

I am delighted to be here at this particular gathering. I am very impressed with the progress that Acumen Fund has made in the last five to six years. I had the pleasure of meeting Jacqueline Novogratz when she came with the idea of establishing Acumen Fund; we did encourage her to indulge in this particular enterprise and I am glad that she did. Today Acumen Fund has grown from almost a crawling baby to a walking child. There is a lot to be done in order to imitate this model, fine tune this model, and replicate this model because the problem of poverty in Pakistan is enormous, and unless we reach scale it is not going to be sufficient for any one fund or any one institution to be able to overcome this problem.

The second challenge we face in Pakistan is that there is a struggle that is constantly going on between the very narrow proverbial interest of the elite, that has captured the state and market, and the remaining socially committed individuals and communities that want to take Pakistan in a different direction where equity and sustainability are the key hallmarks of this development model. Unfortunately we have not been able to come out on the side of the individuals who are trying to steer the country in the later direction, and we are still very much dominated by the old model which is described in my book in 1999.

Considering the fact that the markets have been a disappointment as far as equitable outcomes and sustainability is concerned, they are very good at allocating and utilizing resources, and also recognizing creativity and innovation. If there was no market you would not have Google, Yahoo, eBay; you wouldn't have all the technological changes that are taking place in the world. It is not because of the government's policies or regulatory frameworks, it is the reward to those that took the risk and they were rewarded adequately. That created a demonstration effect which you find in Silicon Valley, Bangalore, Poland, Latin America, and that is the way that the market functions.

We should try to incorporate the best lessons from the market into a different type of model, where the intervention of the state is kept out. Like markets fail there are government failures and government failures become worse in a situation where you have a small group of elites that dominate the state. That is where social entrepreneurs fit in - You operate according to the model of the market mechanism but you are not maximizing the shareholder profits. You are actually aiming at a much larger stakeholder, and community welfare maximizing – that, I think, is the whole crux of social entrepreneurship.

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You have a social objective that is either income generation for the poor, or health, or education, or drinking water supply, or rural infrastructure, which have traditionally been public goods. But these public goods have either been underprovided or they have been provided, not for the larger welfare of the community but for the personal interest of a small group. When there is a failure of provisions of public goods the social entrepreneur comes in the picture and says, “Look, we want to apply the principles of efficient allocation and utilization of resources but for the larger good, not for the corporation or shareholders.” This is a stage where we stand today and it has been very much buttressed by an awakening of people like Warren Buffet and Bill and Melinda Gates that have said, “We have made huge fortunes, how much do we need for ourselves, our families, and our children. That was the gain we have made through the personal effort for the larger course.” The 50 Billionaires Club has now expanded globally, even in India, they are bringing these people. It is a very good reservoir of patient capital because these individuals, foundations, and groups have different objectives. They have used the market to make money and now want to take that money and use it towards the benefit of the downtrodden, disadvantaged poor.

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Here is the mix between the two sides. Here in Pakistan we have a very large philanthropic sector, and unfortunately it is dominated by charity. You have examples that are familiar to all of you - mosques, *madrastas*, Edhi Foundation - these are examples of where Pakistani's individually and collectively do provide a lot. But the agenda for the poor is extremely diverse, even as economists we are trying to struggle with our own development practices and models. At this time we are aware that the third sector, which is made up of NGOs and community civil society organizations, have become very vocal and important, which is a good thing, have become the watchdogs for the corporate sector itself. The green peace struggle with the union members from the plantations of Indonesia, which destroyed the forest, has led to a realization in the boardroom that their own activities and investments should do no harm to the community and environment. That realization means that instead of looking at the

short term bottom line they have begun looking at the triple bottom line, which is ‘what is the social impact of our investments on the communities that we are serving and the individuals below the poverty lines, and what is happening to sustain the environment.

So that's a very good trend. So the trend in the corporate sector is not merely giving lip service to corporate social responsibility, but is rethinking their own role in a society, which has become much more sensitive and conscious of human rights and poverty. This is number one.

Number two, C.K. Prahalad was an Indian professor who died a few years ago and at University of Michigan wrote a very influential book on research he carried out in India about the bottom of the pyramid. The bottom of the pyramid is that you have one billion customers whose demands are completely different from the middle and upper classes. If you tap into these markets, by innovation and by customizing to that particular segment of the population, it makes good business sense.

In Pakistan I have told this to many audiences, some of my friends will forgive me if I have repeated this. In the last two years while the urban economy is contracting, the middle class is being hurt, the fixed income groups are in bad shape, almost 350 billion rupees additional purchasing power has been injected into rural areas in Pakistan because of a crisis of wheat, sugar cane, and rice. And that injection has created demand for those products that cater to this segment, so if businesses try to penetrate into the base of the pyramid markets there profits will be quite large. If you have a socially conscious investment and you are able to make a profit you have a win – win situation.

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What is the missing link then? The missing link is that you cannot count on corporate houses to carry out innovation, experimentation, and new models of delivery of services and income generation for the poor. This is not in their vein or DNA; they are not equipped to do it. This missing link should be provided by the social entrepreneurs. As Aun rightfully pointed out, it is a continuous learning process, and it is based on action research. The whole community or group of communities is your laboratory and you are trying to change one variable or two variables at a time and see what the impact is. When you have gone through this experimentation you have a model that you can have confidence in, and which is robust and you can replicate that model and scale up. That linkage between private sector and social entrepreneurship is pretty strong and should get stronger. It is quite solid in my view.

