



A REPORT BY **HARVARD BUSINESS REVIEW ANALYTIC SERVICES**

# Business Model Innovation in Emerging Markets: New Opportunities and Challenges

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# New products and technologies are not the only game changers.

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## Executive Report

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**NEW INVENTIONS AND “DISRUPTIVE”** technological innovations get much of the attention: smartphones, tablet computers, iPods — these are the glamorous supermodels of business innovation. But in many cases it is the business models with which companies operate that are the “game changers,” not technology.

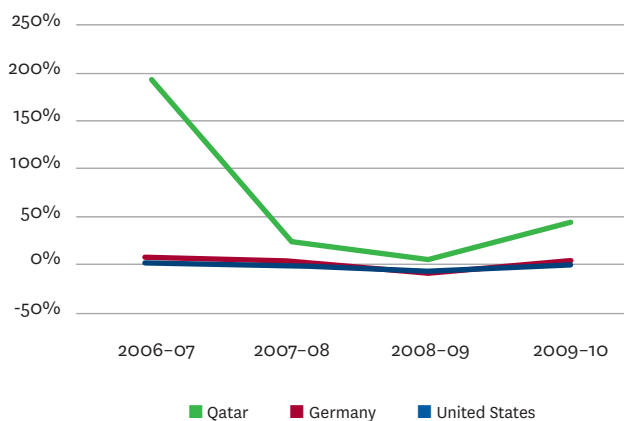
This is especially true in emerging markets. It’s naive to assume that what works, either as a product or a business model, in a developed country will work just as well in emerging markets. Several large U.S. retailers learned the hard way that just transplanting their domestic concepts to overseas emerging markets quite often fails.

Nevertheless, emerging markets offer irresistible growth when developed economies have stalled. For example, per capita income in Qatar is growing at exponential rates compared with income in more mature economies — see figure 1.

## Growth Imperative

It is no surprise that thousands of multinational companies have set up ventures in emerging markets to capture additional revenues, satisfy investors’ expectations for strong annual growth in earnings, and help their growing middle class populations achieve their aspirations. Western multi-

**Per capita income growth: U.S., Germany, and Qatar** figure 1



Source: CIA World Factbook

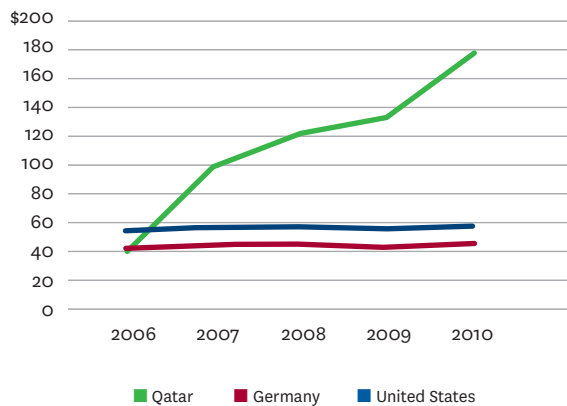
nationals expect to find 70 percent of their growth in these developing economies, according to the article “New Business Models in Emerging Markets” by Matthew Eyring, Mark Johnson, and Hari Nair in the January-February 2011 issue of *Harvard Business Review*.

In emerging markets, developing a new and innovative business model often is far more important to achieving revenue goals than is technological superiority or being a technological innovator.

“Technology product companies have tried to replicate what worked in mature markets and have found that the same success cannot be achieved,” notes Sanjiv Rastogi, president of CloudBridge, LLC, a Chandler, Arizona-based management consulting company that specializes in global expansion and improving marketing effectiveness in emerging markets. Rastogi has more than 20 years of experience at various technology companies, including Microsoft.

### Per capita income: U.S., Germany, and Qatar figure 2

U.S. dollar or equivalent, in thousands of dollars



Source: CIA World Factbook

There are a number of reasons why new and different business approaches are necessary in emerging markets:

- The different sensibilities of the local customers;
- The different sorts of firms that may predominate there;
- Immature distribution channels for consumer products;
- Fragile utility infrastructure; and
- The challenge and opportunity of taking advantage of what is abundant and cheap in the emerging market, such as labor, but high priced in a mature market.

