The Inclusive Business Market in the Philippines
Summary of an ADB study,
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1 BACKGROUND

1. Improving environment for inclusive growth: The financial markets have given the Philippines their most positive assessment for a long time due to marked improvements in the macroeconomic and fiscal situation of the country. The government addresses concerns on governance and competitiveness and thereby contributes to improving the country’s image as an investment opportunity. Although the government has embraced the mantra of “inclusive growth”, it has not yet led to a marked improvement in the reduction of poverty by more job generation and better services delivery to the poor and low income people. In fact poverty in the Philippines remains high at 27.8% of the national poverty line, and up to 63% living on less than $3 a day. Inclusive Business (IB) offers an opportunity for the private sector to contribute towards inclusive growth, and to create new commercial value.

2. Inclusive Business (IB) is generally defined as:
   - commercially viable and profit making private companies in the growth stage,
   - whose core business is designed to address – in scale – pressing social needs of the poor and vulnerable people below the $3 international poverty line (i.e. ca. 60% of the Philippines population, also referred to as the Base of the Pyramid (BoP),
   - by engaging them through the provision of affordable and relevant goods and services and through income and decent work opportunities, in a manner that results in measurable improvements of their living situation and as a
   - systemic contribution to poverty reduction and inclusiveness for the country/region.

3. IB differs from corporate social responsibility (CSR), social enterprise, impact investments, microfinance, and contract farming through its business scale, growth potential, and focus on systemic changes for poor people. Companies adopt inclusive business primarily to create shared value, increase sales, enhance company reputation and develop the ability to maintain a stable supply of inputs.

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2 KEY FINDINGS OF THE PHILIPPINES IB COUNTRY STUDY

4. **IB Market scoping study**: In 2011 ADB commissioned the Asian Social Enterprise Incubator (ASEI) to prepare a study on the market potential of inclusive business in the Philippines. This study was part of a series of studies on the inclusive business potential in Asia.\(^2\) Completed in May 2013, the initial findings of the study were presented at the 1st Inclusive Business Forum held in November 2012 in ADB. The study showed that inclusive business and impact investment are very nascent concepts in the Philippines. More specifically, the business, finance, and donor community showed low awareness of these concepts, little investments, and few innovative business models. Hence there is a need to strengthen the enabling eco-system for inclusive business.\(^3\)

5. **Many Social Enterprises but only few Inclusive Businesses**. The study identified a total of 70 companies with inclusive business models in the Philippines in 11 industries, of which only a few (maybe 15) would be currently bankable. They engage the people at the base of the income pyramid (BoP) mainly as a consumer, supplier and distributor. This compares to a potential of estimated 30,000 social enterprises as identified by Ateneo de Manila University for an ADB study\(^4\), and over 300,000 NGOs and community organizations active in the Philippines. As mentioned above, inclusive business approach differs from these activities in terms of scale of impact, financial return, and investment size. In the Philippines, the social enterprise space consists mainly of two groups: (a) a large number of cooperatives with a potential to develop into for profit businesses, and (b) a smaller group of start-up companies with a dedicated social impact and financial return vision. These have a potential to develop into inclusive business once they reach a critical scale and achieve sustainability.

6. **IB are concentrated in a few sectors**: IB companies in the agricultural sector (24%) make up the largest share of inclusive business sector in the Philippines, followed by IB companies in the financial services sector (14%) and IB in the manufacturing sector (10%). Combined, they comprise over 50% of IB sector in the country. IB companies in others sectors (IT, energy, education, health, and transport and logistics) are fewer but exhibit profitable and impactful inclusive business models.

7. **The need to improve the internal governance of IB companies**: One of the main concerns for both investors and IB companies’ managements is related to internal governance problems that hinder growth, such as weak financial statements and weak compliance with corporate reporting requirements. Pre- and post-investment support for IB companies and business training of lower medium management staff and the awareness-raising among the companies leaderships are essential.

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8. **Issues with public governance is another reason for international companies not to enter the market:** There is a wide-spread perception of the Philippines as a country that tends to change the rules of the game midway. Graft and corruption within government in past has been widely acknowledged, and small scale companies (most IBs are small and medium enterprises) are particularly exposed to local corruption. As a result, much of the Philippines business community has geared its reporting towards “tax avoidance”. This environment however, affects particularly also the IB companies which will then have problems in exposing in a transparent way their financial status and hence, may be sidelined by investors and banks.

