can't educate their way out of poverty, even though access to knowledge is a necessary condition.⁵⁰ Thousands of Peruvian and Filipino MD's and PhD's drive taxis.⁵¹ Developing countries can't borrow their way out of poverty, even though access to capital is a necessary condition. Bolivia's Microcredit industry is approaching market saturation,⁵² yet it remains the poorest country in South America.⁵³ And, nations can't legislate their way out of poverty, even though property

⁴⁸ Erik Simanis, Stuart Hart, Gordon Enk, Duncan Duke, Michael Gordon, Allyson Lippert, "Strategic Initiatives at the Base of the Pyramid: A Protocol for Mutual Value Creation" (Ithaca, NY: Cornell University Center for Sustainable Global Enterprise, February 17, 2005).

⁴⁹ www.globalreporting.org.

⁵⁰ In his penetrating analysis of international development aid failure, William Easterly finds little correlation between education investment in a country and economic growth. William Easterly, *The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics* (Cambridge, MA: MIT Press, 2001). The lack of formal employment opportunities in their home economies is a major reason why so many highly educated people from the developing world migrate to wealthy OECD countries, even though their educational credentials are seldom recognized in their new home.

⁵¹ In developed or transitional economies, education is generally a reliable facilitator of upward social and economic mobility. In many under developed countries, though, there simply are no jobs, even for the highly skilled. The administrator of a vocational education program in Bolivia explained: "There is work, there just aren't any jobs." This situation forces most people in the economy toward self-employment as micro enterprisers.

⁵² "We will see an industry shakeout. Markets are saturated. Expect mergers and acquisitions." María Otero, President & CEO, Acción Internacional. Presentation at the BYU Economic Self-Reliance Conference, March 2005.

⁵³ Eduardo Bazoberry Otero, General Manager, Prodem. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. One of the reasons Microcredit has not moved the dial in Bolivia is that many Microcredit-enabled enterprises are engaged in retail trade. In many low income micro economies, the retail sector is a zero sum game. Microfinance by itself, individual anecdotal success stories notwithstanding, is inherently incapable of eradicating institutionalized, structural poverty within a community. Most of the businesses it facilitates are simply too small and weak to generate significant full-time employment opportunities. Microfinance plus MicroFranchising, on the other hand, can be a potent combination to drive small enterprise growth. See Kirk Magleby, "10 Reasons Why Microcredit Will Never Solve World Poverty" available at www.omidyar.net/group/poverty/file/3.40.11309869403.

protection through law and order is a necessary condition. India enjoys a good legal code as part of its British legacy, but corrupt and overly bureaucratic enforcement dooms millions to lives of squalor.

Families and countries must earn⁵⁴ their way out of poverty.⁵⁵ Although income can be redistributed in many different ways, there is only one way to create wealth: a successful business has to make a profit.⁵⁶ Even the UNDP, which Richard Sandbrook calls “commercially illiterate,”⁵⁷ has in the words of Mark Malloch Brown, “firmly embraced” the idea that the private sector is the primary way to promote economic development.⁵⁸ Traditional relief and infrastructure approaches to economic development “now appear to be all but bankrupt” in Stuart Hart’s view.⁵⁹ The “Washington Consensus” is increasingly irrelevant.⁶⁰ Export led growth strategies resulted in a worldwide race to the bottom where China supplies WalMart and two thirds of humanity sees little or no benefit from global capitalism.⁶¹ The solution is “massive entrepreneurship”⁶² driving “domestic

⁵⁴ “One common mistake in philanthropy is treating symptoms rather than causes. If people are hungry, buy them food. If they are sick, provide medical care. For the uneducated, start schools. In most cases, a much better solution is this: offer a means for people to work their way out of poverty...Lifting a family out of poverty solves a host of other problems.” This is Geneva Global’s laudable concept of “performance philanthropy” to solve world poverty. www.genevaglobal.com.

⁵⁵ “Loans, grants and subsidies sent into regions lacking vigorous cities can shape inert, unbalanced or permanently dependent regions, but are useless for creating self-generating economies.” Jane Jacobs, *Cities and the Wealth of Nations: Principles of Economic Life* (New York: Random House, 1985).

⁵⁶ Joel Madsen helped me understand this primal point: all wealth springs from successful enterprise. John D. Rockefeller’s famous refrain that there are only two ways to make money: get money working for you or get people working for you, is germane.

⁵⁷ Richard Sandbrook. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

⁵⁸ Mark Malloch Brown, former Administrator, United Nations Development Programme, now Chief of Staff, UN Secretary General. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. A good example is the “Growing Sustainable Business” initiative of the UN Global Compact. www.undp.org/business/gsb. An environmental perspective concurs: “It is clear commerce is the engine of change.” William McDonough, Michael Braungart, *Cradle to Cradle: Remaking the Way We Make Things* (New York: North Point Press, 2002).

⁵⁹ Stuart L. Hart, *Capitalism at the Crossroads*.

⁶⁰ The term “Washington Consensus” was coined in 1990 by John Williamson. It is generally synonymous with “neo liberalism” and “globalization.” It connotes fiscal discipline, emphasis on high economic returns, income equality, primary health care, primary education, infrastructure, tax reform for lower rates and a broader tax base, interest rate liberalization, competitive currency exchange rates, trade liberalization, liberalization of FDI, privatization, deregulation and secure property rights. The “Augmented Washington Consensus” associated with Dani Rodrik implies corporate governance, anti-corruption, flexible labor markets, WTO agreements, financial codes and standards, prudent capital account opening, non intermediate exchange rate regimens, independent central banks, inflation targeting, social safety nets, and targeted poverty reduction. The fact that Argentina recently unilaterally repudiated much of its foreign debt with minimal repercussion shows how irrelevant the Washington Consensus has become.

⁶¹ A few years ago, I had an animated discussion with a small group of workers employed at the sprawling Volkswagen Plant in Puebla, Mexico. They were considering a strike. I asked if they were aware of all the “maquiladora” plants in northern Mexico that had recently shut down and moved to China in search of lower wages and more integrated supply chains. The fact that Mexicans would have to compete with Chinese workers for manufacturing jobs seemed preposterous to them.

⁶² C.K. Prahalad, Professor, University of Michigan. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

demand led growth.”⁶³ In other words, to solve global poverty the world needs tens of millions of profitable, locally-owned small businesses creating employment and providing goods and services tailored to emerging markets in the developing world.⁶⁴ *The Economist* argues that the only effective way to deal with global poverty “is to use the solution that worked in the past in America, western Europe and Japan: open, trading economies, exploiting the full infrastructure of capitalism.”⁶⁵ The UN stresses the need for a much greater role for private enterprise in sustainable economic development that will “make business work for the poor.”⁶⁶

Relief versus Sustainability

Those blessed to live and earn in wealthy nations generally ignore global poverty. It is seemingly intractable and supremely unpleasant to contemplate. When Westerners do think about the plight of their impoverished brothers and sisters in faraway lands, their normal reaction is to:

- send money
- send stuff
- send people to provide services

A little temporary relief placates activist consciences and helps relatively wealthy donors feel good.⁶⁷ What would a typical American, Japanese or European think, though, if they were that impoverished aid recipient? Would they be satisfied with a little cash, a care package or a group of adventure travelers on a service project? Of course not. They would want a job.⁶⁸ They would want sustainability. And sustainability comes only

⁶³ Thomas Palley, “A New Development Paradigm: Domestic Demand Led Growth,” *Foreign Policy Focus*, September 2002: 1-8.

⁶⁴ “Aid distorted the development process. Donor organizations emphasize the social sectors – health and education – while almost entirely ignoring the commercial and business sector. Africa’s cities are full of educated, enterprising people. We need health care and education, yes, but we also need a productive sector for the healthy and the educated to work in.” Gebreselassie Tesfamichael, “In Africa, Just Help Us to Help Ourselves,” *Washington Post*, July 24, 2005.

⁶⁵ “Tired of globalization,” *The Economist*, November 5, 2005.

⁶⁶ UN Commission on the Private Sector and Development, *Unleashing Entrepreneurship: Making Business Work for the Poor* (New York: UN Development Programme, 2004).

⁶⁷ Allen Hammond told this story at Cornell’s BOP Learning Lab in February 2005: Al was in a session at Davos when the subject of bednets to prevent malaria in sub Saharan Africa came up. Sharon Stone spontaneously offered \$10,000 to purchase bednets and challenged others in the room to do the same. In just minutes, they raised \$1 million to purchase bednets for Africans. Al, meanwhile, was shaking his head. He knew how hard many companies and NGOs have worked for years to make bednets into a viable, sustainable business, and how \$1 million of free bednets dumped into the economy would poison the commercial bednet market. Many poverty interventions done primarily to appease activist consciences have unintended long term negative consequences that result in more harm than good. One is reminded of the famous T.S. Eliot quote “Half the harm that is done in this world is due to people who want to feel important. They don’t mean to do harm – but the harm does not interest them. Or they do not see it, or they justify it because they are absorbed in the endless struggle to think well of themselves.” T.S. Eliot *The Cocktail Party* (London: Faber and Faber, 1974). Stanford’s Thomas Sowell describes the mindset well: “It was not really about which policy would produce what results. It was about personal identification with lofty goals and kindred souls.” Thomas Sowell, syndicated column, October 2005.

⁶⁸ The Shell Foundation concurs that “jobs are often at the top of poor people’s lists of priorities.” Marc Lopatin, et al, *Enterprise Solutions to Poverty*. The World Bank’s *Voices of the Poor* survey shows low income people longing for jobs that will provide livelihoods for themselves and their families.

through profitable private or social enterprises with viable value propositions in the indigenous economy.

I was in a village located beside a river in Peru's Sacred Valley. The villagers had irrigated fields on a plateau a few dozen feet above the river. A large pump was installed near the river with a four inch pipe running up to the crops. A steady procession of villagers was hauling water in buckets up a well worn track to their fields. "Where did that pump come from?" I asked. "Some Koreans installed it a few years ago," they reported. "So why are you hauling water in buckets?" I continued. "The pump is broken," they answered. "Why don't you fix the pump?" I pressed. "The Koreans have never come back," was their telling reply.

Emergency donations are essential to preserve life in catastrophes like famines in Ethiopia or tsunamis in Indonesia. The only way to solve poverty, though, is through sustainable development.⁶⁹ Carly Fiorina believes "A solution that is not sustainable is not a solution – it is short term relief aid that can and often does more harm than good."⁷⁰

The Spectrum of Development

Stephen W. Gibson and Jason Fairbourne have created a seven step list that ranks potential poverty interventions in order by long term economic development effectiveness:

- Disaster Aid, Taking Things to the Poor, (least long term effect)
- Poverty Relief, Taking Services to the Poor
- Excursions, Taking People to the Poor
- Microcredit, Lending Money to the Poor
- Microfinance, Providing Financial Services to the Poor⁷¹
- Micro enterprise Development, Teaching People to Grow Businesses

⁶⁹ One of the wisest men I know, Arturo de Hoyos, taught me this invaluable lesson many years ago: "If I solve your problem, I grow, but you shrink, and the relative distance between us increases." A native of Mexico, de Hoyos holds a PhD from Michigan State and founded La Universidad Hispana in Utah. He has developed a number of self-sustaining post secondary schools in Mexico.

⁷⁰ Carly Fiorina. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. "Whatever damage European colonialism did to Africa during its relatively brief reign, that was probably less than the damage done later by well-meaning Western would-be saviors of Africa. Africans do not need to be treated as mascots but as people whose own efforts, skills and initiatives need to be freed from the tyranny of their leaders and the paternalism of Western busybodies." Thomas Sowell, "The Tragedy of Africa: Local Tyranny Subsidized by Western Paternalism," syndicated column, July 2005. James Shikwati, Kenyan economist, is even more direct: "For God's sake, please just stop...such intentions have been damaging our continent for the past 40 years. If the industrial countries really want to help the Africans, they should finally terminate this awful aid...huge bureaucracies are financed with the aid money, corruption and complacency are promoted. Africans are taught to be beggars and not to be independent. In addition, development aid weakens the local markets everywhere and dampens the spirit of entrepreneurship that we so desperately need...development aid is one of the reasons for Africa's problems. Interview, *Der Spiegel Online*, July 2005. "What can the West do to help? The worst thing is more foreign aid." Walter Williams, "An Explanation for Third World Poverty," *Capitalism Magazine*, June 30, 2004.

⁷¹ "We began to sense that a school or a water system didn't necessarily have long-term impact." www.accion.org on the reason Accion International evolved from a humanitarian aid group into an MFI.

- MicroFranchising, Providing Business Models and Formats to the Poor (greatest long term development impact)

As this spectrum of development relationships illustrates, MicroFranchising may be a superior way to create and replicate successful private and social enterprises in developing economies.⁷²

Roots of MicroFranchising

About fifteen years ago, the concept of “sustainable development” became firmly entrenched in the public psyche following events like the 1992 Earth Summit in Rio de Janeiro. This notion that private businesses should pursue the triple bottom line of profitability, environmental stewardship and social responsibility is gaining strength worldwide as evidenced by the recently adopted Equator Principles framework for international project finance.⁷³ The Microcredit movement begun by Acción in Brazil, Opportunity International in Colombia, and Muhammad Yunus in Bangladesh in the 70’s and John Hatch in Bolivia in the 80’s is a good example of this enlightened view of economic development. Poverty yields to growth when local enterprises succeed. In the words of Jonathan Lash, “empowering solutions” work better than “imposed or donated solutions.”⁷⁴ The World Business Council for Sustainable Development’s “Sustainable Livelihoods” project is one among many who are now pursuing this laudable goal.⁷⁵ The recent Base of the Pyramid BOP phenomenon is the latest expression of this sustainability movement.⁷⁶

To solve poverty we must:

- Identify high potential private or social enterprisers.
- Train these future owners/managers in environmental and social ethics in addition to sound management principles.
- Help these nascent entrepreneurs found successful enterprises.
- Help these aspiring capitalists and social entrepreneurs grow their organizations and create jobs.
- Help these successful managers protect their property, leverage assets and found new enterprises.⁷⁷

⁷² Stephen W. Gibson and Jason Fairbourne, Presentation at the BYU Economic Self Reliance Conference, MicroFranchise Track, March 2005.

⁷³ www.equator-principles.com.

⁷⁴ Jonathan Lash, President, World Resources Institute. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. “Externally imposed development models have not gotten us very far.” Gebreselassie Tesfamichael, “In Africa, Just Help Us to Help Ourselves,” *Washington Post*, July 24, 2005.

⁷⁵ www.wbcsd.ch.

⁷⁶ BOP means “bottom of the (income) pyramid” in Prof. C.K. Prahalad’s work. Prof. Stuart Hart prefers “base of the pyramid” as somewhat less pejorative toward the poor. WRI has helped these two establish the concept firmly in global discourse. The basic idea is that businesses ignore the 4 billion BOP customers at their peril because that is where the most dynamic future markets will be found.

⁷⁷ “Embrace entrepreneurship and innovation as antidotes to poverty. Wealth-substitution through aid must give way to wealth-creation through entrepreneurship.” C.K. Prahalad, “Aid is Not the Answer”, *The Wall Street Journal*, August 31, 2005.

The most efficient way to ignite and fuel this virtuous entrepreneurial cycle on a scale large enough to move the dial in a poor country may be through MicroFranchises.⁷⁸

Stephen W. Gibson sees MicroFranchises as an effective way to accelerate successful local enterprise creation, and that, ultimately, is the solution to global poverty.⁷⁹

Virtuous Enterprise Cycles

Once a businessman or woman makes a profit, even a very small profit, they have created wealth and own property. The challenge then becomes protecting that property and, if they are enterprising, eventually leveraging their assets to launch a new venture. A friend of mine made money printing software user's manuals. He sold his printing business and is now in real estate development and automobile dealerships. The jobs he created as a successful printer are still paying living wages to the employees of that original firm, but he has now created new jobs in other industries and the US economy has grown commensurately.

This virtuous enterprise cycle does not happen nearly often enough in the developing world.⁸⁰ Emerging countries are capable of impressive economic growth as Chile, India and China have recently demonstrated, but only when their entrepreneurs are empowered to make a profit, protect their property, and leverage assets to create new enterprises.⁸¹ Profitability, property protection and asset leverage are all things franchise networks tend to do very well.

Entrepreneurs are a Subset of the Population

Few people have the aptitude and temperament to successfully own and run a business or social enterprise. To be a successful enterpriser, one must be able to manage vision, risk, capital, marketing, production, people, personal life and change simultaneously.

Approximately one person in ten is a natural entrepreneur with the drive and ability to

⁷⁸ C.K. Prahalad laments the fact that most development projects never become anything more than a "contained experiment." C.K. Prahalad, presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004. The franchise business model, on the other hand, is all about controlled growth through highly replicable business formats.

⁷⁹ Stephen W. Gibson and Jason Fairbourne, *Where There Are No Jobs, Volume 4: The MicroFranchise Handbook*, (Provo, UT: The Academy for Creating Enterprise, 2005). A particularly effective poverty intervention may be to link a production facility (shop, mill, plant, service center, factory, farm, etc.) with a network of MicroFranchised support enterprises. When the yuan floats, which Tim Layton and others think is inevitable, the price of Chinese goods will rise overnight, and it will become more feasible to locate manufacturing production facilities in many other parts of the world. A second concept that shows enormous promise is to link production overruns, model obsolescence and slow moving inventory clearance with MicroFranchised distribution networks in the developing world. Seed Programs Inc. and Globus Relief are two organizations that currently employ this overstock distribution model.

⁸⁰ William Easterly calls this virtuous enterprise cycle the "increasing returns model" of economic growth and argues that since macroeconomic development aid and debt relief programs have failed utterly, the developing world needs small business strategies rooted in the fundamental verity that "people respond to incentives." William Easterly, *The Elusive Quest for Growth*.

⁸¹ Indeed, innovation and entrepreneurship may be the only long term competitive advantages an economy really has. John Hagel III and John Seely Brown, *The Only Sustainable Edge: Why Business Strategy Depends on Productive Friction and Dynamic Specialization* (Boston: Harvard Business School Publishing, 2005).

juggle that many balls in the air simultaneously, and some fraction of that group actually succeed in creating successful enterprises. Two people out of ten are capable of effectively managing an enterprise with adequate structure around them. To be optimally productive, most people (seven out of ten in my experience) should be teachers, production workers, clerks or some other form of employee. In the developing world, though, there simply are so few jobs available that virtually everyone is a de facto small time entrepreneur whether they like it or not. Hundreds of millions of tiny businesses almost never turn a profit and their impoverished owners eke out a subsistence livelihood that perpetuates intergenerational poverty.

My brother-in-law recently returned from a business trip to West Africa.⁸² He was appalled to see rows and rows of virtually identical produce shops where everyone was selling and hardly anyone was buying.⁸³ Somewhere among those underutilized produce merchants is an enterpriser capable of breaking out, growing their business, and creating jobs for their neighbors. In the current social, economic and political climate in Africa, though, most of that potential for enterprise will go unrealized.⁸⁴ When everyone is doing exactly the same thing on a small scale, everyone competes on price alone and Adam Smith's vaunted productivity through specialization never happens.⁸⁵ Geoff Davis estimates that perhaps one or two out of every forty women Microcredit clients is a "real entrepreneur who can really grow an enterprise."⁸⁶ The others will seldom progress beyond a subsistence level and would be much better off as employees if decent jobs existed. John Hatch indicates more or less the same thing, observing that nine out of ten Microcredit-enabled women "plateau their businesses" at a minimal level and invest in their children rather than grow their enterprise.⁸⁷

⁸² John Savage, personal communication, November 2004. John works for Savage Industries which does business in Mali and Senegal.