See figure 3 for a sampling of the business model challenges in emerging markets compared to those of developed countries.

## Emerging market business model challenges figure 3

Challenge	Emerging Market Paradigm	Developed Economy Paradigm
Utility infrastructure	Water, electricity, telecommunication, and sanitation systems are either unreliable or a work in progress and may be expensive	Usually reliable and an afterthought by multinational companies—they assume these systems are functional
Transportation infrastructure	Carts, motorcycles, and bicycles may be more prevalent than tractor trailers. Highways and more robust rail lines are works in progress.	Again, multinationals assume the transportation infrastructure is in place and is adequate
Distribution infrastructure	Numerous small retailers and multiple layers of wholesalers usually create inefficiencies and delays	Fully developed and usually efficient
Customer sensibility	Sometimes low cost is more important than value	Value sometimes more important than cost
Labor costs	Low hourly costs provide manufacturing opportunity but market challenge	High hourly costs provide manufacturing challenge but market opportunity

Source: Harvard Business Review Analytic Services

However, the economy of Qatar, because of its wealth from natural gas and oil (2010 Gross Domestic Product per capita = \$179,000, the highest in the world), is an exhilarating clean slate for development. Indeed, the country's leaders have been selective about its economic development. Some aspects of its deliberate development policy already are bearing fruit.

For example, Qatar sought to lure top universities from around the world to set up satellite campuses. To date Qatar has attracted a number of them, such as Carnegie Mellon, Weill Cornell Medical College, HEC (Hautes Etudes Commerciales), and Imperial College London. Education is fundamental to economic development, and Qatar appears to have reached critical mass. It is becoming a magnet for education in the region.

## Dual Agenda

Qatar has a dual agenda for economic development: to diversify the economy beyond exploiting hydrocarbons and to play a larger role in international affairs. "The country has the luxury to pick the projects it wants," says Nabih Maroun, a partner at Booz & Company who is based in Doha, Qatar, "and it is free of some of the constraints on bigger Arab nations."

Much of Qatar's domestic investment is in infrastructure, but the country has encouraged experimentation in business models in sectors as diverse as education, health care, and telecommunications. Here are a few noteworthy examples.

### KID LIT

A successful business model in an emerging market typically takes into consideration these challenges and also sees opportunity. Consider Araboh.com, an online retailer of Arab-language books, CDs, and DVDs for an Arab-focused clientele. Araboh.com sells to customers all over the world. At first glance Araboh.com's business model appears substantially similar to that of Amazon.com.

However, Araboh.com differs from Amazon.com in that it has tailored its business model to cater to Arab sensibilities. It reads and vets every book it sells. Araboh.com has only 1,500 titles and its list is growing slowly. But Arab customers, and especially those who are Muslim, must eschew any books that would violate their more strict standards of decency in reading materials. Araboh.com enables them to buy with confidence that whatever they buy online will be appropriate.

Being an online retailer, Araboh.com straddles both developed and emerging markets. Although now most of its sales are to customers in the United States, the business model it follows in selling in the Middle East is what distinguishes it. It is the only online retailer of Arabic literature that focuses on children’s literature — other Arabic online retailers emphasize religious merchandise. Araboh.com is secular. Its selectivity in prescreening merchandise is an especially important service for those buying books to read to children or that will be read by children.

“Our selection process is really what makes us stand out,” says Jinanne Tabra, Araboh.com’s 26-year-old founder. “Working in an emerging market like the Middle East, we’re not religiously focused. But we have to keep those sensibilities in mind so as not to alienate our customers.”

Another business model difference: for its customers in the Middle East, Araboh.com does much more outreach. According to Tabra, there is a shortage of good modern Arabic literature, especially children’s literature, in schools and libraries. The Middle East, especially the United Arab Emirates and Qatar, are very Western-focused. Western literature and culture have pushed offstage much of the Arabic culture and literature. Araboh.com is devoted to helping bring that literature and culture back to the Middle East.

The company hosts reading festivals, week-long events at schools and libraries, competitions in Arabic reading or writing, and book fairs once or twice a year at schools. It has an ongoing initiative with various local school organizations to sponsor and encourage an Arabic awakening. “Our merchandise can compete with the best educational materials out there,” says Tabra. Araboh.com also offers free content online: reading guides for parents, suggestions about children’s activities pertaining to the books, and teachers’ guides. See figure 4 for examples of Araboh.com’s innovative business model.

