ICCO'S ROADMAP

OF

MARKET ACCESS STRATEGIES FOR

POVERTY ALLEVIATION

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LEI WAGENINGEN UR

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Foreword by Willemijn Lammers

We live in a globalised world. Decisions taken on one side of the world can have a major impact on the other. Markets in one continent depend on the movements of markets in another. Very few small producers, farmers, entrepreneurs, poor workers or poor households can escape the consequences. Yet many people actively relish them; they know that markets can bring them benefits and that without trade they would have far less access to education, health services and the consumer goods that they want to buy.

Indeed markets, and in particular local markets, are vital for the creation of employment, income and the availability of goods needed locally. These aspects – employment, income and availability - are crucial for the stimulation of effective demand and an internal market. A developed and differentiated internal market ensures that countries are not dependent on floating capital, one-sided primary production, an instable external market or imports for their own food consumption.

Fair and just prices must be paid; they provide an income for the producer/entrepreneur/worker and they will be spent and re-invested in their own market.
That's how economic development can take place; that's how ICCO/Kerk in Actie wants to contribute to one aspect of poverty alleviation and society building. Local market development is the heart of the fair and sustainable economic programme of ICCO and Kerk in Actie.

It's a great pleasure and honour to present 'ICCO's Roadmap for Market development for Poverty alleviation'. It was undeniably a long road to complete the manual, but the end was reached and the result is fantastic. There are not many studies related to stimulating local economies - particularly not from a wider development perspective - and if they do exist, they do not consider the view of producers organisations and/or development institutions.
This Roadmap presents the many theories on market access in a comprehensive document and links them to development practice. It will help analyse the strategies of small producers, farmers, workers and entrepreneurs aimed at achieving better market access, promoting business and chain development and creating a favourable economic environment. It was a challenge to publish something that would really be used, which would serve as a toolkit, would be practical and capable of adjusting and actualisation whenever necessary.

I am proud to confirm that the authors have definitely succeeded in their intentions and 'ICCO's Roadmap for Market development for Poverty alleviation' is a very interesting, practical and useful instrument providing many backgrounds, insights, methodological frameworks and tools.

Let's hope that it will ultimately contribute to the UN Secretary General's mission quoted on the front page: 'to enable women, men and children in cities and in villages around the world to make their lives better'.

Congratulations!

Willemijn Lammers,
Programme manager Fair and Sustainable Economic Development
ICCO/Kerk in Actie
Utrecht, January 2008.

Users guide line

This Roadmap of Market Access Strategies for Poverty Alleviation was developed for ICCO programme officers and Theme Specialists within the DREO programme. It has been an initiative of ICCO market advisors to support Programme Officers in decision making processes and to facilitate internal capacity building. The Roadmap presents the theory and useful tips on tools and intervention strategies that ICCO and its partners can use and develop to help the entrepreneurial poor in developing countries improve their access to local, regional and export markets.

The document summarises information already available within the ICCO office as hard copy or digital documents, such as publications, research reports and evaluation reports of projects. The Agricultural Economics Research Institute (LEI) supported ICCO in summarising these sources and structuring them into a comprehensive compilation of information. This information can be used for individual consultation by Programme Officers as well as for internal training and coaching purposes.

This Roadmap should not:

- ✓ Be read like a novel - sequentially and from cover to cover. We urge readers to use their common sense. Treat the contents page as an *à la carte* menu; read the bits that are interesting, use what is relevant for whatever programme development task is at hand and skim what is not relevant.
- ✓ Be used or read as a comprehensive step-by-step guideline that has to be followed in order to obtain a successful market access strategy. The Roadmap attempts to cover the broad terrain of identifying and analysing opportunities for market access intervention strategies. This information will provide ICCO programme officers and theme specialists with useful background information during the different stages of supporting partners to develop market access strategies for poverty alleviation.

The Roadmap is divided into 5 sub-divisions (see figure 1).