9. **Finance is a barrier to the growth of inclusive business.** Apart from the poor regulatory environment (including corruption and fraud at local levels), little alignment with government support programs for the public sector, and the lack of government incentives, access to capital is a major challenge for IBs. While smaller companies face strong impediments to access debt and equity capital at reasonable interest rates, larger companies do not have such concerns. Philippines investment funds catering the needs of IBs are not existent, but a few selected international fund managers are slowly entering the market. Especially banks and other financial institutions are found to be reluctant to invest in IBs given the smaller size of loans, the perceived risks and risk-averse incentive structure, the low level of innovation for IB appropriate financial products, and the regulatory stipulation such as minimum collateral requirements for investing in small and medium enterprises (SMEs). These hinder adequate capital to be invested in inclusive business.

10. **The need for innovative IB financing:** During the last three years, only two (2) dedicated impact investments with a total of USD 3 million were undertaken in the Philippines. In addition, IFC invested USD 75 million in Manila Water from 2003 to 2005. The study observed a low level of awareness of impact investment among the commercial banks and funds. Also, the independent private equity (PE) market in the Philippines has limited number of participants and there is little, if at all, awareness of IB opportunities in the financial sector. The financial sector also finds the regulatory environment as a major concern for IB investments. The study found a strong reluctance of the financial sector to invest in smaller IB deals due to perceived risks and unfamiliarity. It found that further training of banking staff on IBs, and risk guarantee facilities, as well as examples of anchor investors (like ADB or IFC) would render the financial institutions more inclusive.

11. **Through IB, the government could realize its agenda on inclusive growth:** IB in the Philippines can be adopted to realize the government’s inclusive growth goals, such as creating more employment for the poor in specific geographical areas, and providing better services – especially in housing, health, energy and education. The successful business models in the various sectors can be developed to serve as role models in each industry. For example, Jollibee Corp. actively promotes its IB model and encourages other industry players to join the program. The Philippine Business for Social Progress (PBSP) and the League of Corporate Foundations (LCF) also joined efforts to promote IB as the path towards inclusive growth aiming to expand the reach of IB beyond the few sectors and examples cited in the study.
3 IB POTENTIALS IN KEY SECTORS OF THE PHILIPPINES

12. The following discuss and illustrate the dynamics of IB activities in each industry studied in the Philippines.

3.1 IB for job generation

13. The agriculture/agribusiness sector yielded the highest number of IB companies. This corresponds with the high prevalence of poverty in the rural areas of the country, and the importance of agribusiness to the economy as almost one third of the population is engaged in this sector. Most IB companies in the agribusiness sector source products from small scale farmers (less than 2 ha of land ownership) and fishermen. The products are purchased at a fair price under a contract growing or other procurement arrangements, such as farm gate purchasing. Additionally, technical capacity building and financial assistance are extended to the farmers to meet the yield and quality requirements of the company. IB business models with growth potential in agribusiness were found (1) in higher value markets, such as vegetable and organic produce; (2) with products for which yield issues do not exist or can be overcome, such as coffee, seaweed and seafood; and (3) with companies which are willing to extend financing to the small farmers. This sector is particularly important for job creation for the poor. It will however have only systemic impact if the companies’ business models can be expanded in regions of strategic importance such as Mindanao for peace and poverty reduction, and if the business models allow long term relation building for new income generation and growth. To have stronger impact and scaling up job creation and poverty reduction, the government and the agrobusiness sector could agree on further concentrating their investments in Mindanao. While the study was not comprehensive and many more agrobusiness investments could perhaps be found, good examples for IB business in this sector are:

- **Coffee for Peace** - reaching 15,000 indigenous households in Mindanao;
- **MCPI** - potential to expand seaweed farming from 7,000 to 20,000 fisherfolks in the Visayas; and
- Coco Technologies – expand sourcing from and training of farmers for the production of coco fiber from 2,000 to 6,000 small coconut farmers.