⁸³ I was driving around Lima, Peru years ago and happened upon an area of town where dozens of muffler mechanics were plying their trade on the side of a road. Each muffler technician had a pit they had dug and a few hand tools. Muffler pits stretched almost as far as the eye could see. A customer would drive up, haggle over the price, and pull their vehicle over one of the pits. Suddenly, a parts runner would appear with the appropriate replacement muffler, rental equipment would arrive on the scene, and sparks would begin to fly. Visiting with the mechanics, I learned that each one worked approximately 30 minutes every day and sat idle the rest of the time. No one earned very much because everyone competed solely on price. And the only barrier for a new entrant into this market was a set of tools and a hole in the ground. This copycat mentality that produces concentrations of similar businesses without significant differentiation is rampant in the developing world and is a major contributor to enterprise under performance.

⁸⁴ Scott Graham, FINCA's former country director in Malawi, contrasts the torpidity of the listless Malawian economy with the entrepreneurial energy evident among all socio-economic classes in South Africa. One key difference he notes: the franchise business model, thriving in South Africa, is practically non-existent in Malawi. Scott Graham, personal communication, November 2005.

⁸⁵ Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (First Edition London: William Strahan, 1776; Great Books of the Western World Vol. 39, Chicago: Encyclopaedia Britannica, 1986).

⁸⁶ Geoff Davis, CEO, Unitus. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

⁸⁷ John Hatch, Founder, FINCA. Presentation at the BYU Economic Self-Reliance Conference, MicroFranchise track, March 2005.

It seems that nature endowed a small percentage of humans with the “enterprise gene.” Successful societies are those where natural entrepreneurs flourish and create employment for their friends and neighbors.⁸⁸ MicroFranchises facilitate this because they tend to be larger enterprises than individually owned businesses and they tend to create local employment beyond the proprietor’s immediate family.⁸⁹ MicroFranchises also expand the pool of potential enterprisers from the few naturally gifted to the larger group of people who can successfully follow a well-designed operating system.⁹⁰

Wisdom Literature

Among the dozens of books and articles devoted to poverty alleviation in our era, five titles stand out for the compelling nature of the solutions they posit:

- 1998, Banker to the Poor: Micro-Lending and the Battle Against World Poverty by Muhammad Yunus.
- 2000, The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else by Hernando de Soto.
- 2002, “The Great Leap: Driving Innovation from the Base of the Pyramid” by Clayton Christensen and Stuart Hart
- 2004, The Fortune at the Bottom of the Pyramid: Eradicating Poverty through Profits by C. K. Prahalad.
- 2005, Capitalism at the Crossroads: The Unlimited Business Opportunities in Solving the World’s Most Difficult Problems by Stuart Hart.

These works clearly outline what causes poverty (exploitation), the results of poverty (enslavement), and the solution (liberating institutions that enable innovative, sustainable enterprise). This paper argues that the franchise business model is probably the most effective way to provide the uplifting and nurturing institutional support that oppressed people need in order to earn their way out of poverty. It may be the best way to efficiently deliver the solutions described in these path-breaking treatises.

- The Grameen family of enterprises includes over two dozen different entities, most of them offering franchises with financing packages to small business owners or cooperatives.⁹¹ Examples include the handloom enterprises of

⁸⁸ One is reminded of the statement attributed to the 12th century Hispano Arab philosopher Averroës that a just society is one that allows every woman, child and man to develop the possibilities God gave them.

⁸⁹ “The government of the Philippines is actively promoting indigenous franchises because franchised businesses are generally more successful and employ more people than independent enterprises.” Personal communication with Samie Lim, Chairman, Philippine Franchise Association, March 2005. Private English academies abound in Latin America. Most are quite small. The franchised Wizard schools founded by Carlos Martins in Brazil, though, teach 500,000 students with 15,000 employees in their 1,200 locations. Each Wizard school averages 12.5 employees. In 2004, Martins was honored as one of the top 10 enterprisers in Brazil and his franchise has expanded to the US and Japan. www.wizard.com.br.

⁹⁰ Many franchise psychologists and consultants insist that “intrapreneurs,” not “entrepreneurs” are more suitable franchisees. “Entrepreneurs tend to be highly independent, take a lot of risks and don’t need anyone to manage or get them fired up. Intrapreneurs are self managers, but they like to work within guidelines in concert with other people. Intrapreneurs can be creative within a structure. The entrepreneur needs to define his own structure.” Fred Berni, President, Dynamic Performance Systems, in *The Globe and Mail*, Toronto, July 9, 1999.

⁹¹ Muhammad Yunus, *Banker to the Poor*.

Grameen Uddog and the fisheries pond management of Grameen Motsho.⁹² Muhammad Yunus is again ahead of his time, moving beyond Microfinance into networks of replicable businesses. Don Terry thinks MicroFranchises are the “next generation” of Microfinance.⁹³

- De Soto clearly demonstrates that assets in the informal or underground economy do not form the basis for large scale capital formation like documented assets in the formal economy can.⁹⁴ Much of his work with the ILD involves titling real property and registering businesses.⁹⁵ MicroFranchises may greatly accelerate this process because hundreds or thousands of small, local businesses can enjoy the benefit of the franchisor’s official registered legal status.
- “The Great Leap” is an important adaptation of Clayton Christensen’s insightful work on “disruptive technology”.⁹⁶ Disruptive innovations generally address new or marginalized niche markets in the early stages of their life cycle because they are not yet on par with established mainstream products. Christensen and Hart show in their article why underserved BOP markets are ideal environments to launch new disruptive innovations.⁹⁷ MicroFranchises may be an effective way to deliver new disrupting technology to global BOP markets.
- Prahalad’s message is unmistakable: China and India are economic powerhouses with relatively low domestic cost structures who are beginning to address the needs of the poor. Multinational corporations who wish to remain viable and competitive in the future must address the needs of the four billion people living at the bottom of the income pyramid or risk losing market share to highly efficient Chinese and Indian innovators.⁹⁸ The franchise business model seems to be a very effective way for MNCs to engage the BOP.⁹⁹
- Much in contemporary capitalism is not sustainable when environmental and social considerations are taken into account. Hart deftly articulates the case for sustainable global development that honors triple bottom line principles. He shows how leading edge technology and new business models can help achieve

⁹² www.grameen-info.org

⁹³ Personal communication with Don Terry, Manager, The Multilateral Investment Fund, February 2005. For an articulate overview of the reasons MicroFranchising is vital to Microfinance, see John Hatch, *Why is MicroFranchising Important to MFIs?*, November 2005.

⁹⁴ Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (New York: Basic Books, 2000).

⁹⁵ www.ild.org.pe

⁹⁶ Clayton M. Christensen, *The Innovator’s Dilemma: When New Technologies Cause Great Firms to Fail* (Boston: Harvard Business School Press, 1997).

⁹⁷ Clayton M. Christensen and Stuart L. Hart, “The Great Leap: Driving Innovation from the Base of the Pyramid,” *Sloan Management Review* 44(1) (2002): 51-56. Three years after its publication, Clayton has an even “firmer conviction” about the Great Leap thesis. Clayton M. Christensen, personal communication, November 2005.

⁹⁸ C. K. Prahalad, *The Fortune at the Bottom of the Pyramid*.

⁹⁹ Several of Prahalad’s star exhibits utilize some variation of the franchise business model, e.g. Hindustan Lever’s Shakti Amma local sales consultants and Cemex’ Parimonio Hoy local promoters. “MicroFranchises are an appropriate vehicle for many MNCs to engage the BOP.” Personal communication with Al Hammond, February 2005.

the balanced equilibrium our planet needs so desperately.¹⁰⁰ MicroFranchises may be an excellent implementation of the mutually beneficial egalitarian capitalism Professor Hart describes.

In summary, MicroFranchising may be an effective delivery mechanism for some of the most compelling contemporary solutions to global poverty. The business model pioneered by Isaac Singer and perfected by the food service industry has a proven track record of lifting humans to ever higher levels of productivity through cooperation.

Contemporary Solution to Poverty	MicroFranchises as the Delivery Vehicle
Microfinance as pioneered by Muhammad Yunus, Grameen Bank; John Hatch, FINCA; Maria Otero, Acción International; and many others.	Many micro entrepreneurs struggle to effectively utilize the proceeds from a micro loan. MFIs should consider offering proven MicroFranchise business formats to their clients along with a financing package.
Asset titling and business registration as pioneered by Hernando de Soto through his Institute for Liberty and Democracy in an attempt to foment “property revolutions.”	MicroFranchise networks almost always operate as legally registered entities within the formal economy. Small local franchisees benefit from this legal status which allows them to create new capital by leveraging their assets.
Disruptive technology deployed at the BOP as articulated by Clayton M. Christensen and Stuart L. Hart.	The franchise business model may be the best way to rapidly deploy disruptive innovations like wireless communication, Internet connectivity, smart cards, solar power, LED lighting, etc. to the BOP on a large scale.
Multinational Corporations tailoring products and services to fit the needs and consumptive capacities of the 4 billion people at the base of the income pyramid as propounded by C. K. Prahalad.	MNCs have generally struggled to effectively engage customers and business partners at the BOP. Many of the most conspicuous success stories utilize some variation of the franchise business model. Prahalad’s critics argue that selling to the poor is not the same as serving them. MicroFranchises offer significant employment and ownership opportunities in addition to goods and services.
Sustainable development that honors the triple bottom line principles of environmental stewardship, social responsibility, and economic profitability as advocated by Stuart L. Hart.	Franchises offer control over best practices, distributed ownership and local governance. They may be a premiere mechanism to deliver on Hart’s vision of sustainable mutual value created through indigenous, inclusive capitalism.

¹⁰⁰ Stuart L. Hart, *Capitalism at the Crossroads*.

Variations on the Franchise Theme

For many in the industrialized world, the term “franchise” conjures up a mental image of hundreds or thousands of nearly identical fast food restaurants, but the franchise business model is much broader and more flexible than that. There are at least sixteen different kinds of business relationships that are variations on franchising. In each case, there is a symbiotic relationship between a local entrepreneur and a supportive institution that creates the environment and enables the framework for successful enterprise.

Franchising includes agency, co-op, distributor and representative business models. In some cases the local entrepreneur is a commissioned sales person. In others the local person is a consultant offering pre and post sales support. Storefront business models are often capital intensive, but also potentially lucrative for the owner(s). Most of the successful enterprises on earth could conceivably utilize one or more of these standards-driven, well documented franchise relationships to extend their market reach into the developing world. For franchisor and franchisee alike, a well designed and artfully administered franchise concept can be a consummate win-win.

Business Relationship	Examples	Characteristics
1. Product Franchise	Automobile Dealerships Professional Sports Bottling Plants	Relative Autonomy Local Name Recognition Capital Intensive
2. Business Format Franchise	Restaurants Lodging Properties Gas Stations Health Stores Pharmacies (Kenya) Cellular City (Philippines)	Brand Recognition Strict Operating System Fees, Royalties Financial Audits Operational Audits
3. Informal Business Format	Paleterias La Michoacana (Mexico) multinational	Branded Equipment Branded Supplies Loose Affiliation
4. Buyer’s Cooperative	Associated Food Stores (Utah) regional	Member-Owned Logistics
5. Producer’s Cooperative	Moroni Feed (Utah) Lijjat (India) multinational	Member-Owned Sales Member-Owned Logistics
6. Owner Operator	Truck Drivers Collectivo Drivers (Latin America)	Driver Owns Vehicle(s)
7. Delivery Route	Dairy Roundsmen (UK) Snack Foods Delivery Ice Cream, Soda Carts	Fixed Periodic Circuit Food and Perishables
8. Manufacturer’s Rep	Unilever Shakti Amma (India) Unilever Sales Reps (Vietnam)	Specialized Equipment Specialized Materials Local Sales Consultant Protected Territories
9. Journeyman	Mechanics Electricians, Plumbers	Tradesman Owns Tools Independent Contractor

Business Relationship	Examples	Characteristics
10. Piecework Jobber	Apparel Manufacturing Worldstock.com (Utah) multinational	Cottage Industries Semi-Finished Goods Finished Goods
11. Independent Operator	Hair Stylists Retail Market Stalls	Rents Chair or Space
12. Local Agent	Insurance Agents Real Estate Agents	Commissioned Sales Customer Service
13. Local Distributor	Avon Ladies Newspaper Vendors	Open Territories Informal Sales
14. Local Purveyor	Grameen Phone Ladies (Bangladesh, Uganda)	Scarce Village Resource
15. Local Promoter	Cemex Patrimonio Hoy (Mexico) multinational	Commissioned Agent Organizes Self Help Groups
16. Credit Franchisee	UMU (Acción) Existing Merchants (Uganda)	Storefront Assesses Risk Disburses Loan Proceeds Collects Loan Payments

Characteristics of Franchise Relationships

In each of these 16 situations, a relatively autonomous local entrepreneur owns means of production or an independent business that is closely affiliated with a larger and more powerful local, regional, national or global enterprise. The large enterprise benefits because the entrepreneur provides some of the start-up capital, most of the manpower, and local knowledge and contacts. The entrepreneur has a strong incentive to be profitable. The entrepreneur benefits because the large enterprise provides institutional infrastructure that would be difficult for an individual to build or acquire on their own.

For micro business people in the developing world as for small business people in the industrialized world, franchises tend to be less risky and more profitable than totally independent enterprises. And in many forms of franchise relationships, local owners can build up equity in their businesses through asset acquisition or customer goodwill while they are earning wages. The franchise relationship tends to insulate the entrepreneur from many of the shocks of the open market by providing a micro business person a degree of stability, security and predictability that they could rarely achieve on their own. At its heart, a franchise is a symbiotic relationship between local entrepreneurs and an enabling institution.¹⁰¹ Franchises generally promote and support a mutually beneficial product or service brand. Franchising is a proven method of replicating successful small enterprises on a local, national, regional or global scale.

¹⁰¹ A version of this paper was first presented publicly at a dialogue hosted by the Center for Economic Self-Reliance at BYU on November 5, 2004. After the presentation, Prof. Don Adolphson challenged me to define a franchise in ten words or less. My ten words: “a symbiotic relationship between local entrepreneurs and an enabling institution.”

More Franchise Characteristics

Franchises are inclusive, democratic capitalism. They distribute ownership and wealth widely throughout a target population.¹⁰² They are cooperative entrepreneurship, a system where costs, risks, financing and profits are shared between an enabling franchisor or parent company and an implementing franchisee or local business partner based on a mutually profitable contractual relationship of shared ownership. Franchising is a way to effectively clone successful businesses based on a proven operating system.¹⁰³ Stephen W. Gibson calls franchises a “business in a box.”¹⁰⁴ You don’t need to be a business genius to run a profitable franchise. “Anyone who can make an ice cream cone can run a Dairy Queen,” the people in Minneapolis say.¹⁰⁵ Kevin Miller, head of the North American Subway Owners Council, likes to joke that “Fred DeLuca made thousands of dumb people millionaires.”¹⁰⁶

Franchise organizations are potentially highly scalable as 7 Eleven demonstrates with 27,000 stores in 18 countries.¹⁰⁷ The concept works in almost every country and culture on earth.¹⁰⁸ When governments and most other societal institutions are weak and corrupt

¹⁰² Traditional hierarchical businesses concentrate wealth in the hands of a few privileged elites. Franchise systems distribute ownership and wealth throughout their network. The difference is obvious when one analyzes the annual Forbes list of the world’s billionaires. Some of the top franchisors on earth (the Marriotts, Fred DeLuca of Subway) look positively modest among their billionaire colleagues because they have shared their wealth directly with thousands of local owners. This wealth sharing can be quite dramatic. “The rule of thumb in Brazil is that the US franchisor receives about 20% of what the Brazilian master franchisee receives.” Personal communication with Paulo Cesar Mauro, Director of International Relations, ABF (Brazilian Franchising Association), March 2005.

¹⁰³ The Illinois based franchise consultant Francorp advertises with a photo of a rabbit and the tagline: “The art of reproduction.” The franchising industry advertises the fact that a new franchise location opens somewhere in the US every 8 minutes. Information gathered at the International Franchise Association 45th Annual Convention, Hollywood, FL, March 2005.

¹⁰⁴ Stephen W. Gibson and Jason Fairbourne, *The MicroFranchise Handbook*.

¹⁰⁵ This endearing expression comes from Scott Hillstrom, founder, Health Stores Foundation and a resident of the greater Minneapolis area. Scott is one of the founders and leading proponents of the incipient MicroFranchising movement.

¹⁰⁶ Personal communication with Kevin Miller, March 2005. Kevin implies no pejorative slander. His colloquialism is simply another way of saying that you don’t need to be a business genius to own and manage a successful franchise location.

¹⁰⁷ McDonalds has 31,000 locations operating in 119 countries. Subway has 23,000 locations operating in 77 countries. Burger King operates 11,000 locations in 61 countries. Information comes from an AP news story about McDonalds’ 50th anniversary in April 2005, personal communication with Fred DeLuca, co-founder of Subway in March 2005, and a presentation by Marlene Gordon, intellectual property attorney for Burger King, at the IFA Convention in Hollywood, FL, March 2005. Franchisee organizations can also grow large. Some multi unit franchisees own over 900 locations. Michael H. Seid, Managing Director, Michael H. Seid & Associates. Presentation at IFA Convention, Hollywood, FL, March 2005. Fred DeLuca thinks Subway and other fast food networks could eventually grow to 100,000 locations worldwide. Fred DeLuca with John P. Hayes, *Start Small Finish Big* (New York: Warner Books, 2001).

¹⁰⁸ A large global franchisor with Asian roots is Japan’s Kumon Institute of Education which has 23,000 locations in 43 countries. www.kumon.com. Even these unit numbers pale in comparison, though, to the potential that MicroFranchise networks have in the developing world. For example, there are currently 130,000 Grameen telephone ladies in Bangladesh, and 200,000 are expected by the end of 2005. Personal communication with Muhammad Yunus, July 2005. Successful replications of Grameen Village Phone now operate in Uganda and Rwanda. Personal communication with Barbara Weber, July 2005.

(that describes most of the developing world¹⁰⁹), a parent company, franchisor or master franchisee can be a kind of surrogate government, providing important goods and services that the franchisee would never have access to absent this institutional support. At the same time, well-managed apex franchise organizations generate cash flow and earn a profit. The humanitarian NGO pattern – solicit donations in wealthy countries to fund perpetual deficits in emerging markets – becomes much more self-sustaining using the franchise business model. The ultimate in sustainability is a locally-owned profitable business enterprise with a viable indigenous value proposition that practices social and environmental responsibility.

Social Franchises

Typical MicroFranchises are very small businesses that seek to maximize profit and return on investment. A social franchise, on the other hand, will likely never be profitable for both the franchisee and the franchisor concurrently. A social franchise seeks to accomplish the most good for the greatest number of people and almost always requires a third party funding source to underwrite at least a portion of its operating costs.

