# CHARACTERIZING EMERGING MARKETS

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*Abstract. This article looks at Emerging Markets and Low Income Sector characteristics within the scope of understanding the generalizability of the market-based approaches developed in High Income Countries. The literature review highlights that existing studies have not presented clear classifications of characterics and that current listings are partial.*

*The article adopts and adapts the market environment theory classification and summarizes the published and documented characteristics of EM and LIS. In the process it highlights that it is necessary to distinguish between primary and secondary characteristics and that many of these characteristics overlap. Finally, it builds on the organizational theory distinction between objective and enacted environment to discuss low income sector's emerging market environments as constraints or opportunities.*

*Key words: Emerging markets, low income sectors, market environmental characteristics.*

## Introduction

Prahalad and Hart's (2002) seminal article, *The Fortune at the Bottom of the Pyramid*, highlighted the opportunities associated to the Low Income Sectors (LIS[1]) of BRIC's. Furthermore it argued that market-based approaches should be adopted to address the LIS (Simanis & Hart, 2008). In Hammond et al.'s (2007) terms, "being poor does not eliminate commerce and market processes" (p.6).

Marketing is "context dependent" (Sheth & Sisodia, 1999, p.72), thus translating strategies and practices from developed markets into emerging markets (EM) is not always possible. Particularly, when adopting market-based approaches to address the LIS, since macro environmental conditions are often dysfunctional and consumption habits differ from those in advanced markets (Sheth, 2011). Additionally, EMs include coun-

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1    The term LIS (low income sectors), is used encompassing other terms adopted in the literature such as BOP (bottom of the pyramid) and LIC (low income consumers).

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tries as diverse as Peru, India, China, and Ghana, just to mention a few. These countries not only show heterogeneity in different aspects of the market constitution but also the four billion people that constitute the LIS are not a "monolith" (Prahalad 2010, p.6). As Portocarrero and Delgado (2010) highlight, LIS living in remote regions in the Andean Plateau differ from those in the thick Amazonian rainforest or those living in densely populated neighborhoods located around urban areas. Thus, understanding the EM environmental characteristics is relevant because it allows scholars to assess the "generalizability of marketing theories and the extent to which they are bounded by the institutional context of HIC[2]" (Burgess & Steenkamp, 2006, p. 341).

The literature review shows that complete characterizations are missing (Burgess & Steenkamp, 2006; Gradl et al., 2008; Márquez et al., 2010; Sheth, 2011) and that it is necessary to transcend the prevailing beliefs and stereotypes surrounding the emerging markets (Sheth, 2011). In short, it is necessary for the future of marketing science and practice to conduct more research in the so-called emerging markets (Burgess & Steenkamp, 2006). This paper aims at addressing this gap.

McInnis (2011) adopts the astronaut analogy, "whose view from the spaceship allows him or her step back from the mountains, deserts, cities, and seas to see Earth in its entirety" (p.144), to exemplify a particular type of conceptual contribution, labeled summarizing. This paper will summarize the LIS and EM environmental characteristics. The paper adopts the market environment theory as it provides an overall categorization that can be used as a framework to characterize the EM and the LIS.

The remainder of this article is organized as follows. First, the market environment and EM literature is reviewed to suggest an overall framework. Next, the EM characteristics are presented and discussed. The paper closes with the future research and managerial and academic implications sections.

## An overall framework to characterize the emerging market and the low income sector

This section reviews the market environment literature to suggest an overall framework to portray the EM-LIS. The discussion of the environment-organization relationship is not restricted to the field of marketing. Moreover, organizational theorists and strategic management scholars have had a leading role in documenting the importance of the environment. The 60's highlighted the importance of the environment (Dill, 1958; Thompson, 1967), the 70's looked at the determinants of the environment (Duncan, 1972; Pfeffer & Salancik, 1978) and the 80's tried to answer the question of whether an external objective environment existed (Bourgeois, 1980; Weick & Daft, 1983; Smircich & Stubbart, 1985; Mintzberg, 1987).

Duncan (1972) defined the environment as "the totality of physical and social factors that are taken directly into consideration in the decision-making behavior of indi-

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[2]    High income countries (HIC)

viduals in the organization" (p.314). He distinguished between internal and external environment; the *internal environment* consists of "those relevant physical and social factors within the boundaries of the organization or specific decision unit that are taken directly into consideration in the decision-making behavior of individuals in that system", whilst the *external environment* is "the relevant physical and social factors outside the boundaries of the organization or specific decision units that are taken directly into consideration" (p.314). The external environment has been decomposed in two layers that have distinct influence on policy-makers: the task environment and the general environment (Dill, 1958).