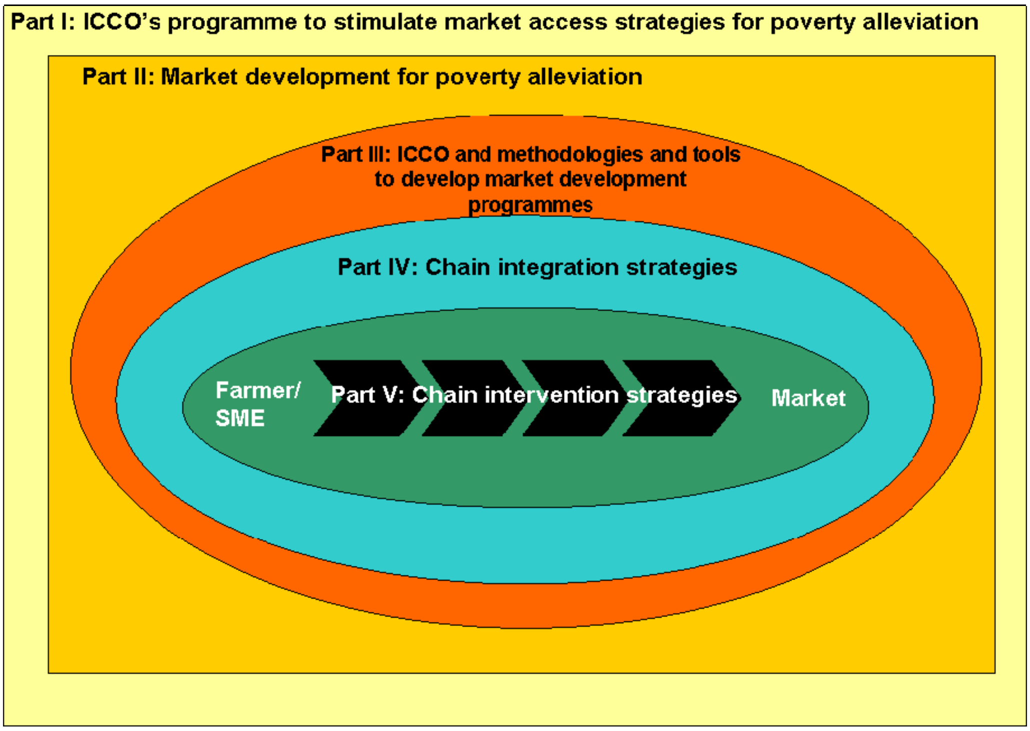

Figure 1: Roadmap document structure

Each subdivision consists of one or more chapters. Part I introduces ICCO's strategic vision on stimulating market access for poverty alleviation. Part II summarises the state of the art general vision on the theme, the importance of the enabling environment and the specific role(s) NGOs can assume to enable these intervention strategies. In 4 consecutive chapters, Part III then presents information about the most commonly economic scanning methods currently in use by development aid organisations to identify and benefit from market opportunities. ICCO programme officer can use these methods to obtain information about the economic activities in a specific region, market opportunities and constraints, sectors in development and specific chains. These methods are particularly useful when entering into a new intervention area, when strategic development plans have changed or there is a need for new initiatives and partners. Market access strategies are about getting (better) integrated into supply chains. For this, Part IV explains the theoretical reasoning behind stimulating horizontal and vertical chain integration strategies. ICCO and its partners stimulate a variety of horizontal and vertical integration strategies and thus support small-scale farmers and/ or small and medium-sized enterprises to improve their access to existing and/ or new markets. Part V presents in 6 different chapters a short description of the main intervention strategies promoted by ICCO to improve the competitive position of small-scale farmers and small and medium-sized enterprises in the chain.

As a summary, the document attempts to span the conceptually abstract (Part I), the contextually relevant (Part II), the methodologically particular (Part III and IV) and the policy relevant (Part V). Each chapter provides information on:

- ✓ the topic
- ✓ its importance for ICCO programme officers
- ✓ ways to use the methods or put in practice the strategy
- ✓ lessons learned and points of attention.

The chapters also contain blue text boxes. These present information on the practical experiences of ICCO partners in that specific topic. Further information on these initiatives can be obtained through the related ICCO Programme Officer mentioned at the end of the text box. We very much appreciate the information that was provided by Gemma Boetekees, Heleen Broekkamp, Petra Hamers, Joost van den Hee, Egbert Hoving, Bert Kling, Peter de Lange, Els Lindeboom, Guus Paardekooper, Marije Rhebergen, , Simon Runia, Annette Smits, Irene Visser, Nelleke van der Vleuten, Jeroen de Vries, , Jochem Schneemann, Johannes Solf, and Gerard Zwetsloot to describe the cases and collect ICCO experience on lessons learned and points of attention.

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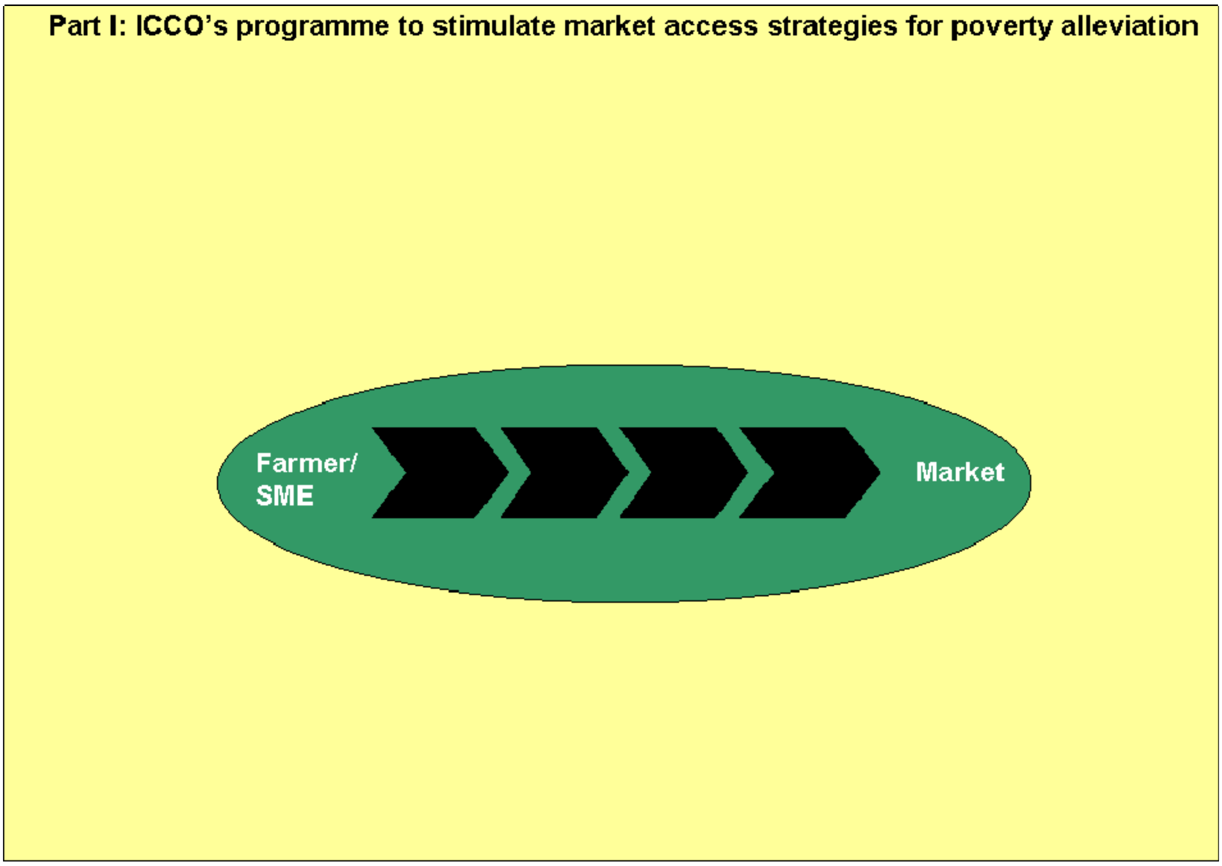
Part I: ICCO's programme to stimulate market access strategies for poverty alleviation