In most societies, health care, education and the arts are social goods that are nearly impossible to distribute via open markets using laissez faire laws of supply and demand. A primary school student, for example, can seldom pay the total cost of his or her own education, nor can parents. If society wants that child educated, a social entity (usually the government) must step in to pay at least a portion of the expense.

Advantages of the Franchise Business Model

Forty years ago, few franchises existed in the US. Today they dominate most main streets and strip malls.¹¹⁰ At the International Franchise Expo held in the Washington, D.C. Convention Center in May 2004, thousands of unique franchise business opportunities were on display or represented. In the developed world, relatively few new independent enterprise start-ups are still in business after five years. On the other hand, a significantly higher percentage of new franchise locations are still viable five years out.¹¹¹ Franchising generally works well relative to small independent businesses because:

- Franchisors generally service viable local markets.
- Franchisors typically employ skilled professionals in key positions.
- Franchisor requirements tend to produce quality applicants.
- Franchisors expend significant resources to perfect their operating systems.¹¹²

¹⁰⁹ Weak institutions are “the hallmark” of poor countries. “U.S. Foreign Aid: Meeting the Challenges of the Twenty-first Century,” USAID White Paper, January 2004.

¹¹⁰ As I was fueling my car recently in Lehi, Utah, I turned and counted every business that was visible in a 360 degree arc. I counted a total of 20 businesses in my field of vision. 18 of them are franchises.

¹¹¹ New Business Magazine, “Franchising Shows Strong Growth,” www.newbusiness.co.uk 2004-02-07. AFDB’s article *Franchising to Support SME’s Development in Africa* cites data from several countries.

¹¹² The importance of a franchise operating system can hardly be overstated. This highly refined and continuously improving set of standards and procedures codified for replication is what sets a franchise concept apart from a traditional small business. Sun Microsystems Chairman Scott McNealy is fond of saying “the network is the computer.” In a franchise, “the system is the business.” Fanatical attention to (...continued)

- Franchisors generally inspect and internally audit their operations.
- Franchisors tend to promote truth in advertising and packaging.
- Franchisors generally price their products rationally across regions or nations.
- Franchisors tend to control site selection which prevents market saturation.
- Franchisors generally innovate to stay abreast of changing market conditions.
- Franchisors can terminate underperforming units quickly.
- Franchisors generally take a long term view of their business.¹¹³
- Economies of scale allow for intelligent and efficient procurement.
- Franchise networks can often afford access to current technology & equipment.
- Franchise networks tend to foster rapid dissemination of best practices.
- Franchises tend to enforce productive standardization and uniformity.
- Franchises strike an appropriate balance between centralization, decentralization.
- Franchises allow for productive local adaptation and pooled creativity.
- Franchises thrive on intensive bi-directional information transfer.
- Franchises distribute ownership which promotes collaborative methodologies.
- Franchises tend to be housed in specialized facilities rather than on the street.
- Franchises tend to distribute professionally & hygienically packaged products.
- Franchises tend to distribute branded products and disparage piracy.
- Franchises are readily fungible if they are successful.
- Franchises are often viewed as collateralized assets by local financial institutions.
- Franchise networks can quickly scale up regionally, nationally, or globally.¹¹⁴
- Franchises often create jobs for people beyond the owner's immediate family.
- Franchises are often viewed as relatively low risk business ventures.
- Franchises often come with bundled financing packages built in.
- Franchises generally enjoy relatively high sales volumes in their market.
- Franchises tend to be adequately capitalized and cooperatively marketed.
- Franchises lend themselves to professional management, freeing up the owner.
- Franchises can penetrate rural areas based on strength from an urban core.¹¹⁵
- Franchises can help obscure communities develop civic pride.¹¹⁶

detail on the part of Ray Kroc allowed thousands of owners in dozens of countries to run successful businesses by focusing simply on McDonalds' famous three metrics: quality, service and cleanliness. A franchise operating system is essentially the same thing as a quality plan that allows a company to achieve ISO 9001 certification: plan precisely, document rigorously, and measure continuously which enables a feedback loop that results in TQM Total Quality Management. "We deliver peace of mind and repeatable success" is the way Varsity Contractors expresses this idea. Michael Gerber in his excellent *E Myth* series stresses this bottom line for a small business owner: If you want to be successful and grow your business, think and act like a franchisor. Michael Gerber, *The E Myth Revisited: Why Most Small Businesses Don't Work and What to Do About It* (New York: Harper Collins, 2001).

¹¹³ "Franchising is all about investing resources up front that pay off in 5 – 10 years." Bachir Mihoubi. Presentation at the IFA Convention, Hollywood, FL, March 2005.

¹¹⁴ Gary Heavin's Curves for Women fitness centers, the fastest growing franchise in history, have expanded to 9,400 locations in several countries since 1995. www.entrepreneur.com, Franchise Zone.

¹¹⁵ MicroFranchises may be "particularly suited for penetrating rural underserved areas." John Paul, *Private Sector Strategies for Providing Healthcare at the Base of the Pyramid*, WRI, A Development Through Enterprise Report, November 2005.

- Franchisees self-select so they tend to be highly motivated.
- Franchisees have time and money invested so they tend to manage attentively.
- Franchisees usually bank with formal financial institutions.
- Franchisee education tends to be highly relevant and therefore effective.¹¹⁷
- Franchisees are generally required to keep accurate accounting records.
- Franchisees who are successful with one line of business can often add a second.
- Consumers generally appreciate the quality and consistency of standard brands.

The Rule of Law

Even more significant, there is one feature of the franchisor/franchisee relationship that is of paramount importance in developing nations. The franchisor develops a franchise operating system and requires compliance to protect the brand. A franchisee who does not follow that operating system may lose their franchise. In other words, franchisees must play by the rules or risk forfeiting their investments. It is in the franchisee's own self-interest to be a law abiding citizen within the franchise community and the franchisor can enforce the rules with both a carrot and a stick.

Margaret Thatcher is prescient in her comments praising Hernando de Soto's imperative book *The Mystery of Capital*. "... It addresses the single greatest source of failure in the Third World and ex-communist countries – the lack of a rule of law that upholds private property and provides a framework for enterprise." It is a daunting, Herculean task to contemplate the effort required to transform a country with endemic corruption where the informal sector dominates the economy into a law-abiding society that protects private property and allows entrepreneurs to leverage assets. In many countries, a violent *coup d'état* may be required (Pinochet in Chile comes to mind). It is much easier to select high potential enterprisers, train them in a franchise operating system, and then let their own self-interest guide them to take advantage of the franchise network's built-in property protections. With a franchise system providing some of the services that ambient social institutions do not offer the poor, it is not too difficult to envision large numbers of successful MicroFranchisees in developing countries selling their businesses, acquiring a second franchise,¹¹⁸ or getting a loan against their assets to finance a new venture.

¹¹⁶ Growing up in the 60's, I remember the excitement young people felt to finally get a McDonalds in their town. Iconic franchises with national cachet can improve a small community's collective self-esteem. In the developing world, building key MicroFranchises in outlying areas could help stem the tide of rural to urban economic migration by providing alternatives to small town ennui.

¹¹⁷ Martin Frey believes that in countries where there is work but no jobs, old-fashioned apprenticeships could empower young people. The franchise business model seems well-suited to apprentice-like on the job training systems that eventually lead to management and then ownership opportunities.

¹¹⁸ Subway currently has 23,000 locations in 77 countries owned by 10,000 franchisees. Personal communication with Fred DeLuca, Co-Founder, Subway, March 2005. This means that the average Subway Franchisee owns 2.3 locations. Total system revenues are \$8 billion, so global average unit volume is about \$345,000. Many MicroFranchise networks will have similar multi unit franchisee dynamics, albeit with much smaller AUV numbers.

MicroFranchising can incite a stealthy commercial revolution that eventually brings an underperforming society to a tipping point.¹¹⁹

Franchise Networks as a Surrogate Rule of Law

In 1973, I was in the home of a college professor in Arequipa, Peru. After a lively conversation about the global economy, this academic opined, “*Ojalá nos hubieron conquistado los Ingleses.*” “I wish the English had conquered us.” What he meant was that Peru would be much more advanced economically if Peruvians generally respected the rule of law. (When Latin American immigrants come to the US, they are often surprised to find that most drivers obey traffic rules and most citizens pay taxes.) Despite diverse cultural mores,¹²⁰ franchise operating systems can serve many of the same functions as a rule of law while franchise networks can be wonderfully supportive social institutions.

Franchises and Intellectual Property Protection

Many multinational corporations employ business models that depend on the kind of intellectual property protection common in the developed world. Those companies are often disappointed when they try to do business in emerging markets like China or Brazil where endemic piracy and counterfeiting are ways of life. Public policy in those countries often aids and abets this widespread flagrant disregard for intellectual property rights.

The franchise business model is all about brand protection.¹²¹ International franchise consultants are quick to point out that entrepreneurs abroad do not strictly “buy and sell franchises”. They “license a brand”.¹²² It is in the self-interest of everyone associated with a franchise network – the franchisor, master franchisee and local franchisee – to protect the brand which delivers ongoing mutual value. Proliferating MicroFranchises throughout an economy will be an effective way to educate large numbers of people about the benefits of IPP as local owners work to protect and strengthen their co-owned brands.

Franchise Networks as Social Liberators

One other aspect of the franchise business relationship is very important to international economic development. In Latin America, for example, the *patron* is the boss, the owner, while most employees are a *peon*, an underling, a have-not. Franchisees are not nearly as deferential to their parent companies as employees tend to be to their bosses. After all, a franchisee is an owner. Franchises empower their many owners financially,

¹¹⁹ Malcolm Gladwell, *The Tipping Point: How Little Things Can Make a Big Difference* (New York: Little, Brown & Company, 2000)

¹²⁰ “There are cultural differences between countries, but in franchising there are more similarities than differences.” Donald Dwyer, Jr. Presentation at the IFA Convention, Hollywood, FL, March 2005.

¹²¹ Burger King, for example, currently operates in 61 countries, but they have legally protected their brand in many additional countries where they expect to do business in the future. The strategic plan at Burger King calls for protecting their brand 5 – 10 years before they actually begin operations in a new country. Presentation by Marlene Gordon, IFA Convention, March 2005.

¹²² Michael Seid. Presentation at the IFA Convention, Hollywood, FL, March 2005.

but also emotionally and socially. In fact, it is commonplace for franchisors to maintain a certain percentage of “company stores” among their locations to prevent their franchisees from becoming too powerful and dictating terms back to the home office.¹²³ Many franchisees band together in owner’s councils or associations to promote their common interest. Franchisees are a rich source of productive innovation in many franchise networks. The social empowerment that franchise networks offer is one reason the SBA recommends franchises as a good first venture for women and minority entrepreneurs.¹²⁴

Networks versus Hierarchies

The Internet is a global distributed peer to peer network largely self-governed by rules, standards and protocols. A mainframe computer system is a hierarchical platform with command and control exercised by privileged elites at the top of a power pyramid. The EU is an increasingly centralized network of independent states who share some common infrastructure. The US is a centralized federal republic with hierarchical control emanating from the capital and 50 subsidiary capitals one level down on the org chart. Rotary International is a global network of largely self-governing clubs bound together by a common value set and similar operating procedures. The US Army is a global force with a clear chain of command stretching from the Commander in Chief to the newest recruit in boot camp. Franchise systems are largely self-governing peer to peer networks.¹²⁵ Traditional large domestic and multinational companies are generally centralized hierarchies.

Both organizational structures have advantages and disadvantages. Hierarchies can be very efficient. They can focus massive force quickly. With enlightened leadership, hierarchies can be liberating, transparent, nurturing, egalitarian and sustainable. With ego-centric leadership, though, hierarchies often become repressive, corrupt, exploitative, elitist and fragile. Malevolent ego centricity fomenting a hierarchical pecking order of exploitation at all levels of society is what creates and perpetuates the global tragedy of institutional poverty. Networks, on the other hand, enjoy intrinsic advantages that make them superior vehicles to help people lift themselves out of poverty:¹²⁶

- Networks are democratic – nodes enjoy a peer to peer relationship.
- Networks tend to self-govern through consensus rather than fiat.

¹²³ Conventional wisdom in the industry is that a franchisor should own 20 – 30% company stores. This builds credibility with the franchisees. It provides a platform for pilot tests and new roll outs. It prevents a lot of poor ideas from being implemented. Excerpted from a presentation by Donald Dwyer, Jr., Director, International Operations, The Dwyer Group, IFA Convention, Hollywood, FL, March 2005.

¹²⁴ www.sba.gov

¹²⁵ A typical franchisor has 1 support staff person at HQ for every 35 international franchisee locations. Donald Dwyer, Jr., Director, International Operations, The Dwyer Group. Presentation at the IFA Convention, Hollywood, FL, March 2005.

¹²⁶ I recommend Tom Munnecke’s “Networked Theory of a Better World”. www.omidyar.net/group/netchange Jeffrey S. Nielsen argues that rank based hierarchies foster secrecy and miscommunication while peer-based groups “harvest the full intelligence of the organization” because “genuine communication only occurs between equals.” Jeffrey S. Nielsen, *The Myth of Leadership: Creating Leaderless Organizations* (Mountain View, CA: Consulting Psychologists Press, Inc. 2004). The US presence in Iraq illustrates this point. A hierarchical military force can topple a standing army, but nation building requires widely diffused networks that gradually win hearts and minds.

- Networks tend to empower participants by broadening their horizons and giving them a voice.
- Networks can be adapted readily to accommodate local diversity.¹²⁷
- Networks are resilient because they spring from a grassroots folk base.
- Networks are robust because decision points are widely distributed.
- Networks are often transparent – they generally foster an environment of full and open disclosure.
- Networks tend to limit spectacular failures because poor ideas or ineffective practices are not likely to proliferate.
- Well designed and competently managed networks can be partially self-propagating. In fact, once they reach critical mass, networks can be virtually unstoppable because their power base is so widely diffused.
- Very small network nodes can still function effectively.
- Networks often bring together diverse viewpoints from people who would not be likely to interact with each other in a hierarchical structure. In other words, networks are generally more heterogeneous than command and control platforms.
- Hierarchies have an advantage when centralized force is important, but in many situations decentralized influence is even more powerful.¹²⁸

After analyzing fifty cases of successful pro poor enterprises in developing countries, David Wheeler and his team from York University in Toronto determined that “sustainable local enterprise networks” provide the human, social, financial and ecological capital low income communities need to create virtuous cycles of economic growth.¹²⁹

Access to the Market for Risk

Latin Americans frequently hear the phrase “*Si Dios quiere*,” “God willing.” Impoverished people have so little control over their own destinies that they often become fatalistic. Cultural legacies contribute to this lack of empowerment. When Spanish entrepreneurs sent ships abroad, they formed mutual stock companies and shared the risk of the voyage. If their ship came in laden with gold and silver, the owners rejoiced. If their ship foundered or was captured by English pirates, the owners often went bankrupt. Their fate was in God’s hands. English entrepreneurs also sent ships abroad through mutual stock companies, but they had Lloyds of London. If their ship came in laden with spices and tobacco, the owners rejoiced. If their ship suffered misfortune, at least the owners were not completely wiped out.

¹²⁷ Because of cultural sensitivity, the franchise network “Church’s Chicken” goes by the name “Texas Chicken” in the Middle East. Bachir Mihoubi, VP of Global Franchising, Caribou Coffee. Presentation at the IFA Convention, Hollywood, FL, March 2005. “Franchising is all about control with local adaptation.” Lee Vala, Sr. VP, The Quiznos Corp. Presentation at IFA Convention, Hollywood FL, March 2005.

¹²⁸ The EU, for example, often outvotes the US at the WTO because the EU brings 25 independent votes.

¹²⁹ Wheeler posits the SLEN model of a “trust-based, densely networked environment.” Wheeler, David, et.al., “Creating Sustainable Local Enterprise Networks,” *MIT Sloan Management Review*, Fall 2005.

Because they employed superior forms of business organization that protected property through shared risk vehicles like insurance, the English had more control over their own fortunes. This gave them greater confidence in the future and confidence is the fuel that feeds the virtuous cycle of enterprise growth. Typical micro enterprisers in the developing world survive on such slim margins for error that the slightest problem can be devastating. If they don't work today, they may not eat tomorrow. Hence, the extreme fatalism of *Si Dios quiere*. Having a franchise network to support and indemnify them through access to the market for risk empowers these tiny business owners and gives them the confidence they need to save, invest and grow their enterprises.¹³⁰

Discipline and Compliance

The discipline franchisors can enforce up and down their franchise network makes this form of business organization an effective solution for some very difficult problems. For example, billions of dollars are being spent right now trying to find efficient methods of essential drug distribution in the less developed world. The Gates Foundation,¹³¹ the Clinton Foundation,¹³² President Bush's PEPFAR fund¹³³ and others struggle to discover ways to get appropriate pharmaceuticals in the hands of those who desperately need them. Health care delivery systems in much of the world are riddled with corruption at all levels. Doctors and nurses who are paid very poorly by Western standards steal drugs from hospital stocks and sell them on the black market to supplement their incomes. Hapless consumers are often unable to distinguish between authentic medicines and cunning counterfeits. Drug faking has been called "the greatest evil of our time."¹³⁴

Franchised pharmacies are much more likely to self-regulate and enforce rational dispensing practices with quality medicines because the inspectors/auditors who come out from headquarters on a regular basis can revoke a franchisee's license if they find a pattern of irregularities. Peer pressure from other franchisees also helps keep local unit owners in conformity.¹³⁵ It is in the self-interest of franchisees to obey the rules since compliance protects their investments and strengthens their co-owned brand.¹³⁶

¹³⁰ I am indebted to Prof. Don Adolphson of the George W. Romney Institute of Public Management, Marriott School, BYU for helping me understand the crucial role the market for risk plays in facilitating virtuous cycles of economic growth in both public and private enterprises.

¹³¹ www.gatesfoundation.org

¹³² www.clintonpresidentialcenter.org

¹³³ www.usaid.gov/our_work/global_health

¹³⁴ Dora Akunyili, Director of Nigeria's Food and Drug Administration, *Time*, November 7, 2005. When Dr. Akunyili assumed her post in 2001, 80% of the drugs sold in Nigeria were adulterated or counterfeit.

¹³⁵ Humans have an innate sense of fairness and an affinity for punishing cheaters. Ernst Fehr says that "altruistic punishment is the glue that holds society together." Ernst Fehr, et. al., "Neurobiology of Altruistic Punishment," *Science*, August 27, 2004. Self-interest magnifies this tendency to discipline errant behavior as owners interact within franchise networks.

¹³⁶ Scott Hillstrom shared this powerful insight. His Health Store pharmacies in Kenya revoke a franchisee's license for clinical or documentary non-compliance. Franchise networks deliver quality products and services in environments where command and control hierarchies routinely fail.