This classification of the dimensions of the external environment has been adopted in the marketing literature. Thorelli (1995), building on organizational ecology theory, describes the environment as a continuum that starts with the *extra-environment* identified as those areas of the total environment that are negligible or have zero relevance to the organization, the *macro-environment* that includes such factors as the general social, economic, political and technological climate in which the organization finds itself operating, the *task environment* seen as that part of the total setting within which the organization is transacting and competing, the *auto-setting* sees the broader organization of which the unit under study is a semi-autonomous part and, finally, the proper *organization*. The paper focuses on the task and general[3] environment. Their differences and categorization are discussed below.

The **task environment** (Thompson, 1967) is the part of the total setting with which the organization is transacting and in which it is competing, specifically: *consumers* (end-users), *suppliers* (material, labor, capital, equipment and workspace), *competitors* (markets and resources) and *distributors*.

The **general environment** (Hatch & Cunliffe, 2006) is divided into different sectors: *social sector* (class structure, demographics, mobility patterns, life styles, social movements, amongst others), *cultural sector* (history, traditions, normative expectations for behavior, beliefs and values), *legal sector* (legal practices, laws, etc.), *political sector* (distribution and concentration of power, nature of political system), *economic sector* (labor, financial and goods/services markets, private vs. public, fiscal policies, consumption habits, banking system, etc.), *technology sector* (knowledge and information, scientific developments and applications, etc.), and *physical sector* (natural resources, effects of nature).

When this categorization is applied to EM-LIS, the *physical infrastructure* aspects need to be added. Whilst the physical variable (Hatch & Cunliffe, 2006) refers exclusively to natural influences, the physical infrastructure variable refers to the roads, logistics, transportation, electricity, running water, etc. (Gradl et al., 2008; Sheth, 2011). Additionally, in order to hold a clear dialogue with the EM literature, the terms used by the EM authors to describe general environment are adopted:

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3    The term general environment  is used to be synonymous with macro environment (Thorelli, 1995) or external environment (Kotler & Armstrong, 2006)

- Culture system (rather than culture), defined as the "culturally supported beliefs, attitudes, habits, norms and behaviors" (Burgess & Steenkamp, 2006, p. 341). Cultural value priorities underlie most aspects of everyday life and relate to generalized beliefs people hold about themselves, their social and physical environment, and the spiritual world (Bond et al., 2004).
- Socio-political governance (rather than political), defined as the sociopolitical characteristics that appear due to the influence of diverse socio-political institutions (Sheth, 2011).
- Socio-economic system (rather than economic), defined as "macroeconomic and demographic characteristics, levels of within country diversity and dynamics caused by rapid social, political, and economic change." (Burgess & Steenkamp, 2006, p. 341).
- Regulatory system (rather than legal), defined as "the capacity to establish formal rules, inspect society member's conformity to them, and if necessary, impose sanctions. It includes the presence and efficacy of regulatory intuitions and the associated legal system that exist to ensure stability, order and continuity of societies." (Burgess & Steenkamp, 2006, p. 342).
- Physical infrastructure (rather than physical as natural), defined as the infrastructural characteristics that provide communication, transportation, data transfer and provision of utilities (Gradl et al., 2008).

Figure 1 presents a visual synthesis of the task and general environment categorization.
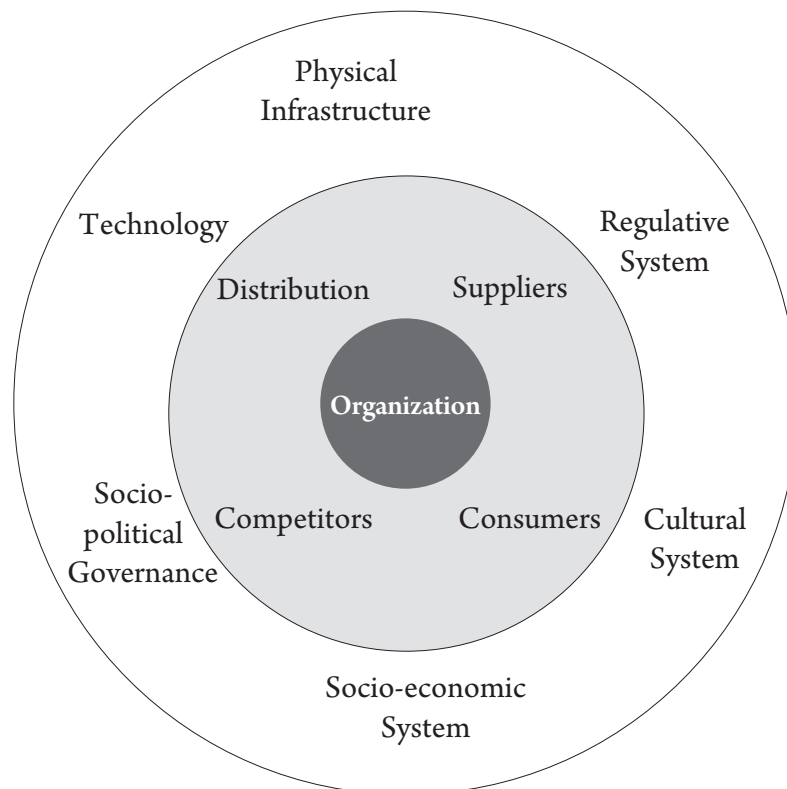