Through a great variety of initiatives ICCO has been active in supporting partners in the South with the development of the livelihoods of the poor for over 40 years. Over the past decade ICCO has shifted to a more thematic approach, with Access to Basic Services, Democracy and Peace, and Sustainable Fair Economic Development as its main themes.

Part I of this Roadmap introduces the main focus of the Sustainable and Fair Economic Development programme currently in place. ICCO programme officers, their partners, but also other development cooperation agencies have learned many lessons from sustainable economic development oriented programmes, the monitoring of the processes and the evaluation of the results and their impact. One of them is the importance of (improved) access to local, regional and international markets, which becomes also evident by ICCO's SFED programme structure, the development objectives for the near future and the capacity that has been created within the organization.

The information of Part I is especially useful for new ICCO employees that will participate in activities of the SFED programme. Also it can be shared with new and existing partners whom are interested in understanding more about the basic position of ICCO regarding sustainable and fair economic development.

I.1 Introduction

Approaches to development that have successfully tapped into and shaped the power of markets have allowed poor people, as consumers, producers and workers, to contribute to and benefit from economic growth. Various strategies are used to try to achieve this result, such as product and process innovation, alliances among farmer groups and alliances between suppliers, processors and traders. Both the renewed focus on economic activities and the fact that new types of partners are appearing within the chain approach requires a different kind of analysis as well as a more open attitude towards other sectors in society by both the partners and ICCO.

I.2 ICCO's Sustainable Fair Economic Development programme

I.2.1 Introduction

In 2001 ICCO opted for Sustainable Fair Economic Development (SFED) as one of its three corporate themes to reach its objective on reducing poverty. This decision and the reasoning behind it are described in the policy document "(On) the Road to Justice" (RtJ)[1]. At the time, this theme was a relatively new topic for the Dutch co-financing world, but for ICCO it was a natural step following the growing focus on this theme both inside and outside the ICCO organisation. The other two themes are Access to Basic Services and Democratisation and Peace Building. Since these themes are partially correlated, ICCO programme officers and thematic experts seek for opportunities to work in initiatives where more than one of the themes is considered.

The main reasons for choosing SFED as the thematic focus was due to the following trends[2]:

- ✓ ***Globalisation:*** In recent decades, far-reaching trade liberalisation of the world market has taken place headed by the WTO. Consequently, trade activities have become more global. This could offer opportunities to many developing countries. However, the dismantling of tariff barriers in western countries is an extremely slow process while Southern markets are regularly swamped; for example, the import of cheaper grain putting pressure on local production or even pushing it out of the market with all the subsequent consequences for food security.
- ✓ ***Chain responsibility and corporate responsibility:*** Far-reaching globalisation has produced more insight into production conditions in various parts of the world. Campaigns by civil organisations against abuse in the area of production (social and environmental) put pressure on the reputations of many companies. This led to a shift in thinking within the private sector in recent years and discussions arose between civil organisations and the business sector about alternative forms of entrepreneurship: Corporate Social Responsibility (CSR).
- ✓ ***Market-oriented thinking in development cooperation:*** Besides these developments at a more macro level, the development sector, having previously focused on (access to) basic facilities and preconditions for this, has increasingly come into contact with the market through concrete economic activities. The fair trade movement was the precursor in this field in the eighties and nineties. Over the years, more and more initiatives have started to focus on the organic and regular market.
- ✓ ***Empowerment of the South:*** More and more economic development initiatives are being developed in the developing countries themselves. Producer organisations created to help producers improve their position in the supply chain and opportunities for strategic alliances between chain members to create win-win situations for the different actors in the chain are initiatives being

[1] (On) the road to justice, ICCO Policy Plan 2001-2005, November 2000
[2] Policy Paper Fair Economic Development, April 2003.

developed in more and more countries. Furthermore, civil organisations are improving their advocacy capacity. This strengthens their capacity to represent and defend the rights of marginal groups in society, including small-scale farmers and micro and small enterprises.

As a result of these trends, awareness about promoting the sustainable development of economic activities in developing countries has grown. This has resulted in a shift in focus within development thinking, which has led to increased investment in private sector development in addition to the support of the public sector.