Franchise Networks as Savings Vehicles

Many governments try desperately to get their citizens to save more money. Capital formation happens when surplus value gets stored as endogenous savings so it is available for future investment. The Banco del Ahorro Nacional in Mexico for instance, works to foment a “savings culture” among the working class in that nation.¹³⁷ Forced savings are not unusual. Social security in many countries is simply government mandated retirement savings. Many highly regarded Microfinance institutions like ProMujer¹³⁸ and Freedom from Hunger¹³⁹ deliver education, health and legal services to their clients in addition to micro banking. These additional services are generally funded through automatic withdrawals from compulsory savings accounts. Because franchisees pay regular royalties, rents or fees back to the franchisor and/or work largely on commission, the franchise business model lends itself well to a system of forced savings for retirement, health insurance premiums, or even a rainy day fund.

Transparent Franchises versus Corruption

C.K. Prahalad in his seminal book, *The Fortune at the Bottom of the Pyramid*, eloquently describes the “poverty penalty.” It is cruelly ironic that the poor in most nations actually pay much more for the same goods and services than their more affluent counterparts in richer neighborhoods.¹⁴⁰ Much of the problem stems from petty profiteering slumlords who exploit their neighbors by protecting “shantytown monopolies.” MicroFranchises can address this problem in two ways. First, franchise systems tend to enforce transparent, rational and often regional or national pricing, so MicroFranchises could provide the poor with affordable options for the goods and services they purchase.

Second, just as England progressed when the small businessmen of that “nation of shopkeepers” acquired political power, poor nations will develop when marginalized business owners stand up to societally-sanctioned corruption and demand transparency.¹⁴¹ The MicroFranchise concept has the potential of politically empowering large numbers of small entrepreneurs¹⁴² who tend to be opinion leaders in their communities.¹⁴³ It is no

¹³⁷ www.condusef.gob.mx/informacion_sobre/patronato/patronato.htm

¹³⁸ www.promujer.org

¹³⁹ www.freedomfromhunger.org

¹⁴⁰ Clean water and credit are two commonly cited examples of goods and services where the poverty penalty can increase prices in poor neighborhoods by a factor of 10 or more.

¹⁴¹ I was in Mexico City many years ago and took a Grey Line tour of the metropolitan area. As the tour bus drove through one of the most affluent neighborhoods in town, the guide mentioned that the largest house in the zone belonged to the Mexico City Police Chief. Many years later, I was in a remote part of Mexico talking with an older gentleman about his son who had recently graduated from the police academy. “*Por fin le dieron su esquina*” the man said. “My son finally got his corner.” In other words, his son would be OK financially because he could now take home all the bribes he could extort from his assigned intersection. When politicians lack the will to clean up this kind of blatant corruption, it will only happen through pressure from business leaders because the average person on the street feels powerless to affect deeply rooted institutional extortion. In India it is called “speed money.” In Peru they call it a “coima.” In Mexico it is a “mordida” or “bite.” Venezuelans say “matraca.” Bribes and corrupt payoffs lie at the very heart of poverty in any language.

¹⁴² Large numbers of people with “economic stakes in their society” will “demand decent public services,” which in turn will “promote growth.” “Micro no more,” *The Economist*, November 5, 2005.

accident that one of the most powerful franchise organizations in Mexico (Laboratorios Best/Farmacias Similares¹⁴⁴) also leads the fight against corruption in that country through their MNA initiative.¹⁴⁵

Christopher Rodrigues says that underperforming economies are characterized by “money under the table, under the bed, and under the water line.” Informal shadow economies (the black market) range from an average of 14% in the OECD states to 70% in the very worst economies.¹⁴⁶ Corruption and informal economies go hand in hand.¹⁴⁷ MicroFranchises mitigate both perverse influences. The very nature of the franchisor franchisee relationship tends to promote a culture of full and open disclosure.

Modern Payment Systems

In 2004, 19% of world consumer expenditure was processed through electronic payment systems (VISA, Mastercard, etc.). That figure is expected to rise to 40% by the year 2015. This is significant because E payments have major beneficial economic multiplier effects:

- They lower transaction costs. Cash handling is expensive.
- They stimulate consumption which increases GDP.
- They increase governmental efficiency by reducing bureaucracy. (2/3 of all government employees in most countries could be replaced by well-written computer programs with far better service to the constituents.)
- E payments also increase the level of financial intermediation in a country since cash reserves reside inside the formal financial system where every dollar contributes to the bank multiplier effect.
- E payment systems increase overall financial transparency in an economy.
- They also tend to promote rational tax structures and force merchants to comply with local tax laws.

Christopher Rodrigues uses the analogy: Cash is like walking to the market. Electronic payments are like riding a bicycle. Credit is like a bicycle with gears.¹⁴⁸ For development to be truly effective, countries need credit bureaus with standardized scoring, modern payment systems and effective communication infrastructures. Proliferating MicroFranchises throughout an economy will speed adoption of all these good things.

Note: VISA will soon have a wireless POS device. Theoretically, any merchant who can afford a cell phone will be able to accept plastic.

¹⁴³ Kapur and McHale call these “feisty people with the spark and the ability to resist corruption and incompetent governance” “institution builders”. Devesh Kapur and John McHale, *Give Us Your Best and Brightest* (Washington, D.C.: Center for Global Development, 2005).

¹⁴⁴ www.porunpaismejor.com.mx/EmpresasComerciales.htm

¹⁴⁵ www.porunpaismejor.com.mx/EmpresasSociales.htm

¹⁴⁶ Christopher Rodrigues, President and CEO, Visa International. Presentation at the WRI Conference “Eradicating Poverty through Profit: Making Business Work for the Poor”, San Francisco, December 2004.

¹⁴⁷ Corruption “raises the cost” of every transaction and allows “undesirable transactions” to take place, undermining consumer confidence. “The Hidden Wealth of the Poor,” *The Economist*, November 5, 2005

¹⁴⁸ Christopher Rodrigues, Presentation at WRI, San Francisco, December 2004.

Case Brief: Street Vendor Beatriz Lagos in Cuzco, Peru

Beatriz Lagos sells snack foods from a tricycle cart a few blocks from the main plaza in Cuzco, Peru. She gets up at 5:45 a.m. and retires at 11:00 p.m. six days a week. Her tiny house is far from the center of town, so she must rent a parking space in a secured lot to store her tricycle overnight. She rents her tricycle from her supplier. Her inventory is worth about \$150 at replacement cost, but she does not own it. It is on loan from her supplier and she pays interest on it at the rate of 10% per month. Her supplier requires that she make daily interest payments. Since she operates her cart 14 hours per day, a lantern is required for light. Lantern fuel costs \$1.80 per week.

Pilferage is a serious problem because all inventory shrinkage reduces her bottom line by the cost of goods plus the carrying cost of her flooring loan. A band of street urchins once overturned her cart and helped themselves to about one third of the scattered snacks before she and a passer-by scared them away. It took Beatriz several months to recover from that financial reverse. She pleaded with her supplier to at least forgive the interest on that distressed inventory, but he refused. Her son now helps her guard the cart during certain hours of the day, even though he is bright and would much rather stay in school.

Outdated inventory is a constant concern because her supplier does not rotate stock or manage shelf lives. Once she takes product through her supplier's door, she cannot return it. She can sell it, consume it, give it away, or dispose of it, but she has to pay for it with interest in any event. Once she was sold a box of D'Onofrio Sublime chocolate bars that were old and full of worms. The box looked fine on the outside. It was only after her customers opened the individual candy bars that the problem became apparent. She tried to return the defective box to her supplier, but he refused to help her.

Itinerant beggars stop by her cart frequently asking for a handout and occasionally she gives something away to a particularly disadvantaged person.irate customers often berate her because of her high prices. Large food processors like Nestlé run TV commercials advertising products at a certain price. Beatriz' cost from her supplier is often 10-15% higher than the advertised price on TV, so after she adds her markup, many customers complain. About once a week, a police officer comes along, expecting a bribe. Beatriz runs an informal, unregistered business that is technically illegal. If she did not pay off the policeman, he could make trouble for her, so she gives him a little money.

On a good day, she takes home \$4. Most days it is \$2 for an effective pay rate of 14 cents per hour. Beatriz Lagos, for all practical purposes, is a slave. She has been marginalized and is being oppressed by forces beyond her control. She bears most of the risk and realizes little of the benefit in an exploitative relationship. There are hundreds of Beatrices in Cuzco, Peru, and millions all over the developing world. Any of several institutionalized MicroFranchise systems could liberate Beatriz Lagos as surely as John Mitchell and John L. Lewis liberated Appalachian coal miners by organizing them in the early part of the 20th century.¹⁴⁹

¹⁴⁹ Personal communication with Beatriz Lagos and members of her family, November 2001.

Case Brief: Vodacom Telecom Kiosks in South Africa

With \$60 billion in annual revenues, Vodafone is the world's largest wireless phone company. They own 35% of Vodacom in South Africa. Much of Vodacom's business with lower income customers comes from prepaid phone cards which are serviced from retail storefronts. Vodacom maintains a network of 5,000 franchised telecom kiosks called "phone centers" throughout the country. Vodacom owns the structures and some fixed equipment. Local franchisees own their equipment, inventory and customer relationships. This symbiosis between a huge multinational corporation and small local entrepreneurs is both enlightening and encouraging:

- Franchisees are given a great deal of business training which they value highly.
- Each kiosk provides jobs for an average of 5 employees.
- Vodacom franchises are very profitable relative to other business opportunities.
- Many franchisees have become quite successful, leveraging assets to found new enterprises in other industries.¹⁵⁰

Case Brief: ICICI's Local Community Banks in India

ICICI Bank is the second largest bank in India with a 30% market share. They are also one of the largest insurers in the country. They were the first Indian firm to be listed on the New York Stock Exchange. Through an acquisition in southern India, ICICI inherited an existing Microfinance business. Although loan default rates were near zero, operating costs were high so ICICI concluded that traditional Microfinance where they dealt directly with large numbers of low income customers does not work because it is not profitable.¹⁵¹ So, the bank changed their business model and began to develop locally franchised partners. These small, semi-independent Microfinance institutions adapt their products to the diverse Indian marketplace, backed up by a menu of options that are available to them through the formidable power of a major world bank. Local MFI's provide ICICI with profound local reach. ICICI in turn provides their partner franchisees with new products, sophisticated services and unprecedented global access.

- 30 local MFI's are now engaged in the network.
- These 30 local institutions collectively service 1 million households.¹⁵²
- ICICI provides their MFI partners with capital at world market rates.
- ICICI also provides the local firms with state of the art technology.
- Using this new franchise model, ICICI's Microfinance business is very profitable.
- Each local partner is capable of 15X to 30X projected growth by using credit franchisees and other hybrid channels.
- ICICI expects to increase the number of local MFI's in their network from 30 to 200–300 in the next 3 years.

¹⁵⁰ Excerpted from presentations by Arun Sarin, CEO, Vodafone and Charlotte Grezo, Director of Corporate Responsibility, Vodafone at the WRI Conference "Eradicating Poverty through Profit: Making Business Work for the Poor", San Francisco, December 2004.

¹⁵¹ In a widely quoted statistic, ICICI calculates that it requires 40 times more manpower to provide \$1.3 million in loans to Microfinance clients than to extend that same amount of credit to a large corporation.

¹⁵² Less than one year later, ICICI Bank reported 1.5 million Microfinance customers served through a network of 53 small local banks. "A survey of Microfinance," *The Economist*, November 5, 2005

- ICICI also sells their various insurance products through this MFI network. One of their most popular offerings: rainfall insurance for small farmers.
- ICICI expects to reach at least 50 million households in 3 years using their scalable franchise network model.
- Gradually, the MFI's are evolving into local community banks. This franchise model of pairing a local financial institution with a major national bank lets both entities do what they do best in concert while productively leveraging shared infrastructure.¹⁵³

Franchise Vendibility

Few successful business owners do the very same thing during their entire career. Most build up a business, grow it into something larger and more diverse, sell it, or stabilize it with professional management which frees them up to start something new. Selling a business can be tricky because the universe of potential buyers is small and privately held firms are notoriously hard to value. For most micro enterprise owners in developing nations, selling their business is practically impossible for a variety of reasons:

- The enterprise is usually informal, not legally registered.
- The enterprise is probably highly personality dependent.
- With no barrier to entry, potential buyers can simply start something identical.
- Added value through advanced skill sets is typically low.
- Marginal capitalization has often created an enterprise with few fixed assets.
- Adequate accounting records probably don't exist so value is indeterminate.

The franchise business model by its very nature solves all of these problems so the owners of MicroFranchises can build up their asset values with confidence, knowing that they can access that capital in the future when a compelling new venture comes along. This built in exit strategy is one reason why banks in the developed and developing worlds are more willing to loan money for a franchise start-up than for a new independent enterprise.¹⁵⁴

¹⁵³ Nachiket Mor, Executive Director, ICICI Bank. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

¹⁵⁴ If a US firm wants to expand abroad, the Overseas Private Investment Corporation, OPIC, has historically required the firm to put up 30% of the financing themselves. During the Clinton administration, OPIC changed the rules for franchisors. If a US franchisor wants to expand abroad, OPIC will finance 100% of the investment. Personal communication with Ann Tull, Director of International Development, Maui Wowi, and former Director of the US Export Assistance Centers, US Department of Commerce, March 2005. Some Banks are so enamored with the predictable performance of franchises that they will finance up to 120% of a franchisee's start up costs. This causes a problem because most franchisors require potential franchisees to put up a certain percentage of the initial investment from their own private equity. Randy Clifton, Senior VP, Franchising, Pizzeria Uno Corporation. Presentation at the IFA Convention, Hollywood, FL, March 2005. Many franchisors line up financing ahead of time and offer potential franchisees a package deal that includes one or more financing options. The fast growing Big O tire franchise, for example, offers a new owner pre-arranged financing from Wachovia, CIT or GE Franchise Finance. This greatly reduces the time required to bring a new Big O location online. John Hyduke, Vice President, Franchise Development, Big O Tires. Presentation at the IFA Convention, Hollywood, FL, March 2005. For a comprehensive look at MicroFranchise finance options, see Kirk Magleby, "Financing MicroFranchise Networks," in the forthcoming *MicroFranchise Toolkit* to be published by the MicroFranchise Development Initiative, Marriott School of Management, BYU.

Market Penetration

The franchise business model is thriving worldwide. Franchises account for 10-20% of GDP in most developed countries, and that number increases annually. Franchises globally are generally growing at least twice as fast as their host national economies.¹⁵⁵ They are also proving to be excellent vehicles for developing export earnings. Many Singaporean franchise systems currently operate in and repatriate profits from Thailand, for example.

Mexico is a Model

Mexico is an instructive model because as one of the strongest economies in the region, it tends to be a bellwether for the rest of Latin America. Franchises were relatively unknown in that society 20 years ago. Today there are hundreds of franchise networks in operation in Mexico and the concept is growing fast. Victor González Torres' Farmacias de Similares have become the largest network of corner drugstores in the country and have expanded throughout Central and South America.¹⁵⁶ Some Mexican franchises such as the informally managed Paleterias La Michoacana with over 15,000 outlets are ubiquitous and have profoundly penetrated the US market.¹⁵⁷ In 20 more years, franchises will dominate Mexican main streets and strip malls just like they do today in the US. (Market studies in both countries indicate that Hispanic consumers tend to be highly brand loyal.) Even the world's largest retailer, Wal-Mart, operates its VIPS restaurant chain in Mexico as a franchise. It is time to unleash the power of the franchise business model to unlock some of the latent potential for sustainable development that lies dormant throughout the developing world.

Appropriate Enterprise Size

MicroFranchises can be very small operations. The 80 Health Stores operated by Scott Hillstrom's Health Stores Foundation (formerly SHEF and CFW) in Kenya are one example.¹⁵⁸ The 30 Cellular City storefronts franchised to alumni of Stephen W. and Bette Gibson's ACE in the Philippines are a second example.¹⁵⁹ Tiny equipment businesses rent bicycles and wheelbarrows. Muhammad Yunus' MicroFranchised Grameen village phone ladies in Bangladesh have a very small business footprint.¹⁶⁰ Direct distribution models like Unilever's kiosk based Shakti Amma dealers in India¹⁶¹

¹⁵⁵ In Mexico, for example, while the economy grew by 4.4% in 2004, the franchise sector grew by 19%. "Franchise businesses have grown at an average annual rate of 20-30% since the late 1990's, compared to an economic growth rate of 6-8%." Dhawal Shah, "The Enormous Potential of International Franchising in India," *India Infoline*, September 4, 2004. The franchise sector is growing much faster than the underlying economy in most countries on earth. The trend is decades old and still appears vigorous.

¹⁵⁶ www.farmaciasdesimilares.com.mx. The franchise network has over 3,200 locations in Mexico, Guatemala, El Salvador, Honduras, Nicaragua, Costa Rica, Ecuador, Peru, Chile and Argentina.

¹⁵⁷ www.paleterialamichoacana.com

¹⁵⁸ www.cfwshops.org. See Michelle Fertig and Herc Tzaras, *What Works: Healthstore's Franchise Approach to Healthcare*, WRI Development Through Enterprise What Works Case Study, November 2005.

¹⁵⁹ www.creatingenterprise.com

¹⁶⁰ www.grameenphone.com. Each lady owns a cell phone and a solar battery charger.

¹⁶¹ Tex Gunning, head of Unilever's global BOP business strategies, told Scott Hillstrom that there are 15,000 Shakti Amma ladies in India presently. Tex expects that number to increase soon to 100,000. Scott Hillstrom, personal communication, November 2005.

and Brazil's nearly ubiquitous Avon ladies generally employ a single person. In most cases, though, that single person earns much more and has more security than they would have on their own without the nurturing support of the large enterprise around them.

Most MicroFranchises will be created in the developing world rather than exported from industrialized nations. A great deal of creative social entrepreneurship will be required. The unit economic numbers are simply too small to allow systems to be merely adapted from developed countries.¹⁶² McDonalds has suspended operations in most of Bolivia and KFC can't compete with the indigenous Pollo Campero franchise in Guatemala and El Salvador. Pollo Campero, on the other hand, has franchised locations throughout California and is beginning to expand into Texas and New York.¹⁶³

In less developed countries, small really can be beautiful as long as there is growth.¹⁶⁴ In Bolivia for example, per capita income is about \$2,500 per year so a MicroFranchise that allowed its owner to take home \$250 per month would give that enterpriser an income above the national average.

The MicroFranchise Development Initiative, MFDI, of the BYU Center for Economic Self-Reliance defines a "MicroFranchise" as a franchised business concept that is available to and within reach of people at the base of the income pyramid in a developing country.¹⁶⁵ It is understood that most potential MicroFranchisees will require financing to pay their franchise fee and other start up costs. The cost threshold for a business to qualify as a MicroFranchise could be as high as \$25,000¹⁶⁶ in countries like Mexico or Brazil where annual per capita GDP adjusted for purchasing power parity ranges from \$8,000 to \$9,500. That same acquisition threshold may be as low as \$3,000 in a nation like Kenya where annual per capita GDP adjusted for PPP is only \$1,000.

Future Trends

Commercial realities such as market demographics, land values and transportation infrastructure dictate the scale of commerce in any given community. In my city of American Fork, Utah, for example, the local Wal-Mart recently vacated its original store and moved to a Super Center across town, adding 300 new jobs in the process. What had been big box retail is now mega box retail.

¹⁶² Unilever Vietnam sells through a network of 100,000 independent representatives, each averaging \$3,000 in sales per year, which allows Unilever Vietnam to gross \$300 million per year.