FIGURE 1: **The task and general environment categorization**
Adapted from Hatch and Cunliffe, 2006

## Characteristics of the Emerging market and Low Income Sector

The World Trade Organization, the United Nations and the World Bank classify countries based on diverse criteria (human development index, gross national income per capita, etc.). Country classifications under these diverse criteria have a high degree of overlapping (Burgess & Steenkamp, 2006); however, these institutions do not provide in-depth descriptions of the EM characteristics.

This section reviews the descriptions and characterizations suggested by Frankel and Rose (1995); Barros and Lee (2000); Olson (2000); London and Hart (2004); Prahalad (2004); Burgess and Steenkamp (2006); Beck et al. (2006); Yunus (2007); Hammond et al. (2007); Hart (2008); Kandachar and Halme (2008); UNDP (2008); Gradl et al. (2008); Bruni Celli et al. (2010); Márquez et al. (2010); Portocarrero and Delgado (2010); Reficco and Berger (2010); Prahalad (2010); Gomez Samper et al. (2010); Karnani (2011); and Sheth (2011). "The goal of summarization is to take stock of, digesting, recapping, and reducing what is known to a manageable set of key takeaways. […] Papers with the goal of summarization are commonly labeled review papers or critical syntheses" (McInnis, 2011, p. 144).

Before presenting the EM-LIS characteristics it is necessary to make some clarifications. First, aspects listed are relevant characteristics that need to be taken into consideration when carrying out market based approaches in emerging markets; yet it is necessary to clarify there is a huge variance between countries. Second, the criterion adopted to classify each characteristic has been to follow most habitual categorization of a given aspect. Third, many of these aspects are interrelated; this point is further discussed in the next section. Fourth, a distinction has been made between primary and secondary characteristics; this distinction will be further discussed in the next section. The listing only includes primary characteristics. Finally, as any criterion, it always implies a certain degree of arbitrariness; our focus is to provide a simple but thorough listing. The characteristics are presented and discussed next and reproduced in a table format in Appendix I.

### General Environment

*Regulative system*

- Legislation is missing or not enforced
- Moderate scores for shareholder rights and creditor rights
- Risk of appropriation or contract repudiation
- Poor judicial system efficiency
- Relevant red tape for all kind of business related procedures
- Different levels of corruption
- Existence of informal business links with organizations and people as well as informal labor

*Socioeconomic system*
- Demographic:
  - Large family size
  - Youth of EM populations
  - Geographically disperse
- Diversity:
  - Extreme socioeconomic variation within EM populations
  - Different types of poverty
  - Urban LIS different from Rural LIS
  - Unemployment
  - Gender and race discrimination
- Crowdedness
- Everyday violence
- Hyper-inflation, inflation, default
- Basic banking functions

*Socio-political governance*
- Socio-political institutions have enormous influence
- Markets governed by institutions and less by competition
- Numerous government-owned and -operated enterprises with monopolistic powers
- Dynamics, rapid socio-political change
- Political barriers

*Infrastructure*
- Poor or inadequate infrastructure: physical roads, logistics, storage
- Poor or unstable provision of electricity, running water, gas
- Poor or inadequate educational and health services
- Poor infrastructure to cope with natural events

*Technology*
- Lack of communication, information, and transaction technologies
- Lack of data transfer networks

*Cultural system*
- Cultural embeddedness and hierarchy
- Maintenance of the status quo and discouraged behaviors that disrupt in-group solidarity
- Autocratic decision making