14. **IB in the food and beverage sector**: The food and beverage sector form an important part of the Philippine economy contributing more than 10% of GDP and growing at more than 4% p.a. The study observed good but not widespread examples of sourcing of raw materials from small farmers in the industry. Well known examples are:

- **Jollibee** – upscaling of Farmer Entrepreneurship Program from 700 to 8,000 small farmer;
- **Nestle** – propagates shared value as the way they do business. In 2012, they engaged 5,000 families from the BoP and they expect the number to rise to 70,000 families by 2016. Nestle’s IB activities would be particularly important for creating new employment, if they could be focused on Mindanao;
Another example is **Kennemer Foods**, an international company sourcing cacao from poor farmers in Mindanao, linked to the programs of the Department of Agrarian Reform (DAR) and the Department of Agriculture (DA).

15. **IB in the finance sector**: The second largest group of companies among the Philippine inclusive businesses is the financial sector with 14% of IB companies. While the study excluded pure micro-credit institutions, it found several examples of MFIs which have expanded under the concept of microfinance plus into micro savings, micro leasing and micro insurance providing the BoP with access to those additional financial products. Also, the large remittance business sector has increased its offering towards new services and bringing its services closer to the customers. Commercial banks were found which have developed products for micro and small entrepreneurs further increasing access to finance. Examples are

- **Climbs** – expanding affordable life and non-life insurance products with fast claim processing from 1 million to 1.7 million customers; and
- **Globe BanKO**, an affiliate of the Ayala Group – expanding mobile based microfinance products including savings and payroll services to 1 million clients.

16. **IB in the manufacturing sector**: Consistent with the high un- and underemployment situation in the country the BoP as employee mode of engagement is the least developed concept among the four modes of engagement. Increasingly, manufacturers in the Philippines have been engaging the use of outsourced labor to avoid the restrictive labor laws. Such firms would barely count as IBs, because IB companies typically follow good labor practices. However there are examples of firms which employ the BoP with all statutory rights, and which pay wages above the minimum wage level and offer training to its employees. Nevertheless, BoP as supplier is the more promising IB approach for manufacturing in the Philippines. Companies from the furniture and handicraft industry in Cebu, for example, have developed profitable and scalable models. The linkage of community-based sourcing of natural materials from the rural areas with either factory-based or outsourced home production is a model that can be both profitable and impact creating (through employment and income for the poor) at the same time. Examples from the Philippines are:

- **All Home Design** – expand sub-contracting basket weaving activities from 580 to 2,200 producers (families); and
- **Gandang Kalikasan** – potential to expand sourcing for Human Nature cosmetic products from 500 to 40,000 farmers;

17. **IB in the retail sector**: Retailers have developed programs to engage over 700,000 informal convenient stores in the Philippines called sari-sari stores, which are mostly run by women from inside their houses or small establishments. These programs offer a mix of lower prices, promotional activities, financing, training and extension of the product range to BoP-specific products, such as dengue-protection sachets and solar lights. The other mode in which the retail sector engages the BoP is as a supplier of produce. Supermarkets with inclusive business activities purchase from small-scale farmers which are located near the store at fair prices which ensures fresh produce for their customers. The direct purchase offers a competitive advantage in terms of freshness and availability on the supermarket shelf. Another
business model observed is based on microfranchising – enabling entrepreneurial livelihood through a systematic franchise offering by the inclusive business, which has the additional effect of developing a last mile distribution channel into the BoP. Examples are:

- **MicroVentures, Inc. (MVI)** manages the Hapinoy Program, a social enterprise with the potential to reach 100,000 sari-sari (mini) stores, thus upscaling to become an inclusive business.

- **Julie’s Bakeshop** – potential to reach 12,500 micro franchisers by 2016 with small kiosk bakeshop concept.

18. **IB in the tourism sector**: The tourism companies identified in the study are either engaged in rural eco-tourism or source souvenir items from low-income households. The integrated community development in the rural tourism models starts by engaging the BoP as tour guides. The tours also empower communities to provide services and products, such as bed and breakfast, food, and others to the tourists. Although tourism has a huge potential in terms of growth and job generation in the rural areas, not many IB companies could be found. This is mainly because very few companies have the potential to scale up beyond 1 or 2 individual island resorts thus not achieving the scale criteria of IB. One example with potential is:

- **Islands Banka Cruises** – potential to expand program to employ or sub-contract tourism workers as small boat operators or as supplier for souvenir items from 40 to 4,000 families.