¹⁶³ www.campero.com

¹⁶⁴ E.F. Schumacher, *Small is Beautiful: Economics as if People Mattered* (New York: Harper & Row, 1973). Amul's global empire, for example, is based on over eight million tiny Indian dairy herds.

¹⁶⁵ Meeting of the Steering Committee, MicroFranchise Development Initiative, Center for Economic Self-Reliance, Marriott School of Management, BYU, April 2005. It is important to note that the term "micro franchise" is commonly used in Europe to denote a small franchised business opportunity available to entrepreneurs in the developed world. The term "MicroFranchise" in this paper refers to a very small franchised business or social enterprise opportunity available to entrepreneurs in the developing world.

¹⁶⁶ Grameen Bank makes loans as high as \$15,000 without collateral in Bangladesh. Personal communication with Muhammad Yunus, July 2005. Local financing is available in most developing countries for amounts up to 3X per capita GDP if an aspiring enterpriser presents a solid business plan. The presence of a franchise network supporting a business plan will be viewed favorably by most lenders.

The same phenomenon will happen with certain MicroFranchise locations under favorable conditions. Some will grow into “mini franchises,” generating more wealth and creating more jobs in the process.¹⁶⁷ The MicroFranchise industry worldwide will trace a trajectory similar to the one that Microfinance has followed where initially, philanthropic support or socially responsible corporations will be needed to create the operating systems, adapt them to local conditions, and implement the pioneering networks. Some franchise organizations will become self-sufficient fairly quickly, while others will be at least partially donor dependent over long periods. Incubators, facilitators, replicators, holding companies and accelerators will arise as the industry matures. Securitization through syndication will attract some interest from mainstream franchise industry players, financial institutions and investors. Some multinationals and large domestic corporations will seize the concept as an opportunity to cost effectively open vast new markets of heretofore underserved consumers. Multinational corporations will forge creative joint ventures with NGOs. Informed people generally will come to realize that large numbers of very small enterprises can be efficiently and profitably run so they create jobs and contribute significantly to national economies.¹⁶⁸ MicroFranchising which has begun as a fledgling social movement will soon go mainstream.

Coalescing World Opinion

Institutions worldwide have begun to direct resources and political will toward sustainable development through private sector initiatives. The IDB¹⁶⁹ created The MIF in 1993 to pursue enterprise based solutions to poverty in the Americas. The World Bank through IFC¹⁷⁰ created a “Grassroots Business” initiative to support private enterprises. The exciting new Millennium Challenge Account¹⁷¹ aims to change historical foreign aid paradigms in favor of real economic growth through private initiatives in countries who create favorable market conditions. “Sustainable” is the new development mantra and sooner or later that means large numbers of profitable businesses. Jonathan Lash sees a “significant overlap in the interests of the private sector and the interests of the poor, such that win-win solutions are not just possible, but likely.”¹⁷² A franchise network represents one of the best win-win scenarios yet developed.

¹⁶⁷ There are several different formats available for a Farmacias de Similares franchise in Mexico. “Chirris” locations are designed for small towns. They cost about \$16,000 to start up, so they fit the definition of a MicroFranchise. “Pueblerinas” locations, designed for larger markets, have many more SKUs and require a more sophisticated facility. “Citadinas” locations, designed for cities with a population above 50,000, have a pharmacy and a medical clinic side by side. “Mega” locations, designed for large cities, have a pharmacy, a medical clinic and a medical lab in their much larger facilities.

¹⁶⁸ Kick Start, for instance, claims to have moved the GDP dial in both Kenya and Tanzania with their Moneymaker treadle pump for improved irrigation. www.approtec.org.

¹⁶⁹ www.iadb.org

¹⁷⁰ www.ifc.org

¹⁷¹ www.mca.gov

¹⁷² Jonathan Lash, President, World Resources Institute, in his welcome to the WRI “Eradicating Poverty through Profit” Conference Program Book, San Francisco, December 2004.

The Grameen Experience

A few years ago, my oldest son spent a summer as an intern with the Grameen Bank in Bangladesh. Upon his return, I asked him for his impression of this revered institution. He said with a bit of disdain in his voice, “Grameen is more of a business conglomerate than a Microfinance institution.” He was referring, of course, to the fabric manufacturing, agri-business, telecommunications, Internet and other for profit commercial and industrial enterprises in the Grameen family. In my son’s mind, it was as if Microcredit was an altruistic and pure little jewel off to the side while large scale business was somehow greedy and dirty.

I asked him to put himself in the shoes of a typical Grameen borrower. Would he rather have a loan and a pat on the back as he went off to do battle with the cold, cruel world and seek his fortune? Or would he prefer a loan and a proven business opportunity that came with considerable institutional support built in? If only one person in ten is destined to be a true entrepreneur as many have suggested, then various kinds of franchise relationships can expand that pool to include enterprisers who do not have to manage innovation if they just follow well established business policies and procedures.¹⁷³ On June 27, 2004, for instance, the Grameen Bank – Village Phone MicroFranchise won the first Petersburg Prize: 100,000 euros given by the Development Gateway Foundation to recognize the outstanding use of information and communication technology to improve people’s lives in the developing world.

Grameen’s successful fish farms have been characterized as an “agribusiness franchise” where up to 40 people jointly own an aquaculture facility.¹⁷⁴

The Microfinance Experience

Grameen pioneered it. FINCA adapted it. Acción institutionalized it. Thousands replicated it. The 1997 Microcredit Summit in Washington DC legitimized it. And now in 2005, more than 7,000 Microfinance institutions worldwide are granting small loans to poor people. Between 70 and 100 million households currently benefit from this innovative financial service and the UN has designated 2005 as the International Year of Microcredit. Major international banks like Citigroup, ABN Amro, and ICICI are beginning to compete for market share and some markets, particularly in Latin America, are approaching saturation. There is a growing realization that MFI’s will gradually evolve into credit unions and local community banks and that the current fragmented market will consolidate as the industry matures and becomes mainstream.¹⁷⁵ Amid these dynamic developments, the franchise business model has quietly become prominent as a preferred way to deliver quality financial services to the world’s underserved poor.

- Citigroup collaborates with local MFI’s as partners in about 20 countries.
- ICICI works with 53 local MFI institutions and has aggressive plans to scale up.

¹⁷³ “Franchisees are called ‘entrepreneurs in a box.’” Jay Finegan, *Inc Magazine*, November 1995.

¹⁷⁴ Muhammad Yunus’ comment after I explained that many industries in the Grameen family of enterprises are classic MicroFranchises: “Yes, that is what we are doing. It works. Just go do it.” Personal communication with Muhammad Yunus, July 2005.

¹⁷⁵ María Otero, Presentation at BYU Economic Self-Reliance Conference, March 2005.

- ABN Amro works with local MFI partners in India and Brazil.
- Janine Firpo who ran HP's Remote Transaction System project in Uganda determined that Acción's UMU model using local merchants (often pharmacists) as credit franchisees holds the most promise among the various MFI systems she worked with.

The inherent benefits of this win-win between local enterprises and regional, national or global institutions are obvious: both benefit from intense neighborhood knowledge and shared infrastructure.¹⁷⁶

Questions and Answers

"How do you create massive entrepreneurship?" C. K. Prahalad

"How can multinational corporations be more fair in distributing wealth? Eduardo Bazoberry

"How can multinational corporations become the driver of a more inclusive capitalism?" Stuart Hart

"Are there solutions in terms of wiring? Network models? An X Prize to solve poverty perhaps?" Holly Wise

"How do you build SME's? Microfinance is at the base. Large companies are at the top. But most of the real economic development takes place in the middle." Mark Malloch Brown¹⁷⁷

The franchise business model reasonably answers all of these questions.

"Internal savings makes a country free. The local private sector is the key, not foreign social investors telling us what to do. The secret is to look for local entrepreneurs." Eduardo Bazoberry

"In emerging markets, conglomerates are very important because there are so many voids in the value chain. You need tremendous horizontal and vertical integration to overcome the huge gaps in the external economy." Yogesh C. Deveshwar

"Agency models make sense in Microfinance, rather than trying to invent all new infrastructure." James Dailey

"Savings flows exist in developing countries. Finding productive ways to deploy those savings is the key to development." Alan Larson

"The goal is enterprise co-creation that builds value for multinational corporations and for the local community." Stuart Hart¹⁷⁸

The franchise business model reasonably meets all of these expectations.

Contrary Examples

A few examples of well-intentioned development programs gone awry:

¹⁷⁶ Kenya-based Pride Africa, for example, using the franchise business model, has grown to become the largest MFI in East Africa. They have franchised operations in five countries managed from their Nairobi headquarters.

¹⁷⁷ All five questions are from presentations at WRI, San Francisco, December 2004.

¹⁷⁸ All five expectations are from presentations at WRI, San Francisco, December 2004.

1. Economic migrants leave their homeland, work in an industrialized country and send money home. “Lots of children benefiting from remittances have drinking and drug problems with far too much leisure time. You have a lot of kids with money in their pocket, but no mother or father and no education¹⁷⁹.” Monica Hernandez. “Cash remittances are extremely socially corrosive. Large flows of remittances create external dependency and huge distortions in asset markets. There are many half-built houses that no one will ever live in. Formerly productive agricultural and small workshop properties lie fallow.” Raul Hinojosa. Don Terry thinks this remittance money should reside in formal financial institutions that can leverage it through the bank multiplier effect and fund local enterprise creation.¹⁸⁰ Many migrants would be willing to invest in hometown MicroFranchised business opportunities if such systems were widely available.

2. A US based religious organization pays janitors in Cuzco, Peru \$500 per month plus lavish benefits in a market where professional people often struggle to make half that amount. This organization also offers student loans to young people for vocational training, but few youth avail themselves of the opportunity to study. Like inner city kids in the US who dream of growing up to be professional athletes, these young Peruvians hope for a high paying job with a foreign firm and almost all end up disillusioned and frustrated.¹⁸¹ How much better would it be for this multinational organization to contract out its custodial services to a local MicroFranchised cleaning contractor?

3. I was in Cochabamba, Bolivia speaking with the owner of a small clothing store.

“Where does your clothing come from?”

“My family makes it in a small sewing shop behind our house.”

“How many sewing machines do you have?”

“Five.”

“How many people do you employ?”

“Two. The business only provides enough for my wife and me, and she can only work part-time.”

“What happened that your business fell off from five active sewing machines to one that only works part-time?”

“Used clothing started coming down from the US. We can’t compete.”

Thrift stores like Goodwill, St. Vincent de Paul and Deseret Industries send large bales of used clothing to developing countries in Latin America. US donors think their castoffs end up benefiting the needy in those countries. In reality, local strongmen (the root cause of poverty) take control of these donated goods and dump them on the black market for a quick profit. Local markets are flooded with cheap used clothing and indigenous garment workers go hungry. Ironically, most of this used clothing is too big to fit the smaller Latin American physiques. How much better would it be if a MicroFranchised apparel

¹⁷⁹ Mexican migrant children get less education than those of non-migrants. Maurice Schiff, Caglar Ozden, editors, *International Migration, Remittances and the Brain Drain* (Washington, D.C.: World Bank, 2005).

¹⁸⁰ Hernandez, Hinojosa and Terry all presented at the MIF and WRI Conference, “The Technology of Remittances,” San Francisco, December 2004.

¹⁸¹ Personal communication with Ruben Andia and family, November 2004.

remanufacturing firm purchased these bales of used clothing in the US and kept local sewing machine operators busy remaking them to fit smaller sizes?¹⁸²

The Grand Convergence

The most significant event I have attended in the 30+ years I have wandered the planet searching for the solution to global poverty happened in San Francisco in December 2004. WRI and about a dozen MNCs sponsored the conference “Eradicating Poverty through Profit: Making Business Work for the Poor.” Based on the work of C.K. Prahalad, Stuart Hart and their associates, the moderator, Scott Shuster, christened it BOP (Bottom or Base of the Pyramid) I. BOP II convened in August 2005 in Sao Paulo and in September 2005 in Mexico City with equally electric atmospheres.

1,000+ attendees from many nations could sense real progress and envision real solutions. Among others, this conference theme was prominent: “Former adversaries and combatants are now collaborating.” Mark Malloch Brown. “The grand convergence between governments, civil society and businesses is an urgent imperative.” Herman Mulder. “We need a more joined up world with effective relationships between NGOs, governments, and the private sector.” Richard Sandbrook. “There is a grand convergence taking place between the private sector, civil society organizations, governments, international aid organizations and local civil servants.” C.K. Prahalad. “We need organizations that are more integrated.” Louis C. Boorstin. Fortunately, franchising is a highly effective form of integration, collaboration and convergence.

James A. Harmon summarized it well: “Transparent, fair and consistently applied law is what we need from government.¹⁸³ Paying attention to the BOP is what we need from the private sector. Innovation and creativity is what we need from NGOs.”¹⁸⁴ Ashoka calls this business/social model “hybrid value chains” or “cross-sector partnerships.”¹⁸⁵

Some MicroFranchise Networks Currently Operating

- Scojo Foundation’s vision through entrepreneurship offers affordable reading glasses in many countries through a network of women MicroFranchisees.
- The Reyes family has done well enough with their 200+ *MicroFranchised* barber shops in the Philippines that they have expanded their operations into California.
- Over 300 Julie’s Bakeshops dot the Philippines, with expansion into Singapore.
- Casa por Casa is a MicroFranchised advertising flyer business in Mexico.
- Over 4,000 MicroFranchised tailors stitch and sell Ruff n Tuff jeans from kits, helping India’s Arvind Mills dominate the domestic denim market.
- DTDC courier service has more than 3,000 tiny franchised outlets across India.

¹⁸² Many governments are aware of the market poisoning and distortion that come with used clothing. Bolivia, for example, now specifically prohibits used clothing in humanitarian shipments.

¹⁸³ An excellent source for details on a given country’s regulatory environment as it relates to starting and running an enterprise is “Doing Business” published by the World Bank, www.doingbusiness.org.

¹⁸⁴ The citations in this section all come from the WRI Conference “Eradicating Poverty through Profit,” San Francisco, December 2004.

¹⁸⁵ Valeria Budinich, *A Framework for Developing Market-Based Strategies that Benefit Low-Income Communities*, Ashoka Full Economic Citizenship Initiative, August 2005.

- Holanda franchises several hundred tiny restaurants throughout Mexico. And, there are dozens of other MicroFranchise networks quietly transforming India, Mexico, Brazil, the Philippines, South Africa, etc.¹⁸⁶ Many of the most successful international economic development projects in recent years utilize some form of the franchise business model.¹⁸⁷ Many egregious failures ignore or overtly contravene proven MicroFranchise principles.¹⁸⁸

Toward a MicroFranchise Heuristic

As hundreds of MicroFranchise networks begin to revolutionize economies in the developing world, a number of common characteristics will become apparent:

- Many products and services will be basic compared with their counterparts in the developed world (bicycles rather than automobiles, drug store reading glasses rather than prescription lenses, cell phones rather than computers).
- Collective access will usually be more common than individual ownership (Pay per use Internet kiosks).
- Most business concepts will be labor rather than capital intensive.
- Units packaged for individual sale will often be very small (tiny jars of lotion that sell for 1 or 2 cents).
- 5,000 people in reasonable proximity will be a typical market or catchments area.
- Prepaid services will generally be more cost effective than extending credit.
- Many delivery systems will be multi-tiered when high skill levels are in short supply (nurses, community health workers or pharmacists attend the masses, referring more serious cases to local clinics who in turn refer the most serious cases to a hospital).
- Product delivery systems will often be direct from the manufacturer to the consumer because the unit economic numbers will not justify a traditional wholesale distribution supply chain.
- Shared infrastructure will be common (several enterprises will use a single delivery vehicle or warehouse).
- Political issues will be more important than they are in the developed world.
- Innovative technologies and business models will be widespread.
- Many businesses will be mobile rather than storefront based.
- MicroFranchises will generally deliver products and services with superior, even world class price performance.
- Rental business models will proliferate.
- Barter will be common in some rural areas.

¹⁸⁶ Over half of the 700 franchise concepts operating in the Philippines, for example, are indigenous, and many of those fit the profile to be classified as MicroFranchises. One interesting example: Oriental acupuncture foot massage. Personal communication with Samie Lim, March 2005.

¹⁸⁷ Honey Care Africa is an award-winning IFC project from Kenya. See www.honeycareafrika.com.

¹⁸⁸ For a list of conspicuous debacles, see James Bovard, *The Continuing Failure of Foreign Aid*, Policy Analysis No. 65, (Washington D.C.: Cato Institute, 1986).

- Compound franchises will allow a single owner or multiple owners to operate two or more concepts within a single shared facility.¹⁸⁹
- Creative fractional equity ownership models will develop.
- Multi unit franchisees will develop over time. This is a healthy sign that the system is working and owners are leveraging assets to found new enterprises.¹⁹⁰
- Many deals will involve creative bundling (a phone company that rents an AMD PIC as part of their monthly service).
- Equipment will tend to be digital rather than analog, electronic rather than electro-mechanical to take advantage of what WRI calls the “digital dividend”.
- The MicroFranchise market will respond better to cost effective, state of the art solutions than to recycled or obsolete products or equipment.
- Conversions between company stores and franchised locations (and vice versa) will be common.
- MicroFranchises will proliferate in the manufacturing and construction sectors in addition to the more traditional retail trade, professional service, business service and retail service sectors.
- Franchisors will often provide a comprehensive service bureau environment to their MicroFranchisees to compensate for their partners’ lack of administrative capacity.

MicroFranchise Development Costs

Too few MicroFranchise business opportunities have been developed to accurately judge costs which will vary by country and industry. \$1 million may be a ballpark cost to develop and deploy a typical MicroFranchise business opportunity.¹⁹¹ Most of the development work will take place in emerging nations with technical assistance and capital from wealthy countries. A typical deployment will involve up to 100 franchisee locations in the pilot phase of the project and networks with tens of thousands of locations will not be uncommon as enterprises scale up around the world.

Sources of Funds

In order to solve global poverty, we need hundreds of MicroFranchise business opportunities available so high potential entrepreneurs have a smorgasbord of options to choose from based on their experience, interest or skill level. Remember the nursery rhyme about the butcher, the baker, the candlestick maker? Every low income community of 5,000 people needs a bicycle repair shop,¹⁹² a pharmacy, and hundreds of other local businesses. So where will all this money come from to develop hundreds of

¹⁸⁹ In the US, for instance, it is commonplace to see a fast food restaurant/gas station combination. This modularity of locating a franchise within a franchise increases the likelihood of a business unit achieving viability.

¹⁹⁰ “Mail Boxes, Etc. does not yield enough profit from a single location to allow a person in the US to live comfortably. So, most MBE franchisees own at least 2 or 3 locations.” Personal communication from Linda L. Burzynski, CEO, CM IT Solutions, March 2005.

¹⁹¹ This \$1 million number comes from several conversations with Scott Hillstrom and is based on his experience building out the Health Stores MicroFranchised pharmacy network in Kenya. Recent personal communication from Chuck Slaughter in June 2005 indicates this number may be low.

¹⁹² Afribike, for example, uses the MicroFranchise business model. www.afribike.org.