*Task Environment variables*

*Consumer*

- Knowledge and skills
  - School dropout and low child enrolment
  - Illiteracy
  - Low formal education
  - Low technical skills
  - Low product knowledge
- Income
  - Low income[4]
  - No consistent income
  - Lack of access to financial products and services.
  - No commercial insurance
- Household
  - Lack of storing space
  - Informal settlements

*Suppliers/producers*

- Chronic shortage of resources in production
- Lack of managerial capabilities by local community groups

*Distribution*

- Traditional mom and pop stores
- Inefficient distribution networks, especially in rural areas
- Lack of market intermediaries to consolidate or distribute information
- Patronage of retail outlets

*Competitors*

- Consumption of unbranded products and services
- Mostly small enterprises
- Household as production unit: availability of labor at home: women and children
- Many branded products and services are not available in rural markets
- Prevalence of used products as direct competitors
- Prevalence of barter exchange or reciprocal offerings.

## Discussion of the emerging market and low income sector characteristics

This section discusses three points considering the previous characterization: interrelatedness or overlapping of characteristics, primary vs. secondary characteristics and

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4    The World Bank (PovcalNet World Bank http://iresearch.worldbank.org/PovcalNet/index.htm?1#) identifies the $1,25/day poverty level (extreme poverty), Prahalad (2004) adopts  the $2/day poverty level (bottom of the pyramid, BoP) and Karnani (2011) also identifies a $8/day cut point.

objective vs. subjective environment. Discussing these three aspects is relevant because it provides a clearer picture of the complexity in the EM-LIS environment.

*Interrelatedness or overlapping of characteristics*

Although organization theorists separate the general environment into clear and distinct dimensions, the influences of each aspect overlap (Hatch & Cunliffe, 2006). This interdependence is even more intertwined in EM involving aspects of both the general environment and the task environment (see Figure 2). In this sense, there can be three types of *overlapping*: between aspects of the general environment, between aspects of the task environment, or between aspects of both environments. A couple of examples are provided to help visualize this interrelatedness:

- General-General: corruption is related to missing or unenforced legislation. Geographically disperse population is related to lack of physical infrastructure (roads, communications, etc.).
- Task-Task: prevalence of barter exchange is related to absence of consistent income. Prevalence of unbranded products is related to low income.
- General-Task: poor or inadequate infrastructure is related to inefficient distribution networks. Unemployment is related to production of homemade products.
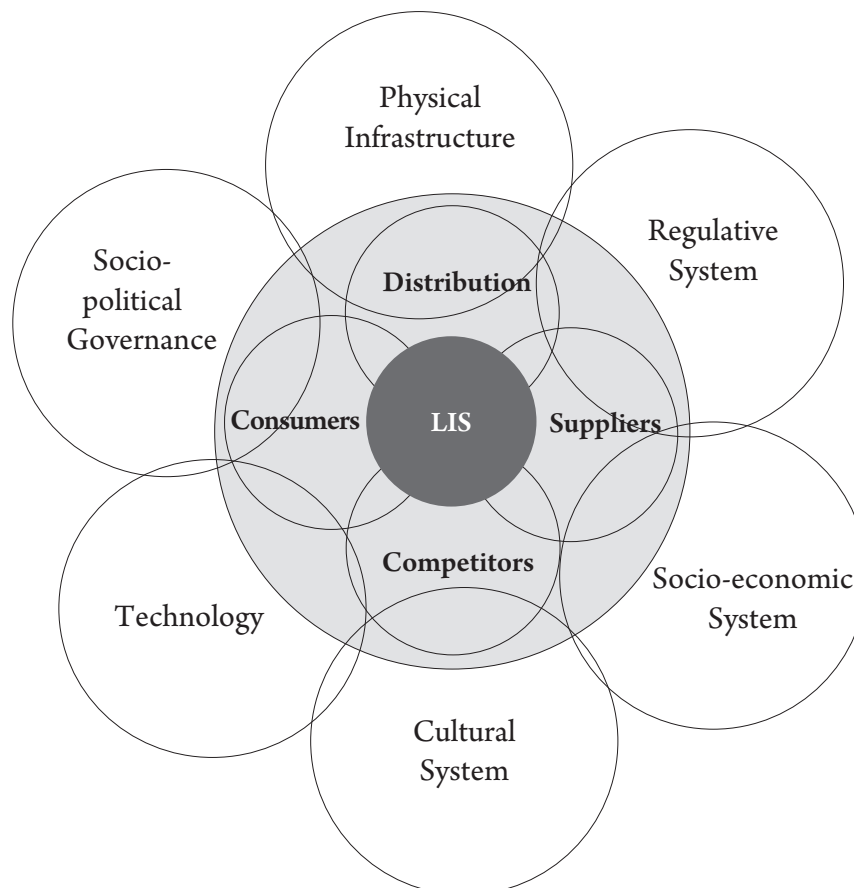