However, there are a number of preconditions that are vital for the success of economic development activities. First of all, the situation in the area/country in question must be fairly stable, both from a political and a social point of view. It is also necessary for a minimum number of essential stakeholders to be present: (organisations of) producers, NGOs, financial institutions, interested companies etc.) in order to make a start on a chain approach. Last but not least, products will have to be available or be found that present opportunities/possibilities to create specific changes in the chain so that the surplus can be redirected to the advantage of the producers. Consequently SFED will not be a logical intervention in every area/country. For this reason, ICCO decides on the basis of set criteria whether or not it can and/or wants to become active in this field in a particular region. ICCO's SFED programmes are currently developed in the following countries:

Region	Countries
Africa and Middle East	Benin, Senegal, Ghana, Cameroon, Burkina Faso, Kenya, South Africa, Ethiopia.
Asia, Eastern Europe and Oceania	India, Philippines, Central Asia, Papua-New-Guinea, Solomon Islands, Southern Caucasus.
Latin America	Brazil, Paraguay, Peru, Bolivia, Ecuador, Guatemala, Nicaragua, Honduras, El Salvador, Surinam.

I.2.2. SFED organisation structure

ICCO has been involved in economic development initiatives since the early nineties. The experience required in the field of economic activities and (international) trade has been acquired from various channels. Since the early nineties, specific attention has been devoted to sustainable forest use and sustainable agriculture. In the mid-nineties, interest in marketing and collaboration with the private sector came into the picture, leading to the introduction of the theme Aid & Trade (A&T). In the late nineties, ICCO set up the Credit Desk and started working together with financial institutes such as Rabobank and Oikocredit.

In 2001, ICCO started its first international market activities, first mainly focused on the sustainable cotton trade. Two years later, this was extended to tropical forest products and tropical fruits. A Local Market Development Advisor also joined the team of experts to develop programmes to improve access to national and regional markets. In 2006, an Advisor for Cooperation with the Private Sector was also assigned. This advisor will facilitate initiatives between the larger scale private sector in developed and developing countries, Programme Officers and ICCO partners[3].

I.2.3. SFED target group and livelihood strategies

ICCO approaches market and economic development issues from the perspective of **disadvantaged target groups in developing countries.** For ICCO, economic growth and

[3] For more information about the organisational structure, see ICCO business plan 2006-2010.

market development should create “inclusive growth” and offer opportunities for marginalised groups of the population. The objective of SFED is the improvement of the economic position of the underprivileged. The resources are the sale of (processed) production items or the supply of labour. The success of this concept depends on whether the production chain in which the players are operating is successful. This is the reason why, within SFED, a relatively high degree of attention is given to production and marketing chains. The success of an SFED activity not only depends on whether income is generated, but also on whether the F of SFED is actually put into practice: whether the yields in the chain are shared fairly and whether the target group has acquired a proportionate say in the trade process.

The majority of the economic activities supported by ICCO take place in the ***rural context***. The same applies to SFED. The target group in question is not homogeneous: differing groups employ a wide range of frequently complex survival strategies. Agriculture plays crucial vital role in the provision of food and income. But migration (temporary and permanent), off-farm employment, other forms of land usage, small-scale enterprises and tourism also constitute important sources of income.

Agriculture is the starting motor for development of many rural communities and has a multiplier effect on other sectors: on processing, trade, services and education. But it does not play this role in all situations. The proximity of a market, the presence of a good infrastructure, supportive regulations and policy and the availability of sufficient land and water are necessary preconditions. This restricts the role of agriculture in a geographic and social sense. It is difficult for agriculture to fulfil this starting motor role, particularly in marginal, isolated communities and it is only of significance for food security. Most marginal groups have insufficient land, water and other resources at their disposal to use agriculture as a source of income. Practice shows that very often only medium-sized farmers are able to develop their agriculture successfully as the (sole) source of income. The more marginalised groups seize alternative survival strategies to improve their position. Increasing diversification and complexity of strategies are consequently characteristic of the present situation. Investing in the education of children is very important in this context because it offers prospects of new sources of income for the future, often in the urban and service sector. In the majority of cases, it is a conscious strategy to (partially) abandon agriculture.

Sustainable rural development extends beyond improved agriculture and/or land usage and takes place within a larger context. Markets are linked to each other with their own rules of play. The effect of market forces and rural development are partially determined and influenced by local, regional, national and international policy. In addition to physical circumstances, political institutions and interests determine to great extent the space which target groups have to effectively exploit and consolidate their production systems and survival strategies. This also applies to the effective space assigned to NGOs when shaping interventions, implementation and evaluation.

Wherever possible, ICCO will try to ***promote and support more organic production*** methods. However, organic production is not an objective in its own right. In terms of poverty alleviation, it is important to ensure that the balance between the extra costs incurred for certification and the profits made from organic production are not disrupted for any length of time at the expense of the producers involved. The emphasis lies on improving the economic conditions in a broader sense, in which both social and environmental aspects play an important role.

ICCO is highly aware of the fact that various target groups have widely diverging interests in the market. Very poor target groups often deploy a more defensive strategy with regard to the market, aimed at survival and self-assertiveness. Those who are slightly less poor can approach the market more pro-actively and organise themselves economically. This is why

ICCO wants to draw a clearer distinction between ***three different target groups for its (SFED) programme****:*

1. We stimulate market-oriented projects, aimed at the development of small and medium-scale enterprises (urban/rural/agrarian) and their producer organisations and thereby the creation of better employment for the very poor groups.
2. We support projects aimed at disadvantaged target groups and the capitalisation of survival assets[4]. In this case, the aim is to increase the self-assertiveness of the poor in their market by promoting economically viable activities though the efficiency may initially be low. These could be farmers who have been able to improve their production capacity of potatoes, for example, which creates a surplus that can be sold to the local market.
3. We collaborate with the larger, formal business sector, aimed at socially responsible entrepreneurship, decent employment, chain responsibility etc.