MicroFranchise systems? The answer is: the money is available if the concept proves compelling enough that political will develops. Alan Larson of the US State Department estimates the following annual resource flows currently reach the developing world:

- \$70 Billion in ODA
- \$93 Billion (MIF's Don Terry says \$175 Billion is the better estimate) from migrant remittances
- \$200 Billion in FDI
- \$2 Trillion in endogenous savings

I estimate that \$250 million will get more than 200 MicroFranchise networks operational and beginning to grow around the world. Based on the same powerful business model that allowed Subway to grow from one store in 1965 to more than 23,000 stores in 77 countries 40 years later, MicroFranchises should be able to help the world's poor get access to clean water, renewable energy and a host of other life enhancing goods and services while providing employment and ownership opportunities on a large scale.¹⁹³

\$250 million¹⁹⁴ to help solve the world's most pressing problem using the same basic formula that enterprises from Starbucks to Marriott have employed to conquer the globe. That is a BHAG (big hairy audacious goal) that even Jim Collins would be proud of.¹⁹⁵

Reality Check

Livelihoods ultimately stem from successful business enterprises. Most of us understand that implicitly. So why do governments, NGOs and socially responsible corporations still deal with global poverty by sending money, stuff or people? Because administering relief aid is quick, easy, and gratifying. Photo ops and anecdotes temporarily satisfy activist ardor. I presented a version of this paper in the 2004 CESR conversation series at BYU.¹⁹⁶ I suggested that it is ten times harder to build a successful business enterprise in a developing nation than it is to simply dispense charity or build infrastructure. A savvy veteran of the poverty wars raised his hand at that point and enlightened me. "It's not ten times harder," he retorted. "It's a hundred times harder."¹⁹⁷ I stand corrected.

Gender Neutrality

Ever since Muhammad Yunus left his classroom at Chittagong University to understand the micro economics of Jobra Village, the Microcredit movement has had a profound

¹⁹³ Nimble franchises penetrating economically distressed areas is not a phenomenon unique to the developing world. Small Sav-A-Lot franchised grocery stores service market areas in the US (like inner cities) that other grocery chains refuse to enter. Growing very rapidly, the 1,229 Sav-A-Lot stores routinely generate higher profit margins than their behemoth competitors in the suburbs. Janet Adamy, "To Find Growth, No-Frills Grocer Goes Where Other Chains Won't," *The Wall Street Journal*, August 30, 2005.

¹⁹⁴ \$250 million should get 200+ MicroFranchise networks built out to 100 locations, at which point they are ready to scale up. \$2.5 billion should get those 200+ networks growing rapidly around the world. It would be like 200 X Prizes to alleviate poverty. This, in my judgment, offers the world its best chance of meeting the Millennium Development Goals by 2015.

¹⁹⁵ Jim Collins and Jerry I. Porras, *Built to Last: Successful Habits of Visionary Companies* (New York: Harper Business Essentials, 2002)

¹⁹⁶ www.marriottschool.byu.edu/selfreliance.

¹⁹⁷ The speaker was Stephen W. Gibson, Senior Entrepreneur in Residence, Marriott School of Management.

feminine bias, and for good reason. Males beat their wives to extort drinking money while females guard the household budget. Males sell the tin roof off their family hut to pay gambling debts while females work to put shoes on the kids. After 30 years of feminized Microcredit, though, people are now rethinking the paradigm. Sustainable development across generations, it turns out, requires the best efforts of everyone in the household. John Hatch observes that far too many children of Microcredit-enabled mothers are wasting their time on unproductive leisure or delinquency. “Our single-minded focus on women has not created the culture of progress we had hoped.”¹⁹⁸ Elizabeth Littlefield adds, “In the MFI world, we have over promised. MF does not eliminate poverty. MF is not a panacea as some thought a few years ago.”¹⁹⁹

MicroFranchising is about scalable family businesses.²⁰⁰ Successful MicroFranchise locations employ Dad, Mom, the older kids and often one or two neighbors.²⁰¹ Children growing up in an enterprising household regard their business as a precious family asset that can increase in value through ambition and applied intelligence. Sons and daughters both can prepare for the day when they too can own an outlet or location. MicroFranchises, like most successful businesses, will typically be gender neutral.

Peculiar Institutions

Poverty is slavery. In the context of the American Civil War, politicians in the antebellum South were fond of calling slavery their “peculiar institution.” It was a malevolent institution that enforced servitude through intimidation and violence on the one hand and dispensed a rude form of charity (often couched in the trappings of religiosity) on the other. (Interesting question: How much longer would institutional slavery have persisted in the US if the developed nations of that era, England and France, had provided massive charity to the American underclass in the name of humanitarian relief?)²⁰² It required the formidable institutions of the Union Army and the emergent federal government to free those slaves. We need a new breed of “peculiar institutions” to free the impoverished slaves who languish in oppression on the planet today.²⁰³

Peculiar can mean corporations who exhibit as much ingenuity as an NGO and a willingness to work with non traditional partners.²⁰⁴ For example, an MNC may operate in the traditional manner in the developed world and adopt some form of the franchise

¹⁹⁸ Personal communication with John Hatch, December 2004.

¹⁹⁹ Elizabeth Littlefield, Presentation at WRI, San Francisco, December 2004.

²⁰⁰ One audit of Microcredit-enabled households in Central America found that only 1 business out of the 400 studied had even one employee besides the owner. Another audit found only 1 business out of 700 with any employees. Todd Manwaring, Stephen W. Gibson, presentations, MicroFranchise Learning Lab, Park City, UT, September 2005.

²⁰¹ “Worldwide, men tend to create larger enterprises than women.” Kristie Seawright, presentation, MicroFranchise Learning Lab, Park City, UT, September 2005.

²⁰² USAID says assistance can “mask underlying instability.” “U.S. Foreign Aid: Meeting the Challenges of the Twenty-first Century,” USAID White Paper, January 2004.

²⁰³ Muhammad Yunus says the world needs “changes in our institutions” which he defines as “businesses with a very special social purpose.” Personal communication with Muhammad Yunus, July 2005.

²⁰⁴ For corporations, “moving down market is a very unnatural act.” Personal communication with Clayton M. Christensen, November 2005.

business model in partnership with NGOs to penetrate markets at the BOP.²⁰⁵ Peculiar can also mean NGOs who form commercial business entities and encourage profitability as much as a corporation.²⁰⁶ Either way, the franchise business model in its search for local profits based on indigenous ownership will help liberate disenfranchised people.²⁰⁷

MicroFranchise NGOs will generally be of two types: global vertical market specialists focused on a single business format (franchisors) and geographic generalists who own the rights to multiple franchise networks in their territory (master franchisees or area developers). A common expansion plan will be for a master franchisee to open a new location as a company store and then let the local manager acquire the franchise through an earn out.²⁰⁸

Leapfrog Opportunities

It took the United States 200 years to develop from a primitive economy based on agriculture and extractive industries into an industrial and now knowledge-based market. Developing nations who intelligently implement what Clayton M. Christensen calls “disruptive technology” can leapfrog into the modern age in much less time and at far less cost than the US required.²⁰⁹ Cell phones versus land lines are one commonly cited scenario.²¹⁰ These statistics are worth noting:

- Uganda has 85% cell phone coverage.
- 1.2 billion VISA cards work at 22 million merchant locations in 150 countries.
- Nearly 2 billion people have a cell phone. 500 million of them are in China.
- By 2009, Mexico will have one ATM for every 250 people.
- The 36% of Filipinos with cell phones send 100 million SMS messages daily.

²⁰⁵ Corporate culture and even nomenclature is quite different in a typical hierarchical MNC than in a franchise network. When MNCs first begin to utilize the franchise business model with its egregious win-win orientation to engage customers and business partners at the BOP, the experience will indeed seem “peculiar” to many of their people. Franchise culture is like the communitarian European style while traditional MNC culture is more like American style rugged individualism. C.K. Prahalad points to Unilever and India’s Amul as examples of a new breed of multinationals who have “fundamentally rethought the nature of the large enterprise – as well as the small enterprise.” “Small is Profitable” in *Business Week Online* August 26, 2002.

²⁰⁶ The Shell Foundation describes it as “transferring business DNA” to the entire international development supply chain. Marc Lopatin, et al, *Enterprise Solutions to Poverty: Opportunities and Challenges for the International Development Community and Big Business*, Shell Foundation, 2005.

²⁰⁷ An interesting peculiar institution is megapastor Rick Warren’s PEACE plan to supply a “school in a box, clinic in a box and business in a box” to each Rwandan church. *Time*, August 22, 2005.

²⁰⁸ I am indebted to Michael H. Seid, Managing Director, Michael H. Seid & Associates for this brilliantly simple solution to a common conundrum: How to help a local entrepreneur acquire a franchise before the franchisee is fully ready for independence. Many MFIs do not grant credit until a client has developed capacity through either savings or training. This same kind of disciplined capacity building will be an important preparatory phase in the personal development of many successful MicroFranchisees. Stephen W. Gibson calls this approach “MicroEquity Financing.” Stephen W. Gibson, “First the Sweat, Then the Equity” in *Deseret Morning News* July 3, 2005.

²⁰⁹ Clayton M. Christensen, *The Innovator’s Dilemma*.

²¹⁰ Allen Burnes, Vice President of High Growth Markets, Motorola, recently announced a \$40 cell phone. After multiple redesigns, it has a 500 hour battery life and features an extra loud volume for use in noisy markets. Motorola expects 2 billion people on earth to purchase a cell phone in the next five to ten years.

- 400 million people have Hotmail accounts.
- AMD's Hector Ruiz hopes to connect 50% of humans to the Internet by 2015.²¹¹
- Khan Bank in Mongolia serves 66% of the households in that rural country.
- Mongolia is already virtually a cashless society. Checks are obsolete there.
- In 2004, 450 million Indians voted in a 100% electronic election.
- Voting in Brazil is nearly 100% electronic.

The opportunities to implement profitable MicroFranchises in most countries on earth are almost endless. HP's former CEO says it well: "Today we have the tools to make more things possible for more people in more places than at any time in history."²¹² It is all a matter of identifying and empowering the "extraordinary entrepreneurs" that Jacqueline Novogratz believes "exist in every region of every country."²¹³

An Historical Precedent

The most impressive economic development the world has witnessed in recent centuries began in 1847 is what is now the state of Utah. Brigham Young led an advance party of 147 hardy trailblazers into a trackless wilderness that was 800 miles from Yerba Buena (later San Francisco, California) to the west and 1,000 miles from St. Joseph, Missouri to the east. This advance party arrived late in the season (Utah celebrates 24 July as Pioneer Day) and immediately set themselves to building a civilization in the desert. Their task bore some urgency because thousands of men, women and children were on the trail headed to the Valley of the Great Salt Lake. Arriving throughout August and September, these pioneers had to provide food, clothing and shelter adequate for a small city to survive that first harsh winter. Tens of thousands more immigrants came in 1848 and 1849 as strings of settlements were founded north and south of Salt Lake. Within three years, Utah had a newspaper, a public theater and a university. Within ten years, per capita income in Utah was approaching the national average and local families were sending their children to good colleges in the East. With investment capital practically non-existent and manufactured goods extremely scarce, Utahns created a thriving economy in the arid Great Basin the same way the ancient Egyptians built the pyramids: through the miracle of cooperation.²¹⁴

In the emerging science of cooperation studies, study after study shows that humans achieve the highest levels of productivity, personal satisfaction and wealth creation when they work together cooperatively.²¹⁵ The franchise business model is a proven, refined

²¹¹ AMD's device is called a "Personal Internet Communicator" or PIC. It sells for about \$185. At least one Taiwanese manufacturer is working on a similar device that could sell for as little as \$100.

²¹² Carly Fiorina. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

²¹³ Jacqueline Novogratz, CEO, Acumen Fund. Presentation at WRI Eradicating Poverty through Profit, San Francisco, December 2004.

²¹⁴ The standard work to consult on Utah's economic development is Leonard J. Arrington, *Great Basin Kingdom: An Economic History of the Latter-day Saints 1830-1900* (First Edition Cambridge, MA: Harvard University Press, 1958; Champaign, IL: University of Illinois Press, 2004)

²¹⁵ Standards in the literature of cooperation include Robert Axelrod, *The Evolution of Cooperation* (New York: Basic Books, 1984) and Elinor Ostrom, *Governing the Commons: The Evolution of Institutions for Collective Action* (New York: Cambridge University Press, 1990). Social scientists have devised a number (...continued)

way to channel the tremendous power of humans working together in cooperation.²¹⁶ Howard Rheingold, a perceptive observer of contemporary society, remarks that because “new forms of cooperation always create new forms of wealth,” franchising as a “highly developed form of cooperative enterprise” can “revolutionize low income economies by empowering micro entrepreneurs.”²¹⁷

Franchisees as Social Evangelists

Many of “the world’s most difficult problems” to borrow Stuart Hart’s phrase require education and training.²¹⁸ Why do so many not understand these simple truths?

- Washing your hands with soap prevents diarrhea
- Sleeping under a pyrethrum impregnated bed net prevents malaria
- Drinking and cooking with clean water prevents cholera and dysentery
- Practicing safe sex prevents HIV/AIDS

These problems are as much about human attitudes and behavior as they are about supply and demand. You change behavior through education, but as Freedom from Hunger or Harvard University can tell you, education is very expensive and usually requires subsidies. The sustainable solution to this quandary is obvious. In Kevin McGovern’s words, we need “social marketing” where key opinion leaders in a community help educate consumers to adopt positive behavior through a “pyramid of influence”.²¹⁹

The question then becomes, who are these social marketers and how do they educate the masses? Do clerics preach fiery sermons from pulpits? Do medical doctors advise patients with an even more paternalistic bedside manner? Do activist moms go door to door in urgent altruism? One very effective way to change human behavior through education and training is to turn MicroFranchisees marketing beneficial wares into social evangelists who spread the word while pursuing profits. If the Assemblies of God can do it throughout Brazil with their version of entrepreneurial Christianity (larger congregation

of games to test theories about cooperative human behavior. Thousands of game iterations scrutinized under controlled conditions show that “reciprocating cooperators” dominate winning populations.

²¹⁶ Sid Feltstein, Chairman of the Board of the International Franchise Association, talks about “the synergies that are unique to franchising: the power of a plan, a network, a family, shared experience.” Presentation at the IFA Convention, Hollywood, FL, March 2005. One is reminded of the remarkably efficient network of 5,000 Dabbawallas delivering 175,000 lunch pails every day to office workers in Mumbai, India using a cooperative system that has been functioning smoothly for 100 years. Many Dabbawallas are illiterate, but their accuracy earned them a six sigma rating from *Forbes*.

²¹⁷ Howard Rheingold, personal communication, November 2005 after he gave the keynote address at the ninth annual Rocco C. and Marion S. Siciliano Forum: Considerations on the Status of the American Society, College of Social and Behavioral Science, University of Utah.

²¹⁸ Stuart L. Hart, *Capitalism at the Crossroads*.

²¹⁹ Kevin H. McGovern, Chairman, McGovern Capital. Presentation at Cornell University, Johnson School of Management, Center for Sustainable Global Enterprise, BOP Learning Lab, February 2005.

= bigger pastor's paycheck),²²⁰ then medicine, water, agricultural input and connectivity merchants can do it throughout the world with the MicroFranchise business model.²²¹

Social advocacy requires evangelistic fervor. In my experience, the degree of ardor found in various kinds of organizations generally occurs in this order:

- Religions demonstrate the most fervor.
- NGOs follow.
- Small independent businesses, multi level marketing organizations and franchise organizations tie for third, the common denominator being local ownership.
- Large domestic corporations come next.
- Multinational corporations rank last in their ability to incite passion.

This means that if an LDC or MNC wants to effect positive change through social marketing, they are well advised to partner with an NGO²²² in a franchise network.²²³

Viability and Inevitability

Enlightened capitalist Stephan Schmidheiny dispatched an associate to Latin America to engineer a program for philanthropic giving. The associate returned without a plan, telling Schmidheiny that there were simply too many poor people for his money to make any difference. At that point the Swiss industrialist wisely began to focus on sustainable development, i.e. profitable socially and environmentally responsible enterprises. FUNDES,²²⁴ followed by the AVINA Foundation²²⁵ which enabled ORIGO²²⁶ and ENDEAVOR²²⁷ are the impressive results.²²⁸

Developing nations are ready for similarly enlightened businesses and NGOs to build MicroFranchise business opportunities²²⁹ that create wealth through profitable enterprises, distribute that wealth widely throughout a target population, provide the

²²⁰ Church membership statistics are notoriously unreliable in South America, but most demographers place the number of Evangelical or Pentecostal Protestants in Brazil at 25 to 30 million. About half of those belong to the Assemblies of God, *Assembléias de Deus* in Portuguese. In temporal matters, most Protestant Christian organizations are franchise networks

²²¹ Diffusing values may be the most important impact MicroFranchises have on a society. Personal communication with Maximo San Roman, July 2005.

²²² The non-profit sector, with 19 million employees, is "already equivalent to the eighth-largest economy in the world." Valeria Budinich, *A Framework for Developing Market-Based Strategies*, August 2005.

²²³ Franchises are simply more successful on balance than small independent ventures. Stephen W. and Bette Gibson founded ACE in Cebu, Philippines in 1999. Over 800 students have graduated from their residential entrepreneurship program and most have founded enterprises. Their most successful alumni own franchises, so the Gibsons plan to transition their school from a general business curriculum into a pre-acquisition franchise boot camp. Personal communication with Stephen W. Gibson, August 2005.

²²⁴ www.fundes.org

²²⁵ www.avina.net

²²⁶ www.origoinc.com

²²⁷ www.endeavor.org

²²⁸ Schmidheiny also founded WBCSD, the World Business Council for Sustainable Development.

²²⁹ Nova of Lima, Peru, is preparing to launch a MicroFranchised bakery concept based on scaled down versions of their industrial equipment. Personal communication with Maximo San Roman, May 2005. Scott Hillstrom has created Franchise Labs to deliver healthcare services in the developing world, beginning in Ranchi, India. Personal communication with Scott Hillstrom, November 2005.

framework franchisees need to grow their enterprises and create jobs, and help micro business owners protect their property so at some future time they can leverage their assets to fund new ventures.²³⁰ Auspiciously, well-financed MicroFranchise initiatives such as the exciting OneRoof in San Francisco²³¹ are beginning to appear.²³²

MicroFranchises will accelerate development of the “ownership societies” Pres. George W. Bush envisioned in his second inaugural address.²³³ Responsible corporations who pursue the triple bottom line of financial, environmental and social return should actively consider employing some version of the franchise business model in their global operations, particularly in the developing world.²³⁴ Large numbers of MicroFranchises are capable of dramatically improving life for those at the bottom by creating jobs and by providing the poor with access to goods and services tailored to their needs and consumptive capacities.²³⁵

Pyramidal economies will become diamonds as we create a strong middle class which should be the goal of every society on earth. As we in the industrialized world dine on franchised food, stay at franchised hotels, have our tax returns prepared by franchised accountants and get our cars serviced by franchised technicians, we owe our impoverished brothers and sisters in developing nations nothing less. I predict that MicroFranchises are the next “big thing” in international economic development.²³⁶

²³⁰ “Franchising creates jobs and then wealth wherever it goes around the world. This business model, based on cooperation between people, companies and nations, can help bring about world peace.” Don DeBolt, former President of the International Franchise Association. Presentation at the 45th annual IFA Convention, Hollywood, FL, March 2005.