**Innovative business model — Araboh.com** figure 4

Key Tactic	Developed Economy Approach	Developing Economy Approach
Community outreach	Online marketing	Reading festivals, school and library events, contests, book fairs
Evaluate product	Rarely done	Intensive review for appropriateness
Inventory	As broad as possible	Highly selective and focused
Attitude toward clients	Buyer beware	Buy with confidence
Cultural engagement	Provide fine product to elicit sales; little sense of responsibility to cultures of developed markets	Strive to promote awareness of the Arabic culture of the emerging markets

**BIG PIPE**

On a much grander scale is a business model that is not only innovative but also completely unprecedented for the Middle East: Gulf Bridge International (GBI), a venture that will connect the Middle East and India with Europe via an 8,125-mile undersea fiber optic cable.

This is a high-capacity pipe, built to handle a lot of traffic. When completed, some sections will offer a transmission speed of 10 terabits per second, or roughly 100 times the speed of a typical corporate network. This new service has roughly 20 times the carrying capacity of the biggest broadband technology currently serving the Middle East.

In an age of satellite communications, why lay cable? Two important reasons. According to Rashid Al Naimi, chairman of GBI and vice president of administration of the Qatar Foundation for Education, Science, and Community Development (QF), one of the founding investors, satellites reach only around 18 percent of the world’s surface. More importantly, satellites cannot carry the quantity of transmission traffic at the speeds that telecoms and Internet service providers envision needing. Nowadays undersea cables still carry 85 percent of the world’s digital traffic.

In the past, undersea cable ventures have been structured as consortia of telecommunications carriers. The cable was a utility serving the purposes of the carriers of the consortia that owned it.

GBI has taken an independent and entirely regional approach. The venture has been set up as a pure connectivity initiative by investors, not telecommunications carriers. They see a huge opportunity — the broadband infrastructure demands of the Middle East are doubling every year. GBI is planning to service that capacity hunger with a cable network that is carrier agnostic. It will serve all operators in the region but not be a captive service provider of any one.

GBI will be wholesaling its transmission capacity to all telecom companies and Internet service providers and pursuing its own regional development objectives. GBI has built the highway, but it thinks that the future of the Middle East as a strategic business hub will be best served if no one else gets to put a toll booth on its twenty-first century network. See figure 5 for more details about GBI’s innovative business model.

“Our decisions will not be driven by the interests of one telecommunications operator,” says Ahmed Mekky, GBI’s CEO. “They will all be our customers, but it’s a region-wide utility for all and a catalyst for the economic interests of the entire region.”

Mekky regards the \$445 million project as a private equity–owned firm. All the financing has come from a group of investment authorities owned by the Gulf state governments such as QF, the Qatar Investment Authority, and the Kuwait Investment Authority, and some investors are directors. But the firm is private in that no single country or investor has voting control.

GBI already has lined up customers in the Middle East. Araboh.com, based in Dubai, soon may be receiving and fulfilling orders throughout the world by getting data through GBI’s cable.

### **Innovative business model — GBI** figure 5

<b>Key Tactic</b>	<b>Developed Economy Approach</b>	<b>Developing Economy Approach</b>
Investors	Customers	Government investment arms
Capacity	Small increment above current need	Plan for long-term future
Business goal	Profitability and return on investment	Accelerate regional growth
Controlling interest	One or more major telecommunications carriers	No carriers in the region have control of the venture
Vision of infrastructure	Serve certain carriers as captive utility	Serve all carriers impartially as valued customers

## ADAPTATION AS ART FORM

It might seem like an axiom of expanding to emerging markets that a firm needs to adapt to the local culture and prevailing business practices. Yet often companies entering emerging markets don't do that. One of the customary mistakes companies make when they enter an emerging market is they don't take a holistic view of the value structure, either of customers or of the overall culture.

"Emerging markets often require business models that have a much broader scope," says Josh Suskewicz, a principal at Innosight LLC, a management consulting company in Lexington, Mass., founded by famous Harvard Business School professor and best-selling author Clayton Christensen. "You need to address the whole ecosystem that surrounds your offering."