3.2 **IB for provision of services to the poor**

19. **IB in the energy sector**: The modes of engagements in the energy sector are split between BoP as consumer and BoP as supplier. Companies providing solar home systems and other distributed energy as a first step of electrification though are finding it difficult to develop profitable business models as the distribution, since after-sales service and competition from government or ODA-funded activities stifle the industry. To give a few examples:

- **The PowerSource Group**, the country’s first “Qualified Third Party” power provider and distributor, has pioneered the development of mini grid to electrify remote regions and islands. In addition to providing reliable power 24/7 and thereby enabling economic development on their sites, the PowerSource Group also actively engages in community development by supporting entrepreneurs in setting up small businesses.

- The BoP as supplier mode of engagement in the energy sector can be found in the biomass sector which requires substantial quantities of raw material which can be sourced from small scale farmers, as practiced by SURE. Due to the large amount of natural raw materials needed for a commercial biomass plant, one plant engages at least 8,000 farmers.

20. **IB in the health sector**: Pharmaceutical companies, pharmacies and medical service businesses engage the BoP as consumers. The emergence of pharmacies specializing in the distribution of generic medicine and their rapid growth through franchising started about five years ago. Since then medicine has become more affordable, however it has still not reached
the low price points seen in other Asian countries. Inclusive health care services could be observed in the specialized health care sector such as vaccination and maternal health. Good examples are:

- **Generika Drugstores** provide - with own and franchised pharmacies - access to low-cost, generic medicine as well as diagnostic health education/services to the BoP reaching 3 million customers

- **Family Vaccine Specialty Clinics (FVSC)** located in 41 rural hospitals nationwide, provide non-mandatory vaccination services, such as rabies vaccine to over 40,000 rural clients.

21. **IB in the IT sector:** The majority of the IB models in the IT industry utilize the BoP as consumer model. The study identified business models in the internet café, mobile communication and finance services sectors. Good examples are:

- The success of **Smart Communications** and **Globe** in bringing mobile communication to the BoP through prepaid e-loading is well-documented. Moreover, both networks also started microfinance mobile banking operations.

- Another example of an inclusive business model utilizing technology to increase access to finance is **Encash** which deploys ATMs in rural areas not deemed viable by commercial banks, allowing users in remote locations to conveniently obtain access to cash.

22. **IB in the education sector:** As in the health sector, primary and secondary education is dominated by the public sector. The private sector is only active in this sector through charitable activities and very recently public private partnerships in building schools. Inclusive business activities in the education sector could be observed from tertiary private schools either in the form of introducing student loan programs to reduce the initial cost of the studies, the establishment of schools in areas where there is no educational facility present and the takeover of badly performing private schools. Vocational and short term training courses is another area in which educational institutions reach the BoP. Examples are:

- **STI** is the biggest college network that focuses on providing education service to the low-income sector by offering 2-year Technical Education and Skills Development Authority (TESDA)-accredited technical courses and regular 4-year degrees

- **Phinma Education Network** has brought extensive faculty and course improvement to its universities and colleges now serving 45,000 students achieving dramatically higher passing rates in professional exams

23. **IB in the urban sector:** Again, as in education and health, the public sector is the primary player in mass or socialized housing, as the housing for the poor market is called in the Philippines. In the recent years, however, real estate developers have started projects aiming at the mass housing market either as a private development or in public private partnerships. However, the lack of an eco system, such as micro mortgage schemes, the high cost of land in the metropolitan areas, regulatory and land title issues, among other barriers, have so far hindered the scaling up of inclusive housing business models. A good example is:
Phinma Properties’ Bisteckville II housing development, the first inner city relocation PPP project with the Quezon City government which could provide a blueprint for the industry.

Clean Engines is a new IB company in the urban transport sector, providing retrofit kits for two stroke engines to reduce smoke emissions and reduce fuel costs thereby increasing the income opportunities of poor three-wheeler taxi drivers in metro Manila.

