Blending Public and Private Value Creation at Natura

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One major, home-grown firm in Brazil offers a successful, impactful business model to overcome skill and talent scarcity.

Starting up a new enterprise in a location that has everything – an educated workforce, access to Wi-Fi, good transport links – is a challenge, but growing a thriving business in a place where the infrastructure is lacking seems nigh impossible. Entrepreneurs in emerging markets struggle with this problem every day.

One extraordinary example of a successful start-up under difficult conditions is Natura, the “cosmetics pioneer in Brazil” that has grown into a huge global beauty conglomerate, even acquiring its main global competitor, Avon. Starting out as a direct sales firm (e.g. a “door-to-door” distribution model), with “consultants” instead of employees, Natura managed to navigate the unknown waters of supply chain issues, educational deficits in its workforce and myriad other waves of uncertainty.

To unlock the secrets of Natura’s success, we applied **Elinor Ostrom**'s principles of polycentric governance – in which multiple governing bodies

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interact to make and enforce rules for protecting collective resources – to compare the firm's approach with more traditional paths. In an **article** in the *Strategic Management Journal* (see video abstract below), using novel pattern-matching methods to analyse archival data and detailed interviews, we found how this firm was different from traditional companies in the way it managed infrastructure issues. We were also able to map out a way for others to work with and within communities.

Like many Silicon Valley start-ups, Natura began with very little capital, but its founders had an inspired vision. The original concept was to incorporate cosmetics treatments inspired from nature with a personalised approach. But Natura had more than a cash shortage to overcome. Emerging markets lack many of the basics often taken for granted elsewhere – good roads, fast transportation, equal access to quality education, reliable telecommunications, supply chain expertise, etc.

Traditionally, firms (often business groups or multinational corporations) had one of two approaches to these problems. They either bought the infrastructure, controlling it; or these firms looked to other providers to create and maintain infrastructure while also trying to influence it. Natura, we found, uncovered a third way.

Open institutional infrastructure

Natura's success, viewed through a particular prism, is the model solution for firms lacking access to talent, organisational requirements and other challenges. Its novel approach is what we've dubbed open institutional infrastructure (OII) – when a firm invests in a pool of resources that is accessible to their commercial partners, communities and competitors. OII is not the simplest path for firms, but those who do engage with it may reap great success for the organisation and community, like Natura.

When services are lacking, firms need to take an active role in building institutional infrastructure, preferably an open one (OII). In business, polycentric governance encompasses sharing management ideas, roles and decisions with partners outside the firm, including governmental actors, NGOs and competitors. Of course, this requires non-standard types of processes.

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Who gets what? Ostrom's principles related to allocation of resources include the familiar boundary setting and benefit/cost ratios. In OII, however, firms have somewhat porous boundaries to encourage the access to resources for suppliers, partners, the community and even competitors. For a business to invest more money than it sees in return, relative to others who contributed less, may be difficult for firms in "developed" nations to get their heads around. The firm isn't necessarily the one that reaps the most direct, immediate benefit. For example, Natura experienced trouble when training its consultants because they were not always literate or numerate, due to gaps in the educational infrastructure. Rather than sending in an NGO to fix the problem or educating the sales force itself, Natura worked with partners and communities to find the right learning solution for the community.

A Natura HR executive explains: "We like to think of ourselves rather as the drummer boy; we organise the process in a totally transparent way. We're an invisible hand in this process…but we organise it so that the group becomes self-governing." The firm neither takes the lead on joint initiatives nor does it impose its own corporate objectives.

What to do? Allow for permeable boundaries and – this is difficult for many firms – accept some "free riding" from partners and suppliers. Accept that some costs to the firm will not have an immediate ROI but will add to long-term advantages.

Who makes the rules? These principles are about decision making and conflict resolution. In OII, the firm needs to deeply understand relationships between its partners and lift up the less powerful, encouraging them to participate in leadership and decision making. Conflict resolution may take longer with a holistic and long-lasting approach. This is especially important because governance stretches across public, private and non-profit sectors, creating multilateral cross-sector partnerships.

For reporting about its business, Natura was part of the pilot for the **Global Reporting Initiative** in 2000. The company's annual reports are incredibly rich in terms of information, not only for mandatory financials, but also about the company's different types of stakeholder relationships. One report was used to create a network graph depicting the structure of Natura's partnerships in our article.

This **graph** shows, for example, how Natura leveraged multilateral cross-sector partnerships to connect with supplier communities in the Amazon. The

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firm used communally held knowledge about natural ingredients to create some of its product lines, so executives wanted to make sure an entire community received compensation. If the firm had entrusted the money to community leaders, it's possible that only a few would have benefitted. In our paper, we mention suggestions made by a "leader" that funds be used to open a bar on a powerful community member's land. Natura worked with different partners, including an anthropologist briefly but also grassroots NGOs, via trial and error to empower the whole community to make decisions about the funds.

What to do? Help the less powerful gain rights; empower all actors to participate and make decisions.

How are rules enforced? In Ostrom's principles, rules and roles are clearly defined with fast conflict resolution enforced by sanctions that gradually become more severe. Firms are often more likely to look for rigid systems enforced by official positions and contractual agreements. Natura's approach to rules and conflict resolution is cooperation based on norms so that mutually agreed guidelines are followed.

Those norms are designed around the alignment of different partners' goals. In the words of Natura's former CEO: "It's a different type of partnership, we have to find harmony with each other to attain shared objectives." In other words, nobody bends the rules to fit their own objectives in ways that could potentially hurt others. Partnership means looking out for one another.

While this comes at a cost, the ensuing relationships are more enduring and result in more innovative and productive outcomes for everyone involved. In practical terms for Natura, this means lower default rates when salespeople pay off their product purchases, higher satisfaction rates and better performance than when their partners work with other companies.

What to do? A kind of voluntary cooperation should take over amongst partners that dovetails with public and private interests.

Beyond the current crisis

It's clear that the complex, large-scale, social, political and economic problems in the headlines require both cross-sector approaches and, importantly, business involvement as a force for good. In order to create value sustainably over time, firms can't ignore these issues. **Business**

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solutions should not be just for the good of the firm and its business partners.

Indeed, creating an infrastructure collectively, bringing together all the different partners with varied capacities, competencies and skills benefits everyone – a rising tide lifts all *boats*. Working across sectors with a diverse group of partners to collectively define solutions to fill gaps is how a new institutional infrastructure can be managed with polycentric governance.

Due to their rich experience in working with differing levels of institutional infrastructure, companies based in emerging markets may be better equipped for the complexity of business in uncertain times, especially those with experience in polycentric governance. Like Natura, these firms are more accustomed to the hurdles and benefits of working across sectors; they understand how business problems are social problems. Open institutional infrastructure creates business and social solutions.

*Click **here** for a video abstract of our article in the* Strategic Management Journal*.*

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