I have had the pleasure of being the Director of Poverty and Social Policy Department of the World Bank and we carried out a number of studies, from the deserts of Mali and mountains of Guatemala, where social enterprises and funds - although in infancy -were making a huge difference in the lives of poor communities. I think what was happening ten years ago is not valid today and what will happen ten years from today will not be what Aun was telling you today. It will be a completely different type of work being done by the social entrepreneurs. That is the beauty of it.

Now, what is the role of the government in all this? I personally believe, and I convinced my Board of Directors of the State Bank, and was vehemently opposed by Professor Yunus, who I consider to be a mentor, that the government should have no business regulating micro-finance in Pakistan. His argument was that like all other government interventions you would stifle the growth of micro-finance in this country. My argument to him, that I made publicly at the ‘Micro-Finance Summit’ in Daka where we were both panelists, was that if you are regulating and supervising the deposits and savings of the middle and high income groups through the regulating system why are you excluding the savings of the poor? We had so many scandals where people have taken money from the poor and run away with it. If you don’t take care of the safety and security of their deposits you will not have a self-sustained micro finance system. You will have donations and philanthropic contributions but it will not become a self - sustaining business for the poor.

I am very happy that today Pakistan’s regulatory framework is recognized by economists as number one, and there are people who are coming to Pakistan and looking at the model to replicate it in their own countries. Unfortunately the last two years have been very bad for micro-finance and let me say that those of us who want to take the micro-financing movement to the next level have a lot to learn from what’s happening inside and outside of the country.

Two years ago I happened to be the Chairman of the Board of Kashf Foundations, the largest NGO foundation outside of NRSP, providing 350,000 women with micro -finance. We had a complete breakdown of our system because some newly elected political leaders took it upon themselves to get micro-finance loans unilaterally written off. They said [In Urdu: From tomorrow you do not need to return any money. All of the debt is forgiven]. We went through quite the ordeal in order to reestablish ourselves with the help of many people including Acumen Fund, Grameen Foundation, and many others who helped us walk through a different scenario for the delivery of micro-finance. We fine tuned out model from the collective groups lending to verifying the credit worthiness of the individual borrowers. We are now reconstituting the whole business model, which is doing quite well despite the fact that we have urban-based, urban clients and the urban economy is not doing well.

On the other hand, Utter Pradesh is the largest user of micro-finance in India. India went into commercial domain use too soon, in my view. They had not really built all the building blocks in order to take the plunge, but there were some very smart private equity mangers that saw the opportunity that micro finance could take a quantum jump using the private equity model. Utter Pradesh did a great disservice to the micro-finance institutions by posing certain restrictions.

The whole idea - whether I was in Bolivia or Hyderabad – and the whole debate about micro-finance is the high lending rates of the micro-finance institutions. And the politicians take advantage of that. [In Urdu: You give to the poor at a lower rate and forgive their loans, while you give the rich higher interest rate]. That is the essence of the argument and what they don’t realize is that in the absence of the micro-finance the alternative is not the banking system that does not cater to the micro-finance target groups, it is moneylenders. The rate of interest of moneylenders is exorbitant. They are not interested in carrying the capital back. We have conducted studies on the behavior of the moneylenders. If they charge 100% they are only taking interest, and the principle remains the same. I have had people tell me that they are interested in

paying the principle back and the moneylender said, “No. We wont accept your money.” That is the alternative.

Why is the micro-financing lending rate high relative to other financial banking centers? It doesn't have a low cost deposit base and the banks have more than 50% of the deposits, which are reservations because they are current account deposits. The micro finance institutions do not have this. The State Bank never allowed any micro financing banking institutions to carry out deposit taking. Now the micro-finance bank has taken it, but not the micro-finance institutions. You don't have a stable, low cost deposit base. So your funding cost is quite high because you are taking a wholesale market or you are taking high net worth individuals who are interested in making a large return on investment.

The second problem is that a transaction cost of a small loan is the same cost of a transaction cost of 100,000,000 rupees loan. You have so many small transactions, the administrative costs of analyzing, assessing, and monitoring these loans is high. People go for syndication so they can have one billion dollar and your contribution is 1 billion, all the underlying work is the same. That is what the banking sector is good at. But ask them to go and talk to 75 individual borrowers and assess if they are worth taking the risk or not - you will need a huge amount of dedicated, trained man power and you need systems. That all costs money. If the cost of funding is high and the transaction cost is high, naturally the lending rate is going to reflect this; otherwise it is not a sustainable proposition.

Where does social enterprise come in to this whole equation? The way has been shown by Grameen and BRAC. They have for profit enterprises - they take the profits they from the enterprises and put into their social activities. So the cost to the ultimate borrower is reduced. That is the key purpose where the social enterprises can play a role in reducing the cost of doing business for the micro enterprises.

I want to end by saying that it is not just going to be money, but it will be human resources. At IBA, the premier business school, when I introduced the course for Social Enterprises and Marketing there were 3 students that came. Next time, I said that there would be a compulsory one-month internship in all the social enterprises in Pakistan because that is the way they will be familiar with what is really needed and they will try to go forward with opportunities in social enterprises. If you don't have the same human resources and manpower that you have in the corporate sector you cannot run social enterprises. We have a duty to provide these human resources.

Finally, we are also setting up the Center for Entrepreneurship Development, in which we will be training young entrepreneurs, women entrepreneurs, and our own students for BBA and MBA courses, so we will provide a pipeline of people who will eventually become the social entrepreneurs. This is our largest contribution. We must view this in a holistic manner rather than in a partial manner.

I am very grateful to Aun, Zubyr, and the whole Acumen Fund team for providing me with the opportunity to share my thoughts this morning. Thank you very much.