SFED does not focus on those activities aimed at achieving a minimum subsistence level and at safeguarding food security. ICCO has a separate policy on this. However, it should be noted that the dividing line between those two different policies is not always clear and that, in terms of subsistence policy, one also explicitly looks for initiatives that could develop into a situation in which (part of) the production is intended for cash income. As far as the topic of ***food security*** is concerned, only those **aspects that are concerned with the relationship between the terms and conditions of production and trade are covered by SFED**.[5]

I.2.4. Objectives and ICCO roles

The SFED programme is aimed at sustainably improving the socio-economic position of underprivileged population groups through a market mechanism that is fair, social, ecologically sustainable and economically viable. The ICCO alliance focuses on smallholder producers, employees and self-employed workers in rural areas.

Objectives at ICCO level

In the 2007-2010 period, the ICCO alliance will focus particularly on the following specific objectives[6]:

1. At chain level:
   - ✓ The economic creation of added value in the South itself
   - ✓ Improving the position and working conditions of (agro-industrial) employees
   - ✓ The possible contribution of migrants to economic development
   - ✓ Multi chain partnerships
   - ✓ Innovative investment opportunities
2. With regard to preconditions for market and chain development:
   - ✓ Strengthening the service provision for (non-agricultural) company development, market development and entrepreneurship
   - ✓ Rural microfinancing and fund engineering

The development and harmonisation of standards:

- ✓ Developing local quality certificates
- ✓ International codes and certification schemes within mainstream markets

[4] Survival assets such as securing own food production, seasonal work in the dry season, some savings for a rainy day, safety networks for emergency situations and the aspiration to work for a decent boss.
[5] For example, the negative consequences for producers in newly established free trade zones such as the Mercosur, Alca etc.
[6] For more detail: ICCO Alliance Operation Plan 2007-2010.

Roles and instruments
To achieve these objectives, SFED is developed by using a mixture of instruments that will together lead to:

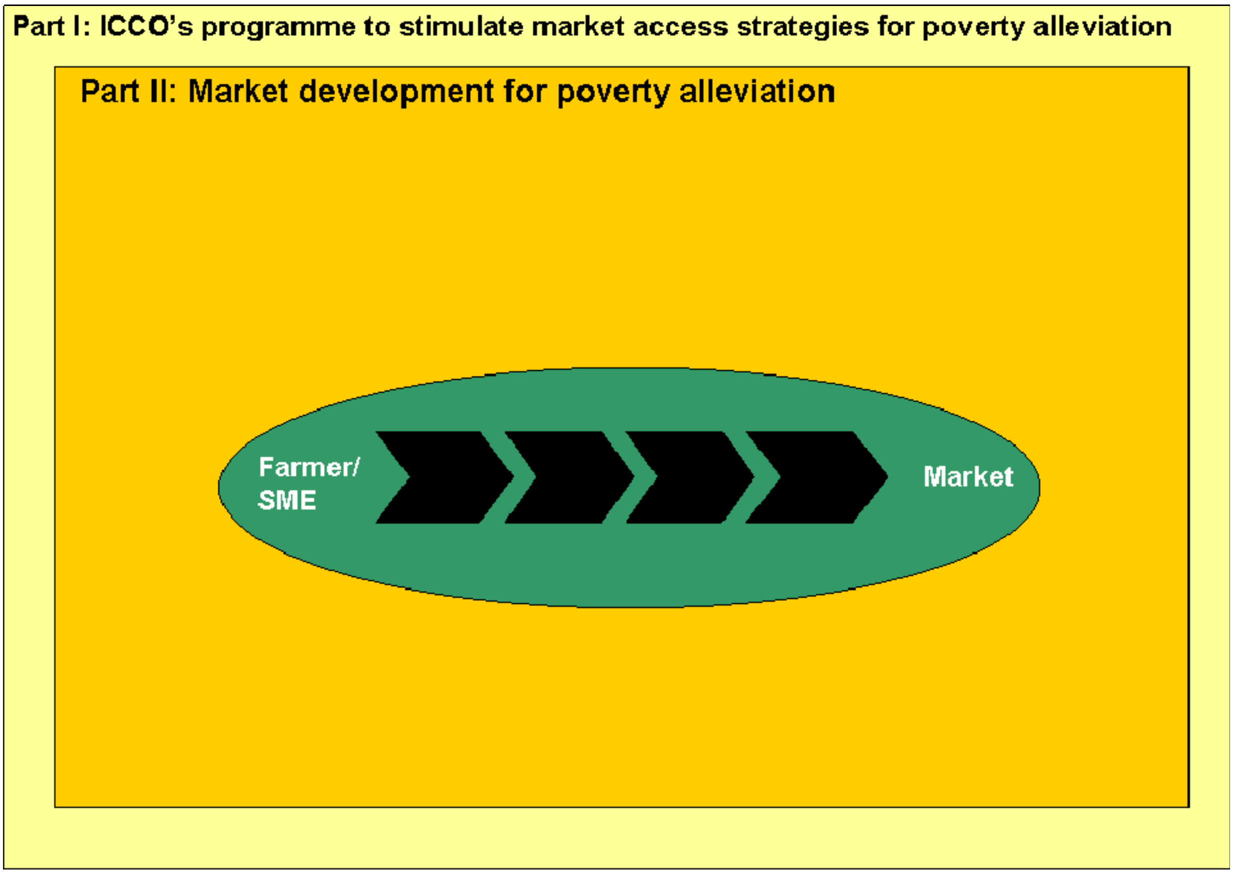
a Direct poverty alleviation by improving the competitive position of small rural entrepreneurs, producer organisations and microfinance institutes;
b Social Development, by creating an appropriate enabling environment;
c Lobby, by emphasising the importance of fair trade agreements, codes of conduct for the private sector and fair labels for produce.