²³¹ www.oneroof.com

²³² OneRoof CEO Dwight Wilson has a bold and comprehensive vision of “humble Kinkos” community information centers evolving into franchised enterprises that supply clean water, essential medicines, etc. in underserved communities worldwide. Dwight Wilson, personal communication, November 2005.

²³³ Bush’s goal: “the dignity and security of economic independence, instead of laboring on the edge of subsistence.” George W. Bush, 2nd inaugural address, January 2005. Denise Dresser thinks Mexico has “too few owners and too many laborers”. Denise Dresser, presentation at “Crecimiento de Negocios e Innovación dentro de la Base de la Pirámide (BOP II), Mexico City, September 2005. USAID is now emphasizing “partnership, ownership, and participation,” which is a good way of describing the franchise business model. “U.S. Foreign Aid: Meeting the Challenges of the Twenty-first Century,” USAID White Paper, January 2004.

²³⁴ Imagine The Home Depot and Lowes competing worldwide with small MicroFranchised hardware stores. The very idea is pregnant with possibilities.

²³⁵ Samie Lim believes franchising can reverse urban migration by providing employment opportunities in provincial areas of the Philippines. He thinks franchising will float the underground economy by enabling small informal businesses to become legal and scalable. He sees a natural economic evolution in the manufacturing sector from contract work to original designs and finally to indigenous Filipino brands. Personal communication with Samie Lim, March 2005.

²³⁶ Sibley International has done some compelling work using the franchise business model as a tool for economic development, particularly in Russia and the NIS. DAI believes the keys to improved MSE performance include a business enabling environment, horizontal and vertical inter-firm linkages, continual upgrading for competitiveness and supporting services for business finance, raw material inputs, etc. so businesses can scale up and move up the value chain from assembly of imported components to local sourcing, then to indigenous product design and finally to dealing with “branded merchandise”. Lara Goldmark and Ted Barber, “Trade, Micro and Small Enterprises, and Global Value Chains”, DAI under (...continued)

Two Paths Divergent

Capitalism really is at a crossroads as Stuart Hart's important new book declares.²³⁷ Will the world turn left or right? Democracy or totalitarianism? Peace or terror? Markets or social planning? Urban sprawl or biodiversity? Will economic and social empowerment bless every human or must egalitarian capitalism remain the exclusive domain of the privileged elite inside Hernando de Soto's bell jar?²³⁸

Ted Turner is right. In the next 50 years, we can create a paradise, or we can all be living in a hot, burning hell.²³⁹ We can live in Allen Hammond's "fortress world" of poverty and conflict²⁴⁰ or a "transformed world" full of hope for fulfilling human aspirations.²⁴¹ The genie is out of the bottle and there is no turning back. The world is becoming flat.²⁴² Orange clad populists in Kiev and machete wielding *campesinos* in Chiapas will have their day in the sun as "smart mobs" change the dynamics of power in one nation after another.²⁴³ We are witnessing a paradigm shift as fundamental as the renaissance and the industrial revolution that created the modern Western world. The death of feudalism is inexorably transforming one society after another.²⁴⁴ The incipient BOP Protocol coming out of Michigan and Cornell to provide a framework for sustainable global development is an excellent road map for the path ahead.²⁴⁵ It stresses "mutual value creation" which is one way of describing the franchise business model.

The Power of a Name

MicroFranchising is beginning to happen in the developing world. It is time to recognize it for what it is, codify the nomenclature, disseminate best practices and turn this

contract to USAID, February 2005. Franchising creates these favorable conditions and outcomes for small firms more effectively than any other extant business model.

²³⁷ Stuart Hart, *Capitalism at the Crossroads*.

²³⁸ Hernando de Soto, *The Mystery of Capital*.

²³⁹ For an optimistic assessment, see Stephen Moore and Julian L. Simon, *The Greatest Century That Ever Was: 25 Miraculous Trends of the Past 100 Years*, Policy Analysis No. 364, (Washington, D.C.: Cato Institute, 1999). Additional examples of general human progress are in Gregg Easterbrook, *The Progress Paradox: How Life Gets Better While People Feel Worse* (New York: Random House, 2003).

²⁴⁰ "What will happen when youth does what is asked, gets educated, and still can't find a job? Answer: They get very angry. I submit that youth unemployment, if unchecked, will cause decades of global terrorism. France today is only the tip of the iceberg." John Hatch, *Why is MicroFranchising Important to MFIs?*, November 2005.

²⁴¹ Allen Hammond, *Which World? Scenarios for the 21st Century* (Washington, D.C.: Island Press, 1998). Hammond uses the phrase "global destinies, regional choices" which is strikingly similar to the terminology that franchise industry insiders use to describe their methodology. C.f. Lee Vala's "The franchise business model is the ultimate manifestation of the popular refrain, 'Think globally, act locally'". Lee Vala. Presentation at the IFA Convention, Hollywood, FL, March 2005.

²⁴² Thomas L. Friedman, *The World is Flat: A Brief History of the Twenty-First Century* (New York: Farrar, Straus and Giroux, 2005).

²⁴³ Howard Rheingold, *Smart Mobs: The Next Social Revolution* (Cambridge, MA: Perseus Publishing, 2002).

²⁴⁴ I am indebted to Prof. Joan Dixon, Marriott School, BYU for helping me understand how profoundly information, communication and entertainment technologies have changed societies worldwide. Much of her recent fieldwork has been in village development in rural Indonesia.

²⁴⁵ Erik Simanis, Stuart Hart, Gordon Enk, Duncan Duke, Michael Gordon, Allyson Lippert, "Strategic Initiatives at the Base of the Pyramid: A Protocol for Mutual Value Creation," February 17, 2005 Draft.

powerful business model loose to achieve the UN Millennium Development Goals. People worldwide are calling for local enterprise creation on a massive scale. Franchisors know how to build business and social enterprise networks that scale rapidly. The art and science of franchising is well developed.²⁴⁶ Adapting it to meet the needs of the world's poor will trigger a revolutionary new approach to international development as the principal actors realize how quickly viable, sustainable enterprises can bring growth and hope to stagnant or receding micro economies.

In a remarkable document, The Shell Foundation articulates a number of best practices gleaned from five years of innovative work in global pro-poor energy initiatives:

- Shell, with a core competency in energy, focuses on energy related enterprises.
- These enterprises sell products to, employ, and are owned by poor people.
- Each local enterprise is or expects to soon become profitable.
- Each local enterprise gets most of its funding from local capital.
- Initial investments by “barefoot entrepreneurs” can be as low as \$1,000.
- The enterprises Shell is creating are designed to be highly scalable.
- These enterprises are blended from the “poverty” and “business” worlds.
- Dozens or even hundreds of micro enterprises are networked in a decentralized business model.
- Shell offers both financing help in conjunction with local banks and business development assistance.
- Emphasis is placed on sound and robust business plans.
- NGOs are involved with Shell in some of these enterprises.

So far, so good. The Shell Foundation is describing a classic MicroFranchise. The word “franchise,” though, never appears in their document and they describe their enterprises as “financially viable, hybrid ‘network business models’ capable of delivering pro-poor services on a large scale.”²⁴⁷

Why not create a brand, write a UFOC functional equivalent, engineer not just a business plan but a franchise operating system, call it a MicroFranchise and then scale it up to tens of thousands of network nodes? Shell Oil already belongs to the IFA. Like many other global energy companies, they use the franchise business model extensively in their petroleum retailing operations.²⁴⁸

²⁴⁶ For example, Cheryl Babcock heads the International Institute for Franchise Education in the H. Wayne Huizenga School of Business and Entrepreneurship at Nova Southeastern University in Ft. Lauderdale, FL.

²⁴⁷ Shell Foundation, Marc Lopatin, et al, *Enterprise Solutions to Poverty*. Similar examples are found in the article “Small is Profitable” by Manjeet Kripalani and Pete Engardio in *Business Week Online* August 26, 2002 where they describe businesses with the “benefits of scale, but the uniqueness of small size.” When biologists come across a life form in the wild, they attempt to quickly identify its taxonomy which allows them to take advantage of the scientific literature accumulated for that genus and species.

Identifying MicroFranchises by name will help development actors understand the “nature of the beast.”

²⁴⁸ At the IFA Convention in Florida in March 2005, I enjoyed getting to know Todd Campi, a native New Zealander based in Australia who is Shell Oil's Global Retail Franchise Channel Strategy Manager.

Five MicroFranchise Networks That Can Change the World

30,000 people, many of them children, die every day from preventable diseases. More than 2 billion people on earth suffer from water-borne diseases. Myriad problems stem from malnutrition in all of its insidious forms. Access to modern information, communication and entertainment technology has demonstrated its ability to lift entire communities quickly to new levels of prosperity. Education is a key driver of continued productivity in an increasingly competitive global economy.

The World Health Organization resolutely maintains that disease is the #1 drag on the world economy. Affordable access to high quality essential medicines is the key to curing infectious diseases. The Health Stores in Kenya are a good early stage example of a MicroFranchised network with pharmacies and clinics that dispense essential medicines, health supplies and routine ambulatory health care.²⁴⁹ The Farmacias de Similares network in Mexico is somewhat more advanced with several thousand MicroFranchised and company owned locations in nine countries.²⁵⁰

Clean water distributed by tiny local plants or point of use purifiers have huge MicroFranchised potential in most parts of the world. Procter & Gamble's PUR, KX Industries' World Filter and L'Eau's agua station are all viable candidates for the foundational technology. Strong markets exist in urban, peri-urban and rural settings.

Technology exists today for small scale integrated agriculture, aviculture and aquaculture food production facilities that can provide employment while improving the diets of millions.²⁵¹ Greenhouses with inexpensive drip irrigation systems, poultry and fish farms can be located in most inhabited parts of the planet. Advanced nutritional products like Plumpy'nut²⁵² or Procter & Gamble's micronutrient enriched NutriStar²⁵³ can greatly reduce the incidence and severity of malnutrition in vulnerable populations

People in villages, towns and peri-urban slums everywhere are clamoring for cell phones, computers and electronic media, the modern tools of the information, communications and entertainment technology revolution. Whoever solves the puzzle of widespread educational broadband connectivity access subsidized by nearby commercial access will have found one of the holy grails of scalable, sustainable global development. Information and connectivity offer fundamental power in today's wired world, and empowered humans can earn their way out of poverty's stifling clutch.

Primary education, almost ubiquitous in the world today, is beset with problems. The quality of education available in many communities is marginal at best. A thriving complementary education business exists in many parts of the world. India's Aptech, for

²⁴⁹ www.cfwhops.org

²⁵⁰ www.farmaciasdesimilares.com.mx. This organization also offers micro health insurance.

²⁵¹ One integrated system, refined since the early 1980's, is the Benson Institute's model that has proven successful in Africa and Latin America. Allen C. Christensen, et. al., *The Benson Institute Small-Scale Agriculture Model*, Benson Agriculture and Food Institute, BYU, Provo, UT, March 2003.

²⁵² "The Wonders of Plumpy'nut," *The Economist*, November 5, 2005.

²⁵³ See *Procter & Gamble: Combating "Hidden Hunger"* WBCSD Case Study, 2004.

example, offers computer based training for as low as \$7 per course at 2,500 MicroFranchised locations in 30 countries.²⁵⁴ The Pratham organization in India is demonstrating a remarkable ability to improve local educational outcomes at very modest cost, and in some communities their private, complementary educational institutions are self-sustaining.²⁵⁵

Economic Building Blocks

The following list of potential MicroFranchised private or social enterprises could provide a solid foundation for economic development in many parts of the world:²⁵⁶

- Accounting services, agricultural inputs, apparel
- Bakeries, barber shops, beauty parlors, bicycles, building materials, butcher shops
- Construction, cooking oil, cosmetics, courier services
- Electrical contracting, equipment rental (wheelbarrows, bicycles, etc.)
- Financial services, food, fuel, furniture
- Hardware, house wares and other specialty retailers
- Movie theaters
- Plumbing contracting
- Renewable energy, repair shops
- Transportation for commodities, transportation for people

In Clayton M. Christensen's compelling world view, innovation begins with highly trained specialists experimenting through trial and error, who then gradually discern patterns in their results. This pattern recognition leads to general laws, and finally to rules-based technology that many people worldwide can access and successfully implement. This "commoditization of expertise" makes it possible for non-specialists to achieve good outcomes by competently manipulating proven technology.²⁵⁷ In many cases, successful MicroFranchises will be built around proven technology that effectively encapsulates commoditized expertise. First movers will enjoy a competitive advantage as they deploy new technology in the developing world as soon as the price point becomes viable in a shared access business model.

Eco-Systems, Clusters and Value Chains

If it takes a village to raise a child, it should be obvious that no business operates in a vacuum. Economic activity takes place in an eco-system with anchor industries, lead firms, support industries, and a dizzying variety of micro, small, medium and large enterprises all contributing. Some of these enterprises are B to C, business to consumer.

²⁵⁴ www.aptech-education.com. CDI is a similar organization based in Brazil.

²⁵⁵ www.prathamusa.org, personal communication with Yogi Patel, Pratham USA, December 2004.

²⁵⁶ Appropriate technology solutions to enable many of these businesses are available at www.thesustainablevillage.com. Steve Troy's eclectic collection of development resources. Al Hammond and John Paul catalog dozens of intriguing possibilities in their "Technology Innovations at the Edge," WRI, A Development Through Enterprise Report, October 2005.

²⁵⁷ Clayton M. Christensen, personal communication, November 2005. Howard Rheingold suggests that in a wired world, innovation can also originate with the grass roots and flow the other direction. "Ten thousand literates can equal the power of one genius." Howard Rheingold, personal communication, November 2005.

The more interesting enterprises from an economic development perspective are B to B, business to business, because they tend to increase productivity and the amount of value added at various stages of production and distribution processes. Significant development happens when lead firms (often exporters) locally source an increasingly sophisticated array of products and services from integrated suppliers vertically linked in a value chain.²⁵⁸ Complementary enterprises can cluster to form a critical mass.

The reality in the Bolivias and Burkina Fasons of the world, though, is grinding poverty because contaminated, near toxic business eco-systems restrict most economic activity to agriculture, extractive industries, and low productivity B to C enterprises. Given that La Paz and Ouagadougou are not likely to emulate Shanghai or Bangalore in the short term, developing countries should create at least some economic growth by facilitating large numbers of MicroFranchises. Whether they cobble shoes or peddle trinkets on the street corner, micro and small entrepreneurs will be more productive and add more value to the local economy when they are horizontally linked in franchise networks. Franchises can supply small businesses with much of the nurturing eco-system inherent in an effective B to B value chain. Clustering is intrinsic to the franchise model.

Modern Luddites

At the dawn of the industrial age, Luddite gangs roamed Nottinghamshire, Yorkshire and Lancashire, destroying textile equipment as a form of protest against economic changes that threatened their livelihoods.²⁵⁹ The working class uprising in England's industrial heartland was so profoundly disruptive that at one time, there were more English troops deployed against the Luddites than against Napoleon Bonaparte on the Iberian Peninsula. Social unrest is a blunt instrument being shrewdly manipulated by disadvantaged groups all over the world. Whether they burn cars, decree work stoppages or barricade roads, modern social activists can and do bring economies to a screeching halt while focusing intense public attention on their cause.²⁶⁰

In most cases, modern activists demand the same thing the Luddites wanted: steady jobs. As MicroFranchise networks begin to transform under performing economies, it will be important to employ labor intensive rather than capital intensive production and distribution processes whenever possible to maximize local employment opportunities. Human, social and financial capital are so precious in developing countries that it makes no sense to squander blood, trust or treasure on internecine confrontation.

²⁵⁸ China's vaunted "supply chain cities" are outstanding contemporary examples of vertical integration driving economic growth. Dale Gledhill's impressive Grandway Honduras wood products manufacturing complex in Cholulteca is a more modest example, well within reach for many developing nations.

²⁵⁹ See Kirkpatrick Sale, *Rebels Against the Future: The Luddites and their War on the Industrial Revolution, Lessons for the Computer Age*, (New York: Perseus Publishing, 1996).

²⁶⁰ Tim Stay offers this sage parable: The developing world is like a freeway with three lanes of traffic and barricades so motorists cannot change lanes. Cars are whizzing by in the fast lane. The middle lane is more sluggish, but cars are still moving. The slow lane, though, is one big traffic jam. People are out of their cars, looking down the road, trying to figure out why nobody is moving. Eventually, the people in the slow lane become so angry that they forget about trying to get their lane moving again and focus on throwing rocks to slow down the other two lanes. Tim Stay, personal communication, September 2005.

The Development Ladder, Two Seasoned Perspectives

John Hatch has spent 40 years assisting the world's poor. A Development Alternatives, Inc. co-founder in the '70's, he went on to pioneer the village banking method of Microcredit. He founded FINCA, a global Microfinance leader operating in 23 countries. John likens the development process to a ladder. For most people on the planet, the ladder has just one or two top rungs, accessible only to the elites. Microcredit attempts to provide the first rung on the ladder, as close to the ground as possible.²⁶¹ MicroFranchising builds the second, third and fourth rungs to provide the all-important "missing middle" where most economic growth and development actually occur.²⁶²

The government of the Philippines has determined that only 13% of low income households in that country are viable candidates for Microcredit.²⁶³ Experience shows that very few of those households will establish businesses strong enough to provide full-time employment to even one other person besides the owner operator. Jovy Guanzon, who has helped over 10,000 Filipino micro business owners achieve some degree of success, thinks MicroFranchising is "exactly what we need" to create small enterprise growth and broad-based employment opportunities in metro Manila.²⁶⁴

What Are We Really Trying to Accomplish Again?

If a poor person is happy, are they better off than a wealthy individual who is depressed? If a country increases per capita GDP at the expense of species extinction, has society gained or lost? If SMEs are the engines of economic growth, how do the poorest of the poor benefit? Global development through local enterprise creation seeks:
Sustainability - economic profitability, social responsibility, environmental stewardship
Equality – flatter income distribution within a society²⁶⁵
Liberty - freedom so human development happens naturally
Fraternity - tolerance, diversity, transparency and an environment of personal safety and security. You can almost hear *La Marseillaise* in the background. Self actualization through community nurture is the goal.²⁶⁶

Humans, empowered with expanding choices, can begin to approach their potential.²⁶⁷

²⁶¹ John Hatch, *Small Fortunes: Microcredit and the Future of Poverty*, PBS Documentary, October 2005 Premiere. www.kbyutv.org/smallfortunes.

²⁶² Personal communication with John Hatch, October 2005.

²⁶³ 22% of households have entrepreneurial potential, but only 60% of those will risk a business loan.

²⁶⁴ Personal communication with Jovy Guanzon, October 2005.

²⁶⁵ In the US, the median income is approximately 90% of the mean. In Brazil with much higher inequality, the median income is only about 30% of the mean. Nancy Birdsall, cited in David Rothkopf, "Pain in the Middle," *Newsweek*, November 21, 2005.