FIGURE 2: **Overlapping variables in the general environment of EM-LIS**
Adapted from Hatch and Cunliffe, 2006

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*Differentiating primary from secondary characteristics*

As in any new area of study, initial works often describe the most outstanding characteristic. It is only in later works that distinctions between causes and consequences can be made. Some examples are presented below.

- Social exclusion defined as a process whereby individuals and groups are denied access to opportunities (Márquez et al., 2010), is best considered a consequence from diverse primary characteristics such as poor legislation, unemployment, low formal education, etc.
- Malnutrition (Karnani, 2011) is an outcome from characteristics such as low income, low product knowledge, poor health services, etc.
- Preference for small package sizes and frequent shopping (Burgess & Steenkamp, 2006), is an effect from variable income, lack of storing space, poor or unstable provision of electricity, etc.
- Unfulfilled basic needs (Kandachar & Halme, 2008), is a result from low income, unemployment, poor educational and health services, etc.

*The Objective Environment vs. the Subjective Environment*

As stated above, organizational theorists and strategic management scholars tried to answer the question of whether an external objective environment existed. Two approaches have been identified: objective environment and subjective environment. Scholars on which this paper has based its literature review have studied and characterized emerging market environment implicitly adopting one of these two approaches.

For example, Karnani (2011) looks at low technical skills, illiteracy and diseconomies of scale and concludes that microcredit and entrepreneurial initiatives from the LIS fail and that "employment is the solution" (Karnani, 2011, p.145). Burgess and Steenkamp (2006) look at institutional context and conclude that the absence of conditions in the institutional context enables markets to function efficiently. These scholars advocate *environmental determinism*. They imply that an objective environment exists; i.e., they see the environment as external and given, and believe that organizations need to adapt to contingent realities in order to survive (Grönroos, 1991; Sheth & Shah, 2003; Sharma & Pillai, 2003). The underlying assumption is that if a firm were culture-free and perfect information were possible then the organization could scan the relevant factors in the task and general environment and achieve (through changes in organizational structure and/or strategy) an optimal fit.

Alternatively, Prahalad (2004) recognizes the LIS fragile income condition yet concludes that the BOP, when considered from an aggregated point of view, represents a 'fortune'. Yunus (2007) looks at the LIS's lack of physical guarantees yet contemplates the LIS's social capital and collective responsibility as an alternative. Yunus (2010) also looks at low product knowledge yet concludes that LIS are able to consume consciously. These scholars advocate the *enacted environment approach*. They imply that a subjective environment exists; i.e., they see the environment as social construction (Berger &

Luckmann, 1967), allowing for creativity. The underlying assumption is that different environmental enactments result from various social constructions and images of the environment. In this way, the general environment is the infinite set of possible combinations an organization could envision, while the enacted environment is the combination of physical and social factors a given firm is actually considering.

In other words, the listing in the previous section and their interrelatedness can be considered either as a set of given constraints or a set of enacted opportunities.

## Future research and managerial implications

According to McInnis (2011, p. 145), summarization implications "identify knowledge gaps and lay out research priorities (Folkes, 1988; Rindfleisch & Heide, 1997)" and they may also develop managerial implications that pertain to the summarized findings (Gardner, 1985). The understanding of the EM-LIS characteristics has both academic and managerial implications.

In the academic field, this article highlights the EM-LIS characteristics and invites scholars to develop comparisons with HIC characterizations in order to analyse if traditional business models and theory that have embedded assumptions from HIC may be generalizable to this new context. Except for Burgess and Steenkamp (2006) comparison of institutional subsystems, no such studies have been found. This paper also introduced the concept of interrelatedness. However, the full implications of overlapping of characteristics have not been fully discussed or explored. The literature on collective impact (Kania & Kramer, 2011) might be useful to look at how to address complex multidimensional phenomena. Finally, a conceptual differentiation between primary and secondary characteristics has been suggested. The topic has only been introduced; further work on which characteristics pertain to the EM-LIS and which result from primary characteristics should be further studied. Moreover, clearer criteria should be developed.