In recent years, besides its traditional role of financing, ICCO has developed other functions necessary for the thematic development. These are the roles as intermediary, capacity developer and support, participation and lobbying. For more information on these roles, see Chapter 2.3 of this booklet and pages 26 and 27 of the ICCO business plan 2006-2010.

I.3. References

ICCO (2003), (On) the road to justice, Policy document for internal use, April 2003.
ICCO (2003), Bedrijfsplan 2003-2006, Policy document for internal use, April 2003.
ICCO (2006), Bedrijfsplan 2007-2010, Policy document for internal use, February 2006.

Part II: Market development for poverty alleviation



Approaches to development that have tapped into and shaped the power of markets successfully have allowed poor people, as consumers, producers and workers, to contribute to and benefit from economic growth. Part II presents an introduction to the state of the art thinking on market development and its potential contribution to poverty alleviation. Governments and development agencies' efforts at promoting economic growth and poverty reduction have achieved mixed results. What's worked and what hasn't? Why is it that poor people in some countries have experienced huge improvements in their lives and retain the realistic expectation of more to come while, in many others, the numbers of the poor have grown and their prospects, apparently, are not very good? What explains this difference and how can we learn the right lessons to allow more people to move away from poverty? Answers to many of these questions lie in markets.

The introduction in II.1 makes clear that the effective support to the development of rural areas and enable farmers by improving their access to the market requires a good understanding of the market, but also the factors that influence the functioning of this market. Therefore chapter II.2 explains market development and the so-called enabling environment. Within this dynamic and fluid environment, actors of all colours can be seen as stakeholders. At the level of (inter)national societies, stakeholder relationships are traditionally cast in the form of a triangle: market, state and civil society. The interactions between stakeholders from these 'spheres' shape the institutional environment and define the 'rules of the game'. ICCO is one of the multiple actors involved. Both the renewed focus on economic activities as well as the fact that new sorts of partners are appearing within the thematic working field, requires a different kind of analysis as well as a more open attitude towards other sectors in society, on the part of both the partners and ICCO. Chapter II.3 explains which mayor actors can be involved and the roles each one may play to stimulate strategies on market development for poverty alleviation, with special emphasis on NGO's.

II.1. Market development for poverty alleviation

II.1.1. Introduction

In development literature, the economic definitions of poverty have been primarily based on the ability to purchase goods and service. That is, on income and consumption and on material possessions of assets. The dollar a day poverty line[7], refers to household expenditure per person. Economic conditions of poverty thus focus on goods and services as measured through the market (or imputed market) process and the corresponding policy thrust in poverty reduction is on increasing income and consumption.

But over the last 25 years, there have been significant changes in development thinking and poverty and a broader multi-dimensional concept of poverty has been increasingly adopted by actors in the international development arena. Income measures of poverty continue to remain important, but there is great consensus that a thorough understanding of poverty requires more comprehensive socio-economic analysis. This includes the need to incorporate the views of poor people themselves if poverty reduction policies are to be successful.

II.1.2 Importance of markets in poverty alleviation

The role of markets is critical to understanding and addressing poverty. Properly functioning markets provide jobs, opportunities, services and information which offer chances to the poor to increase their income. The poor can be involved in many different markets like the labour, land and financial markets, commodity and product markets (such as in agriculture) and service markets (such as infrastructure and business services).

Markets offer the primary means through which poor people can participate in economic activities. They can do so as producers (farmers, business owners), as employees (i.e. providers of labour) and as consumers (of goods and services). However, when markets are not functioning properly, poor people have fewer chances to participate and benefit from economic growth. The condition of income poverty is therefore inextricably linked to the functioning of markets (Gibson et al., 2004).

II.1.3 Functioning of the market

In order to increase the participation of the poor in markets, it is important to understand how the market functions. Markets can be generally described by their core market of trading which is embedded in an environment of services, infrastructure and institutions (Gibson et al., 2004):

1. <u>The core market</u>: the supply and demand essence of any market, sellers and buyers who constitute the central transaction process. The poor participate in this market as:
    - ✓ Buyers or consumers of goods and services such as finance, water, electricity, agricultural inputs and food. The degree of the poor's market engagement can be measured by the market use and consumption intensity and their perception of the market.
    - ✓ Sellers or producers: for example as small-scale farmers. Participation is shown in their number, market share and in the prices or margins they achieve.
    - ✓ Employees: numbers and wages are key indicators.

2. <u>Institutions</u>: the rules of the game, formal and informal, and their enforcement that shape how markets operate. Informal practices take over where formal rules and their

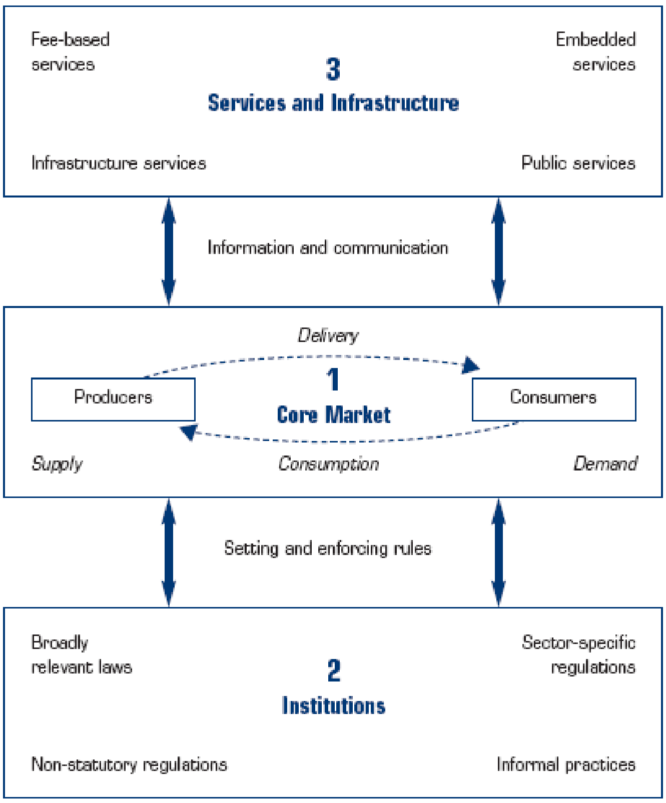
[7] World Bank, 1990, World Development Report