A company that seems to have made a virtue of adapting and catering to the needs of its emerging market is Virgin Health Bank's venture in Qatar. Virgin Health Bank QSTP-LLC, a for-profit British firm, collects, processes, stores, and supplies units of stem cells derived from umbilical cord blood that have been donated by parents. It is a part of the global Virgin airline, telecom, and book conglomerate launched by British entrepreneur Richard Branson.

Cord blood stem-cell units can play a clinically useful role in the treatment of certain types of leukemia and lymphoma, or blood disorders such as sickle cell anemia and beta thalassemia. In the future they also may serve as the basis for regenerative medical treatments for conditions such as diabetes and heart disease, among others.

Yet in setting up a business in the Middle East, Virgin Health Bank was moving to a location in which public awareness of stem-cell medicine and its benefits was virtually nonexistent. To give you a sense of the non-awareness, there are over 19 million registered stem-cell donors on the Bone Marrow Donors Worldwide registry, which is a global registry of bone marrow donors and donated cord blood units. Only 45 of those units are from the Middle East, which means that the Arab community is significantly under-represented on the registry and that physicians requiring stem-cell units for Arab patients find it very difficult to get them.

In Qatar, Virgin Health Bank would have to create both the supply and the demand. It could not rely on the sort of widespread understanding that exists in markets such as the United States. That meant educating not only the public in Qatar, but also the government regulators and the medical community.

In setting up a branch in Qatar, Virgin Health Bank went from operating in a secular society to a very religious one. "People live their lives according to the tenets of the Islamic faith," says Andrew Glen, the commercial director of Virgin Health Bank. "That context is crucial for the Muslim community."

At the outset Virgin Health Bank consulted with a widely influential Sunni cleric to determine that its practices were consistent with the Islamic faith. It sought and received from the cleric an opinion (a fatwa) that its operations were permissible under Islamic law.

Without such approval, Virgin Health Bank's business would have been over before it even began. "It's not just that we did the due diligence," says Glen, "but also we've engaged with people the community respects."



Then Virgin Health Bank had to develop a campaign to educate the community about the benefits of its services and to provide enough information to enable potential donors to make a well-informed consent.

Here too Virgin needed to be especially understanding about cultural values. For example, in Qatar and other Islamic countries, all the products of conception — not only the baby but also the umbilical cord and the afterbirth — belong to the father. Ultimately it is the father’s decision to donate because it’s the father who has proprietary rights in the eyes of their faith. See figure 6 for other details about Virgin Health Bank’s innovative business model.

**Innovative business model: Virgin Health Bank** figure 6

Key Tactic	Developed Economy Approach	Developing Economy Approach
Creating supply and demand	Extensive promotion but moderate educational outreach	Heavy educational efforts for prospective donors, regulators, and medical professionals
Religious leader endorsement	Not sought	Crucial to venture
Target audience	Mothers mainly	Fathers (crucially) as well as mothers
Social structure of business	Serves all donors as well as other patients of British national health service	Serves both private donors and public recipients
Social engagement	Serves national health service	Creating sustainable public resource in addition to private bank

Source: Harvard Business Review Analytic Services

“We engage with the mothers-to-be,” says Glen, “but we have to be sure also to engage with the fathers-to-be. We’re working in a different culture, and some of these cultural differences are very significant.”

Virgin Health Bank begins its educational outreach very early in the pregnancy cycle. It has recruited Arabic-speaking nurses to talk to both mothers and fathers in terms they find comprehensible and culturally appropriate. When mothers-to-be transfer their care in the latter part of their pregnancy to the hospital at which they will deliver, they meet with “clinical advisors” working for Virgin Health Bank.

The company also invests plenty of effort to convince medical professionals of its ethics and the high quality of its practices. It makes a big point about its quality standards for its units. It won’t process blood that fails to pass an especially rigorous test demonstrating that the stem cells will be viable after the blood is thawed. With both parents-to-be and medical personnel, it will not oversell the value of harvesting the cells by alluding to future treatments that might be developed with the cells.