4 SOCIAL IMPACT ASSESSMENT

24. **Why impact assessment:** Inclusive business projects are increasingly becoming relevant for companies and investors not only for doing business well, but also for doing good things in business. At the same time, the government and development partners are increasingly looking to the private sector to provide the jobs and services needed for a more inclusive economy and society in the Philippines. However to design fully effective projects according to the needs of the poor and to maximize the social impact in scale, ex-ante impact assessments are necessary for both the company as well as the government. Such assessments clarify not only beneficiaries (reach) and change (depth), but also the direct and indirect impact channels in its systemic contribution to address root causes of poverty and deprivation. Ex-ante impact assessment is therefore also an essential component of ADB’s inclusive business work.

25. **Self-rating methodology:** At its first IB Forum in November 2013, ADB asked the participating companies to do a self-rating of their financial and social impact. To this end, ADB and ASEI developed a simple “IB Impact Assessment” methodology specifically targeted to markets in the Philippines. The toll was slightly refined and will be used by companies attending the 2nd IB Forum. Inclusiveness of companies is determined through evaluating their commercial and social impact in terms of:

- **Profitability and returns** refers to a company’s financial performance and was measured based on the companies’ internal rate of return (IRR). This includes:
  - Investment scale and cost structure
  - Financial performance
  - Growth potential of the IB model, including scalability and replicability

- **The social impact** is assessed based on:
  - **Reach** refers to the extent to which the business model is engaging the BoP population. The measure depends on the business model: if supplier or distributor

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5 As this is the first effort in the country, we expect this methodology to be developed and improved over time. ADB has also prepared an overview of the IB impact assessment methodologies globally, and developed a tool to measure impact of IB companies in Asia. The tool will be further refined, and harmonized with other impact investors. For more information on see: [http://www.adb.org/themes/poverty/inclusive-business-base-pyramid/impact-assessment](http://www.adb.org/themes/poverty/inclusive-business-base-pyramid/impact-assessment).

model, by households affected; if employee model, the number of employees hired; if consumer model, number of clients per year.

- **Depth of impact on systemic poverty reduction and contribution to inclusive growth**, measured by income increase per household, labor relations, stability of income, share in company's profit, others (IB supplier model); income increase per household, payment and commercial relations, relevance of product for reducing poverty and improving standards of living (IB distributor model); income increase per individual, labor relations, stability of income and job, share in company's profit, others (IB employee model); and in clients per year, relevance of product, pricing for the BoP, payment relations, supply of products, ability to pay, others (IB consumer model).

- **Systemic impact** identifies the relevance and scale of the IB model (and its location) for the poverty reduction and inclusive growth root causes of a country. For example, if a company like Nestle wants to upscale the sourcing of coffee from 5,000 farmers to 70,000 farmers, its impact may be so much higher if it could concentrate the job creation for example in an area of Mindanao where income generation for the poor is of such high strategic importance for the country and hence systemic value.

- The assessment also includes a review of:
  - the **sustainability** of the investment decision, and
  - the **innovativeness** of the IB model, and its investment components

5  **THE IB SUPPORT STRUCTURE IN THE PHILIPPINES**

26. **Business associations have a key role in making the concept of IB more public:** The study found that many companies in the Philippines either (a) confuse IB with corporate social responsibility activities, or (b) with social enterprises without growth potential as part of their immediate business plan, or (c) are little interested in creating shared value for the society and the poor. Hence, business associations could therefore play a major role in making the concept of IB more known, promote knowledge sharing, and help facilitating investment potentials through interacting with governments, the financial sector and the business sector.

- The **Inclusive Business Imperative**, a joint initiative of major business associations (i.e. the PBSP, the LCF, the Makati Business Club, and the Management Association of the Philippines (MAP) is an example of a major commitment to move the IB agenda in the country. PBSP, the business association of the 250 larger firms in the country, set a good example when it made IB – in January 2013 – part of its 3-year work program, and committed itself to become the main support platform for business-government interaction on IB.

- **IB-Hub in PBSP**: PBSP has been a partner of the ADB IB study and the 1st IB Forum. In 2013, PBSP choose IB as its main working theme for the coming years. It is in the process of setting up an IB center to promote IB among and beyond its membership through consulting, knowledge dissemination, workshops and other eco system building
activities. This IB Hub will also serve as the counter part to the government’s IB structures.