application are weak. To understand the institutional framework, it is important to identify those that impact most on market development and, crucially, how they impact on markets. Different sets of institutions affect the market:

- ✓ Broadly relevant or non-market-specific laws that shape the market such as contract, property, consumer protection, weights and measures, health and safety, competition and tax laws.
- ✓ Sector specific laws are focused for example on banking, electricity or land use.
- ✓ Non-statutory regulations such as industry codes of good conduct, quality standards and registers.

3. Services and infrastructure: smoothening markets through information and communication, providing the means through which markets can change and improve. Services can be divided into the following groups:
    - ✓ Fee-based business services such as business consulting, accountancy, advertising, computer services, security, legal, market research, technical information and equipment maintenance.
    - ✓ "Embedded" business services where no separate fee is paid but which is included within the commercial transaction – for example, market designs as part of a retailer-producer relationship or livestock advice from input supplier to farmer.
    - ✓ Infrastructure: this includes electricity, telephones, roads and water. While these are conventionally seen as hard, physical facilities, at the point of consumption they are (soft) services.
    - ✓ Public services – although not a fixed category and often allied to regulatory roles, there are clearly some services that are aimed at a wider public purpose, including business statistics, public health and information on regulations. Services are often offered through a market and are becoming a transaction process in the core market.

Figure 1: Key Market Dimensions



Source: Gibson et al., 2004

Markets are inter-connected. The performance of one, whether good or bad, affects another. Effective land markets can provide the collateral basis to stimulate financial service markets; specialised business services markets impact on manufacturing competitiveness; relevant information provided through a functioning media feeds into many markets; improved telecommunication offers previously unconnected farmers the means to access up-to-date price information (Gibson et al., 2004).

The poor are mostly producers or consumers in the core market. The poor are seldom service providers or involved in setting the rules of the game. The functioning of the market to the poor depends substantially on the performance of the institutions, the available infrastructure and the services delivered. The government and companies are key players in these dimensions.

II.1.4 Market access and appropriateness

Malfunctioning markets are excluding the poor. The poor can be physically too far away from the market due to poor infrastructure services. Access to the market is also obstructed for poor people because of the lack of know-how and know-who caused by poor institutions and the lack of services to the poor. In financial markets, lack of understanding about how to open a bank account or provide references from existing account holders may present even greater constraints than physical distance from banks. Access to information depends on the performance of other markets (including radio, mobile phone and IT) and the services provided. The poor generally lack a network of people and institutions that could help them improve their access to the market. At international level, the poor, especially farmers, have problems accessing the market due to trade policies and strict food safety and standard levels.

Secondly, poor people can be excluded from the market because the available market is not appropriate for them. The appropriateness relates to the characteristics of what is dealt with in the market, notably in terms of prices and conditions. Furthermore, questions arise as to whether regulations allow employers to offer suitable jobs for the poor and whether banks will accept a deposit which a poor person can afford to start saving.

If the poor are to integrate with the markets, they need to have access to the market which offers them reasonable prices and conditions (Gibson et al., 2004).

II.1.5 References

Gibson A., H. Scott and D. Ferrand 2004, *Making markets work for the poor – An objective and approach for governments and development agencies*, ConMark Trust, Woodmead, South Africa.
Moll, H., F. van der Staaij and A van Tilburg, 2001, *Smallholder and markets – towards a conducive environment,* Policy and Best Practice Document 8, Dutch Ministry of Foreign Affairs, ACI Amsterdam, The Netherlands.

II.2. Enabling Environment

II.2.1. Introduction

The enabling environment of the market is generally regarded as a broad set of political, social and legal institutions together with available services and infrastructure. Institutions are defined as formal and informal rules that shape human interaction (North, 1990). Formal rules refer to laws and regulations, while informal rules are based on customs, norms and on the available social network. These rules and their enforcement mechanisms and organisations promote market transactions.

Institutions have three main functions (World Bank, 2001):

1. Transmit information about market conditions, goods and participants.
2. Enforce property rights and contracts.
3. Manage the degree of competition.

The functioning of the institutions thus affects the costs of exchange and production. If institutions function properly, obtaining information, negotiations and contract enforcement will be easier and quicker and will therefore lower the costs, often referred to as transaction costs. Informal rules and norms are important in lowering transaction costs because knowing and trusting people will enhance exchange (Eaton and Meijerink, 2007). Services and infrastructure are the loosest dimension within this view of market development. Due their apparent intangibility, this sometimes leads to the question: Where are the services in any particular market? (for further details, see also Chapter V.2).

II.2.2. Why is an enabling environment important?

In developing countries, informal rules are relatively more important than formal ones, because the surrounding community often influences the creation of possibilities and how new ideas are established (World Bank, 2001).