The price for collecting, processing, and storing stem-cell blood units is \$3,550. Although health care costs in Qatar are paid for by the government (if patients use public hospitals), the charge for collecting cord blood is not paid for by the state medical service. So Virgin Health Bank has to sell convincingly the value of its services in a way that most medical service providers in Qatar do not.

It’s a situation ripe for conflicts of interest and shady dealing. For example, other blood banks pay doctors for referring parents to them. Virgin Health Bank says it would never do that.

For parents the long-range benefit is that, years later, the stem-cell blood may be crucial in treating a member of their family with a dire illness if that person is a close genetic match with the cells in storage.

Stem-cell treatment is a transplant and rejection is always possible. But such rejection is less probable the closer the future patient is to the child from whose cord the blood was collected. With a private blood-banking model like this, only the donors or their family members may use the blood.

Virgin Health Bank has also been developing for Qatar a sustainable public blood bank. It will use the same education and medical outreach services to encourage parents to donate their cord blood to the public blood bank. The parents would pay nothing for that donation, but the donation does not give them the exclusive right to use their child's blood in the future.

To collect units the public blood bank requires altruism on the part of the donors, but the public need is enormous. There are so few Arab stem-cell cord blood units in reserve worldwide (45 out of 19 million units), that the only hope for nonfamily members to benefit from stem-cell therapies in the future is for a sustainable public blood bank program to begin and expand.

Virgin Health Bank has won favor with the royal family in Qatar as well as much community goodwill for committing to this public blood-banking initiative. But gaining traction for the public bank could be a long, slow process. This is an emerging market in which almost all umbilical cords are discarded.

As with other health care costs in Qatar, if a Qatari patient needs a unit of stem-cell blood and happens to be a good genetic match for a unit in the public bank, that unit will be provided to the patient's doctor free of charge.

Virgin Health Bank is hoping to commence operations for the Qatari public bank in 2012, and this will function along with the private bank it established in 2009. After five years the Qatar public bank will be self-sustaining and require no more state funds but will continue to bank donated cord blood units in perpetuity. Virgin Health Bank is also developing a training program to develop skills among the local population. It hopes that, after five years of the public program, it will have predominantly Qatari technical staff delivering services to their own community. The goodwill its business model has earned is something it can bank on.

## Conclusion

Innovative business models, no matter which industry or target market, clearly depend on more than just a great technology or an appealing product. Globalization may provide lucrative business opportunities in more locations than ever before, but companies venturing outside their original borders need to consider a variety of factors beyond population, per capita income growth, and other standard business metrics. Indeed, as some companies have learned the hard way, sometimes the price is not right.

Emerging markets have to deal with scarcity in so many forms: lack of capital, inadequate infrastructure, and low levels of literacy and educational attainment, among others. What is also clear, however, is that they don't have a scarcity of ingenuity and determination to succeed. Araboh.com, Gulf Bridge International, and Virgin Health Bank all show how innovative and indispensable a start-up can be to an emerging market, whether it's a small, homegrown Arab-language book retailer, a cutting-edge medical resource bank, or an 8,000-mile-long transcontinental pipeline that is a twenty-first century digital connection with the rest of the world.

All three ventures have business models that are different from anything that has gone before. They illustrate how brainpower and a willingness to try new approaches can create an oasis of value and opportunity for the emerging market of the Middle East.

## ABOUT THE SPONSOR

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# The Qatar Foundation

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The Qatar Foundation for Education, Science, and Community Development is a private, nonprofit organization that is supporting Qatar on its journey from carbon economy to knowledge economy by unlocking human potential for the benefit of not only Qatar, but the world. Founded in 1995 by His Highness Sheikh Hamad bin Khalifa Al-Thani, Amir of Qatar, QF is chaired by Her Highness Sheikha Moza bint Nasser.

QF carries out its mission through three strategic pillars: education, science and research, and community development. QF's education pillar brings world-class universities to Qatar to help create an education sector in which young people can develop the attitudes and skills required for a knowledge economy. Meanwhile, its science and research pillar builds Qatar's innovation and technology capacity by developing and commercialising solutions through key sciences. Finally, its community development pillar helps foster a progressive society while also enhancing cultural life, protecting Qatar's heritage, and addressing immediate social needs in the community.

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