- In addition, corporate social responsibility programs of companies and foundations could be better aligned with the IB agenda. The **League of Corporate Foundations (LCF)** has already made inclusive growth a theme this year. LCF could facilitate the paradigm shift of company foundations committing resources on their own company IB efforts to leverage company assets and increase measureable impact manifold as well as assure sustainability through profitable or cost saving IB business models.

27. **Inclusive Business Task Force of the Government:** The Government of the Philippines has embraced inclusive growth as the overriding theme of all actions. This was recently expressed in the State of the Nation Address (SONA, July 2013) of President Benigno Aquino III to create jobs, income and access to goods and services at the BoP by allocating budget, align expenditures with IB activities and establish targets and measurements. To achieve this, the Administration is in the process to develop an inclusive business task force under the Budget Secretary (Department of Budget and Management, DBM), with support from key departments such as National Economic and Development Authority (NEDA), Department of Trade and Industry (DTI), DAR, DA, Department of Health (DOH), and Department of Education (DepEd). In addition, the government is considering an IB secretariat that could directly interact with PBSP’s **IB Imperative**, to (a) develop relevant IB support policies, (b) programs and financing tools, and (c) serve as one-stop window for solving concrete problems of companies with government bureaucracies. Of particular importance is the setting of targets for IB’s share in the delivery of services (for example, in the 100,000 low cost housing program of the government for Manila’s slum population), and the planning of large-scale sustainable income creation for the poor in specific regions beyond livelihoods (as in the case of job creation for Mindanao’s poor).

28. **Legislators**, such as Senator Paolo Benigno “Bam” Aquino, are increasingly developing legislation to strengthen the role of social enterprises and inclusive businesses in contributing to inclusive growth, for example with the submission of the Social Enterprise Bill.

29. **Development partners** like CIDA (Canada), the European Commission, AusAID (Australia), USAID (USA), ADB, and IFC (World Bank) showed interest in coordinating their private sector efforts and aligning their PPP, trade, infrastructure, and business environment programs more under the inclusive business heading. ADB is currently finalizing a regional technical assistance program for IB support, which will also benefit the Philippines, and some of the above mentioned development partners are considering co-financing this initiative. Other development partners such as the Spanish development organization (CODESPA) and the German international cooperation agency (GIZ) are developing their own IB programs in specific regions.
6 LOOKING AHEAD

30. **IB is a promising concept in the Philippines.** For it to mature and develop its full potential, an enabling eco-system has to be built involving all stakeholders. 2013 has already seen a marked increase in IB related activities such as two PBSP fora, LCF’S CSR Expo and special press conference, Jollibee’s Farmer Entrepreneurship Program (FEP) seminar and now the 2nd ADB IB Forum. Companies increasingly see societal problems as business opportunities to achieve growth by integrating the low income population in their core business activities. The positive examples in the various sectors illustrate that financial return and social impact can be achieved by engaging the BoP as supplier, distributor, employee and customer. Larger companies, such as Jollibee, Nestle and Manila Water, have started to promote their IB models to other businesses in the industry to strengthen an emerging supply chain.

31. **Challenges ahead:** However to reach its full potential:
- The concept of IB in the Philippines needs to be made more known to more companies to see the business opportunities of IB. Some companies also need help in developing sufficiently profitable and impact oriented business models.
- The government would need to develop a more conducive eco-system for IB, including setting of clear targets what a societal private sector can deliver terms of jobs and services for the poor, thereby helping to make growth more inclusive.
- The financial sector needs to be educated that inclusive business investments often have higher returns (and less corruption) than traditional investments. New financial instruments could be developed, such as a credit guarantee facility for IB interested banks. The guarantee facility could be sourced jointly from CSR funding from foundations, government, and development partners/development banks.

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7 The historical investment of the Ayala Group in Manila Water is seen worldwide as one of the biggest success stories for inclusive business. After the privatization of the water distribution system in Metro Manila in 1999, Manila Water focused on expanding the access of safe water to the slum areas of Eastern Manila. The group invested about $475 million and achieved coverage of 98% of the population (up from 26% in 1999) for today about 0.9 million households (or 5 million people) – more than 50% of them poor – with 24 hours access to quality water at fair prices. Manila Water is also a highly profitable business, and the company has turned around from a loss of $1 million in 1999 to net income of $49 million every year since 2006 after tax.