In the managerial field, this article invites managers to review their market based approaches and strategies to the EM-LIS by consciously acknowledging their subjective or objective environment approaches. When addressing EM-LIS characteristics, managers that see EM-LIS as market constraints, will agree with the authors that argue that the absence of conditions that enable markets to function efficiently (Burgess & Steenkamp, 2006) make it difficult to apply current business practices (Gradl et al., 2008), leading to very high costs to serve this market (Karnani, 2011), and difficulties in reaching economies of scale (Bruni Celli et al., 2010). On the other hand, managers that see EM-LIS market as opportunities, will feel comfortable with the authors such as Prahalad (2010), who argues that there are 'biased assumptions' associated to EM-LIS. These managers will focus on the growth rates (Sheth, 2011), aggregated purchasing power of the LIS (Prahalad, 2004), social capital (Yunus, 2007), and show "how the 'impossible' can be made 'possible'" (Mashelkar, cited in Munshi 2009, p. xiv).

Finally, the core concept of bounded rationality (Simon, 1957) is particularly relevant to managers operating in EM-LIS environments. Managers rely on cognitive

maps to organize issues and events into manageable sets of categories; the challenge is to minimize the gap between flawed perceptions of these environments. This does not mean that there is an external objective environment; it implies recognizing that is difficult to achieve a perfectly rational decision.

This article has adopted and adapted the market environment theory classification and provided an EM-LIS characterization. In doing so, it has closed a conceptual and factual gap. Moreover, marketing knowledge has been further enriched as it has moved from a colonial mind-set to a global mind-set (Sheth, 2011).

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# APPENDIX I: Emerging Markets and LIS characteristics

| EMERGING MARKET AND LOW INCOME SECTOR CHARACTERISTICS | | |
|---|---|---|
| **General environ-ment** | Regulative system | • Legislation is missing or not enforced<br>• Moderate scores for shareholder rights and creditor rights<br>• Risk of appropriation or contract repudiation<br>• Poor judicial system efficiency<br>• Relevant red tape for all kind of business related procedures<br>• Different levels of corruption<br>• Existence of informal business links with organizations and people as well as informal labor |
| | Socio-economic system | • Demographic:<br> o Large family size<br> o Youth of EM populations<br> o Geographically disperse<br>• Diversity:<br> o Extreme socioeconomic variation within EM populations<br> o Different types of poverty<br> o Urban LIS different from Rural LIS<br> o Unemployment<br> o Gender and race discrimination<br>• Crowdedness<br>• Everyday violence<br>• Hyper-inflation, inflation, default<br>• Basic banking functions |
| | Socio-political govern-ance | • Socio-political institutions have enormous influence<br>• Markets governed by institutions and less by competition<br>• Numerous government-owned and -operated enterprises with monopolistic powers<br>• Dynamics, rapid socio-political change<br>• Political barriers |
| | Infrastruc-ture | • Poor or inadequate infrastructure: physical roads, logistics, storage<br>• Poor or unstable provision of electricity, running water, gas<br>• Poor or inadequate educational and health services<br>• Poor infrastructure to cope with natural events |
| | Techno-logy | • Lack of communication, information, and transaction technologies<br>• Lack of data transfer networks |
| | Cultural system | • Cultural embeddedness and hierarchy<br>• Maintenance of the status quo and discouraged behaviors that disrupt in-group solidarity<br>• Autocratic decision making |

| Task environment | Con-sumers | • Knowledge and skills:<br>  o School dropout and low child enrolment<br>  o Illiteracy<br>  o Low formal education<br>  o Low technical skills<br>  o Low product knowledge |
|---|---|---|
| | | • Income:<br>  o Low income<br>  o No consistent income<br>  o Lack of access to financial products and services.<br>  o No commercial insurance |
| | | • Household:<br>  o Lack of storing space<br>  o Informal settlements |
| | Suppliers/producers | • Chronic shortage of resources in production<br>• Lack of managerial capabilities by local community groups |
| | Distri-bution | • Traditional mom and pop stores<br>• Inefficient distribution networks, especially in rural areas<br>• Lack of market intermediaries to consolidate or distribute information<br>• Patronage of retail outlets |
| | Com-petitors | • Consumption for unbranded products and services<br>• Mostly small enterprises<br>• Household as production unit: availability of labor at home: women and children<br>• Many branded products and services are not available in rural markets<br>• Prevalence of used products as direct competitors<br>• Prevalence of barter exchange or reciprocal offerings |