²⁶⁶ Pierre Omidyar describes the goal as reprogramming certain key lines in the "source code of humanity." www.omidyar.net/group/humansourcecode. The net effect will be to move from exploitation to cooperation, to change attitudes from an acquisitive, hoarding, ego-centric scarcity mentality to an abundance mentality. One of the finest examples of this altruistic mentality is memorialized in the famous John Trumbull painting of Washington resigning his commission that hangs in the rotunda of the US Capitol in Washington, D.C. After his Revolutionary War triumph, George Washington could have been king, but he returned to Mount Vernon to be a farmer, thus helping form the character of a new nation.

Every person on the planet deserves the opportunity to improve their talents. Human dignity eradicates global poverty.²⁶⁸

At the same time, companies who expressly serve low income communities can do very well by doing good. Vincent Ricasio says that alleviating poverty through socially responsible enterprise represents “the biggest opportunity for wealth creation” in world history.²⁶⁹ Companies including Cemex and Unilever with overtly pro poor cultures are global profit leaders in their market segments. MicroFranchises will become important to at least five different constituencies:

- Multinational corporations²⁷⁰
- Large domestic corporations
- Humanitarian NGOs
- Microfinance Institutions
- Domestic franchisors

Sherle Schwenninger believes that only by “extending the system of mass affluence found in the United States and Europe to the developing world” can we enjoy prosperity and peace in the future.²⁷¹ That sounds like a job for the franchise business model.

Recap

World poverty causes untold suffering and squandered human potential. Profitable private and social enterprises help families and nations lift themselves out of misery. Large numbers of successful small, locally-owned enterprises in the developing world will dramatically reduce global poverty. The franchise business model is uniquely adept at creating large numbers of successful small, locally-owned enterprises. Organizations in the future will be more networked and less hierarchical.²⁷²

Microfinance institutions can improve their portfolio performance and impact by offering their clients MicroFranchised business formats bundled with financing packages.

Humanitarian NGOs can become partially sustainable by deploying the MicroFranchise business model throughout their operations in the developing world. Societal institutions can accelerate governance reform, increase transparency, expand business formality and strengthen private property protection throughout their economies by proliferating

²⁶⁷ The real business of the franchisor is “putting people into business and providing them with the systems and support that enables them to achieve their personal and financial aspirations.” Greg Nathan, *Profitable Partnerships*, (Toowong, Queensland, Australia: Franchise Relationships Institute, 2002)

²⁶⁸ “Being human and being poor are incompatible.” Personal communication with Muhammad Yunus, July 2005.

²⁶⁹ Vincent R. Ricasio, “A Social Enterprise Approach to Combating Poverty,” 2005.

²⁷⁰ Eliot Jamison, emerging markets consultant, intelligently asks how the 175 WBCSD companies can be “catalysts to create MicroFranchise networks?” Eliot Jamison, personal communication, November 2005.

²⁷¹ Sherle R. Schwenninger, “Revamping American Grand Strategy,” *World Policy Journal*, November 1, 2003.

²⁷² “We’re going from a world where value is largely created in vertical silos of command and control to a world where value will be increasingly created by who you connect and collaborate with horizontally.” Thomas L. Friedman, presentation at TIECON 2005, Santa Clara, CA, May 2005.

MicroFranchise networks. Organizations trying to introduce appropriate disruptive products and services in the developing world should consider using MicroFranchises as their delivery vehicle. Multinational corporations who want to engage the BOP as customers and business partners should consider incorporating the MicroFranchise business model into their emerging market strategy.²⁷³ MicroFranchises can help create widespread indigenous, inclusive capitalism.²⁷⁴

Billions of marginalized humans can improve their quality of life by adopting sustainable, environmentally friendly technologies. The innovative MicroFranchise business model can help deliver the products and services these people need in a way that is socially responsible and economically viable. The MicroFranchise movement is building momentum worldwide. Increased mindshare and political will can accelerate its progress. All humanity will benefit.

“I have the audacity to believe that people everywhere can have three meals a day for their bodies, education and culture for their minds, and dignity, equality and freedom for their spirits.” Martin Luther King, Jr.

“Systems permit ordinary people to achieve extraordinary results, predictably.” Michael Gerber, *The E Myth*.

Acronym Index

ABA American Bar Association

ABF Brazilian Franchising Association

ACCION Acción International – MFI holding company

ACE Academy for Creating Enterprise, Cebu, Philippines

AFDB African Development Bank

AIDS acquired immune deficiency syndrome

AMD Advanced Micro Devices

AUV average unit volume

BHAG big, hairy, audacious goal

BOP base of the pyramid – the world’s poor

BYU Brigham Young University

CEO chief executive officer

CD compact disk

CDI Committee for the Democratization of Information Resources, Brazil

CESR Center for Economic Self Reliance, Marriott School of Management, BYU

CFW Child and Family Wellness – MicroFranchised pharmacies in East Africa

²⁷³ John Hatch sees “the imminent convergence of free enterprise from top-down, multinational corporations with free enterprise from the bottom up, the world’s 100 million micro entrepreneurs, a strategic partnership that I believe has the potential to end poverty on our planet forever.” FINCA International Annual Report 2003, Founder’s Message. Most successful MNC BOP initiatives in recent years utilize some form of MicroFranchising as their operative business model.

²⁷⁴ Jane Jacobs describes effective development agents as “large symbiotic collections of small enterprises” indigenous to a city or its surrounding regions linked together in “swiftly emerging, logical chains” forming a “web of symbiotic relationships”. Jane Jacobs, *Cities and the Wealth of Nations*.

CGAP Consultative Group to Assist the Poor, World Bank
 CSO citizen sector organization
 DAI Development Alternatives, Inc.
 DNA deoxyribonucleic acid
 DTDC Door to Door Courier, a MicroFranchise network in India
 EMI Enterprise Mentors International
 EU European Union
 FDI foreign direct investment
 FEC Full Economic Citizenship, Ashoka initiative
 FINCA Foundation for International Community Assistance
 FUNDES Fundación del Desarrollo
 GDP gross domestic product
 GRI Global Reporting Initiative
 HQ headquarters or home office
 HIV human immunodeficiency virus
 HP Hewlett Packard
 IDB Inter American Development Bank
 IEA Institute of Economic Affairs, UK
 IFA International Franchise Association
 IFC International Finance Corporation, World Bank
 IIE Institute for International Economics
 ILD Institute for Liberty and Democracy, Peru
 IMF International Monetary Fund
 IPP intellectual property protection
 IREN Inter Region Economic Network, Kenyan think tank
 IQ intelligence quotient
 ISO International Standards Organization
 ITC Imperial Tobacco Company, India
 KFC Kentucky Fried Chicken
 LDC large domestic corporation (also less developed countries)
 LDS Latter-day Saints (Mormons)
 LED light emitting diode
 MCA Millennium Challenge Account
 MCC Millennium Challenge Corporation
 MD Doctor of Medicine
 MDB Multilateral Development Bank, i.e. World Bank, AFDB, IDB, etc.
 MF Microfinance
 MFI Microfinance institution
 MFDI MicroFranchise Development Initiative, BYU Marriott School of Management
 MIF Multilateral Investment Fund, IDB
 MNA Movimiento Nacional Anticorrupción, Mexico
 MNC multinational corporation
 MSE micro and small enterprise
 NGO non governmental organization – non profit
 NIS newly independent states, formerly part of the Soviet Union
 NSU Nova Southeastern University

ODA overseas development aid – foreign aid
OECD Organization for Economic Co-operation and Development
OPIC Overseas Private Investment Corporation (US Department of Commerce)
PEPFAR President’s Emergency Plan for AIDS Relief
PhD Doctor of Philosophy
PIC Personal Internet Communicator from AMD
PMDF Philippine Microenterprise Development Foundation
POS Point of Sale - cash registers, merchant card terminals
PPP purchasing power parity
SBA Small Business Administration
SHEF Sustainable Healthcare Enterprise Foundation (now Health Stores Foundation)
SKU stocking unit or inventory line item
SME small and medium enterprise
SMS short message service – text messages on cell phones
SLEN sustainable local enterprise networks
TQM total quality management
UFOC Uniform Franchise Offering Circular
UK United Kingdom
UMU Uganda Microfinance Union, Acción
UMWA United Mine Workers of America
UNDP United Nations Development Programme
US United States of America
USAID US Agency for International Development
VP Vice President
WBCSD World Business Council for Sustainable Development
WRI World Resources Institute
WTO World Trade Organization

People Index

Adolphson, Don, Profesor, BYU
Annan, Kofi, Secretary General, United Nations
Arrington, Leonard J., economic historian
Babcock, Cheryl, Director, International Institute for Franchise Education, NSU
Bazoberry, Eduardo, General Manager, Prodem (Bolivia)
Bernstein, Andrew, Senior Writer, Ayn Rand Institute
Birdsall, Nancy, economist and President, Center for Global Development
Blair, Tony, Prime Minister of the UK
Blundell, John, Director, Institute of Economic Affairs (UK)
Boorstin, Louis C., Manager, Grassroots Business Organizations, IFC
Brown, Mark Malloch, former Administrator, UNDP, now chief of staff to Kofi Annan
Budinich, Valeria, VP for Full Economic Citizenship (FEC), Ashoka
Burnes, Allen, VP of High Growth Markets, Motorola
Bush, George W., President of the US
Christensen, Clayton M., Professor, Harvard Business School
Clifton, Randy, Sr. VP, Franchising, Pizzeria Uno
Collins, Jim, business author
Dailey, James, Technical Project Manager, Grameen Foundation USA

Davis, Geoff, CEO, Unitus, a Microfinance accelerator
 De Soto, Hernando, Founder, Institute of Liberty and Democracy (Peru)
 DeBolt, Don, former President, International Franchise Association
 DeLuca, Fred, President and Co-Founder, Subway
 Demille, Cecil B., Hollywood producer, best known for *The Ten Commandments* (1956)
 Deveshwar, Yogesh C., Chairman, Imperial Tobacco Company (India)
 Dichter, Thomas W., consultant to USAID, UNDP, and the World Bank
 Dixon, Joan, Professor, BYU
 Dwyer, Jr., Donald, Director, International Operations, The Dwyer Group
 Easterly, William, Senior Fellow, Center for Global Development, IIE
 Fairbourne, Jason, Director, MicroFranchise Development Initiative, BYU
 Fehr, Ersnt, Director, Institute for Empirical Research in Economics (Switzerland)
 Feltenstein, Sid, Chairman, International Franchise Association
 Fiorina, Carly, former CEO, HP
 Firpo, Janine, Director, Global Multisector Initiatives, HP
 Frey, Martin, Director, Division of Business and Economic Development, State of Utah
 Friedman, Thomas L., foreign affairs columnist, New York Times
 Gandhi, Mahatma, father of modern India
 Gerber, Michael, entrepreneur, business author
 Gibson, Stephen W., Founder, ACE (Philippines)
 Glassman, James, Resident Fellow, American Enterprise Institute
 González Torres, Victor, President, Farmacias de Similares (Mexico)
 Gordon, Marlene, intellectual property attorney, Burger King
 Graham, Scott, Strategic Alliances Manager, FINCA
 Grezo, Charlotte, Director of Corporate Responsibility, Vodafone
 Guanzon, Jovy, Executive Director, PMDF (Philippines)
 Hammond, Allen, VP Innovation & Special Projects, WRI
 Harmon, James A., Chairman, WRI
 Hart, Stuart, Professor, Cornell
 Hatch, John, Founder, FINCA
 Hernandez, Monica, Executive Director, Banco Solidario (Ecuador)
 Hillstrom, Scott, Founder, The Health Stores (Kenya) and Franchise Labs
 Hinckley, Gordon B., President, The Church of Jesus Christ of Latter-day Saints
 Hinojosa, Raul, Profesor, UCLA
 Hyduke, John, VP, Franchise Development, Big O Tires
 Jamison, Eliot, Partner, Origo
 Jefferson, Thomas, 3rd President, US, author of the Declaration of Independence
 Kroc, Ray, Founder, McDonald's Corporation
 Lagos, Beatriz, street vendor, Cuzco (Peru)
 Landes, David S., Emeritus Professor, Harvard University
 Larson, Alan, Under Secretary of State, US State Department
 Lash, Jonathan, President, WRI
 Layton, Tim, Managing Partner, Sorenson Capital
 Lewis, John L., President, UMWA (1920-1959)
 Lim, Samie, Chairman, Philippine Franchise Association
 Littlefield, Elizabeth, CEO, CGAP, World Bank

Lopatin, Marc, Communications Advisor, The Shell Foundation
 Lyman, Paul, Juvenile Judge, Utah State Courts
 Macmillan, Graham, Director, Scojo Foundaion
 Madsen, Joel, Chairman, Chasqui Humanitarian
 Mandela, Nelson, former President of South Africa
 Manwaring, Todd, Director, CESR
 Maren, Michael, Peace Corps volunteer, journalist, author
 Marsden, Craig, emergency physician
 Martins, Carlos, Founder, Wizard Schools (Brazil)
 Mauro, Paulo Cesar, Director of International Relations, ABF
 McGovern, Kevin, Chairman, McGovern Capital
 McNealy, Scott, Chairman, Sun Microsystems
 Mihoubi, Bachir, VP, Global Franchising, Caribou Coffee
 Milanovic, Branko, Sr. Associate, Carnegie Endowment for International Peace
 Miller, Kevin, head of North American Subway Owner's Council
 Mitchell, John, President, UMWA (1898-1920)
 Mor, Nachiket, Executive Director, ICICI Bank (India)
 Mulder, Herman, Senior Executive VP, ABN Amro Bank
 Munnecke, Tom, Founder, Giving Space and Uplift Academy
 Novogratz, Jacqueline, CEO, Acumen Fund
 Omidyar, Pierre, Founder, eBay
 Otero, María, President and CEO, Acción International
 Patel, Yogi, President, Pratham USA
 Pinochet, Augusto, former President of Chile
 Prahalad, C. K., Professor, University of Michigan
 Roach, John, journalist, National Geographic
 Ricasio, Vincent R., retired economist and investment banker
 Robertson, Peter J., Vice Chairman, Chevron Texaco
 Rodrigues, Christopher, President and CEO, VISA International
 Rodrik, Dani, Professor, Harvard University
 Rothkopf, David, international correspondent, Newsweek
 Ruiz, Hector, President and CEO, AMD Worldwide
 Sachs, Jeffrey, Director, The Earth Institute, Colombia and The UN Millennium Project
 Sandbrook, Richard, Senior Advisor, UNDP
 San Roman, Maximo, Former Vice President of Peru; Owner, Nova Industries (Peru)
 Sarin, Arun, CEO, Vodafone
 Savage, John, VP, Savage Industries
 Schmidheiny, Stephan, Founder, WBCSD
 Schwenninger, Sherle R., Director, Global Middle Class Program, New America Fdn.
 Seawright, Kristie, Professor, BYU
 Seid, Michael H., Managing Director, Michael H. Seid & Associates
 Sen, Amartya, Nobel prize winning economist
 Shikwati, James, founder, IREN (Kenya)
 Shuster, Scott, President, The Shuster Group
 Slaughter, Chuck, CEO, SHEF
 Smith, Adam, father of modern economics

Sowell, Thomas, Senior Fellow, Hoover Institution, Stanford University
 Stay, Tim, Board Member, Unitus Global Microfinance Accelerator
 Stephens, David, CEO, OnSat
 Stone, Sharon, actress, model and producer
 Terry, Donald, Manager, The MIF
 Tesfamichael, Gebreselassie Y., economist, former Finance Minister, Eritrea
 Thatcher, Margaret, former Prime Minister, UK
 Tull, Ann, Director of International Development, Maui Wowi
 Turner, Ted, media entrepreneur, social and environmental activist
 Vala, Lee, Sr., VP, The Quizno's Corporation
 Weber, Barbara, Development Specialist, Grameen Technology Center
 Wheeler, David, Professor, York University (Canada)
 Will, George F., columnist, Washington Post
 Williams, Walter, Professor, George Mason University
 Williamson, John, Senior Fellow, Institute of International Economics
 Wise, Holly, Director, Global Development Alliance, USAID
 Young, Brigham, pioneer colonizer of Utah
 Yunus, Muhammad, Founder, Grameen Bank (Bangladesh)

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Kirk Magleby – Autobiographical, Historiographical & Contact Info

I am married to the former Shannon Savage. We have four children, a daughter and son-in-law, and an “adopted” Ukrainian son. I founded Nuvek www.nuvek.com, a technology firm with offices in Idaho, Utah and Mexico. I serve on the board of Ascend, A Humanitarian Alliance www.ascendalliance.org and on the steering committee for the MicroFranchise Development Initiative, Center for Economic Self-Reliance www.marriottschool.byu.edu/selfreliance, Marriott School of Management, BYU. I have an undergraduate degree in Economics with a minor in Latin American Studies from BYU. I served a mission for the LDS Church in Peru from 1972 – 1974. I have empathy

for the oppressed and impoverished in our world. I have traveled extensively throughout the Americas for many years and consider myself a well-informed student of poverty and international development. My personal quest to end world poverty began in Bolivia in 1974. For decades I despaired that the issue was so complex as to be intractable. Thankfully, the last few years have seen such a flurry of encouraging developments that I now think poverty is a problem we can solve in our lifetime with appropriate technology and effective business models. I moderate the poverty group on Omidyar.net where this paper is available: www.omidyar.net/group/poverty/file/7.35.11055472357. The Spanish version is at: www.omidyar.net/group/poverty/file/3.15.11188136153. During November 2004, an earlier version of this paper was presented at colloquia in Provo, Utah and in La Paz, Santa Cruz, and Cochabamba, Bolivia. In December 2004, a version of this paper was included on the resource CD for the World Resources Institute San Francisco Conference “Eradicating Poverty through Profit: Making Business Work for the Poor.” In June 2005 links to the paper were posted in several topic areas on www.developmentgateway.org and www.nextbillion.net. In July 2005 the Spanish version of the paper was featured on the Ecuadorian Franchise Association website www.aefran.org. Links to the paper are also found on the Bangladesh Microfinance portal www.bangladeshgateway.org. In October 2005, thanks to a Google grant, sponsored links to the paper began appearing on certain Google searches in both English and Spanish. In November 2005, the paper was cited in the USAID sponsored case study “What Works: Healthstore’s Franchise Approach to Healthcare,” published by WRI.

Kirk Magleby, 801.756.8854, microfranchises@gmail.com

Other Relevant Resources

A concise 7 page catalog of MicroFranchise business opportunities aimed at BOP enterprisers: www.omidyar.net/group/poverty/file/4.35.11298662354.

A quick 3 page recap of worldwide MicroFranchising activities:
www.omidyar.net/group/poverty/file/7.09.11319421097.

Notes of a global MicroFranchise strategy session held in San Francisco, November 21, 2005, 9 pages: www.omidyar.net/group/poverty/file/4.39.11333853394.

Notes of the first MicroFranchise Learning Lab held in Park City, Utah, September 15-16, 2005, 13 pages: www.omidyar.net/group/poverty/file/3.46.11291598463.

Notes of the WRI BOP Conference in Mexico City, September 1, 2005, 16 pages:
www.omidyar.net/group/poverty/file/5.17.11265500175.

Notes of the seminal WRI BOP Conference in San Francisco, California, “Eradicating Poverty through Profits,” December 11-14, 2004, 42 pages:
www.omidyar.net/group/poverty/file/9.98.11055472989.