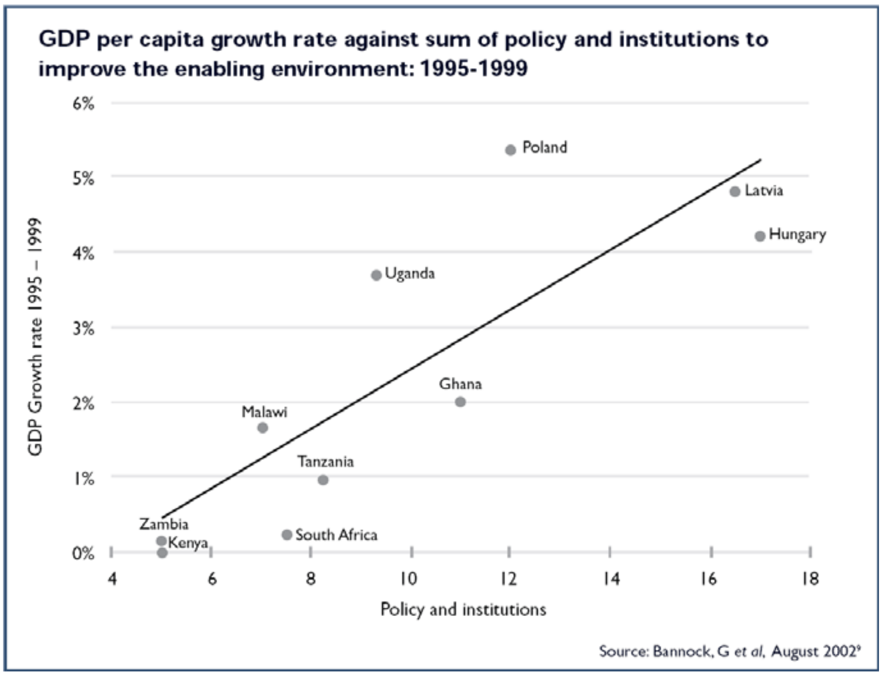


Figure 3: GDP per capita growth rate against sum of policy and institutions to improve the enabling environment[8].

[8] Note: The scale of policy and institutions shows the extent of presence and functioning of certain policies and institutions aimed at 'best practices'.

Formal rules are sometimes not enforced, providing more room for informal rules. Institutions can lower (or raise) barriers to firm entry and exit and affect the speed of the enterprise formalisation process. Adoption of favourable policies and institutions for an enabling environment will not guarantee economic growth or growth in GDP. However, Figure 3 shows that those countries that have adopted most elements of the favourable institutional and policy mix also have the highest growth rates.

II.2.3. How to improve enabling environment?

Since markets are multidimensional and multiplayer by nature, the essence of market access strategies for poverty alleviation is working with the market players to create a "better" market system.

General strategies to improve the enabling environment include policy studies, building the capacity of private-sector associations and coalitions and developing the capacity of government agencies to analyse and revise their own regulations and practices.

The World Bank has developed four approaches that should ensure development of effective institutions (2001):

- ✓ Complement what exists as the impact of an institution depends on the availability of supporting institutions, existing levels of corruption, degree of transparency and underlying human capacity and technology.
- ✓ Innovate to identify institutions that work – and those that do not.
- ✓ Connect communities of market players through open information flows and open trade.
- ✓ Promote competition since more competition will improve existing institutions. The service content in products is becoming an increasingly important way of providing a competitive advantage. For example, agriculture input suppliers increasingly compete on the basis of information they can offer along with seeds, fertilisers etc.

In some cases, support is also provided to develop new institutions. An important factor for the success of these initiatives depends on whether the institution is respected or can be enforced (Eaton and Meijerink, 2007).

Quite practically, the World Bank developed the "Doing Business" database with objective measures of business regulations and their enforcement. The database provides indications on the regulatory costs of businesses and can be used to analyse specific regulations that enhance or constrain investment, productivity and growth. This database helps define benchmark countries on their business environments and it is arguably creating peer pressure amongst countries to improve their business regulatory environments (Miehlbradt and McVay, 2005).

Governments have played a leading role in the provision of particular services, usually on the basis that these benefit a wider public and that the poor in particular will be excluded if governments do not have a leading role. For this reason, if considering direct provision roles, three trends should be taken into account (Gibson, et.al., 2004):

- a Direct provision is often captured by those who are better off and better connected and in this process the poor might get excluded;
- b Services such as water, electricity, telecom, which have traditionally been seen as the domain of the government, have been privatised in some countries within a framework set by government.
- c With regard to business services and agricultural advice for farmers, functioning markets can offer these through a range of formal and informal sources.

Commercial banking potentially provides a highly efficient system for mediation in an economy, but these gains can only be obtained through effective regulation. However, regulation is more than a simple administrative task. It requires in-depth understanding of how an industry and a market work to allow knowledgeable engagement with private sector players. It requires a clear vision of how the market can work and the role of different players within it.

II.2.4. What are the points of attention when developing initiatives to influence the enabling environment?

1. In understanding the institutional framework, the priority is not to exhaustively list all the rules that exist but to identify those that impact most on market development and, importantly, how they impact on markets. Three sets of questions could be useful (Gibson, Scott and Ferrand, 2004)
    a What are the most important formal rules and informal institutions impinging on the market and the poor and how do they impact on the market?
    b What (and who) are the most important formal mechanisms for enforcement of rules and how do they impact the market?
4. When analysing services and infrastructure, three important facts should be taken into account (Gibson et.al, 2004).
    - Markets are interdependent and it is not always clear where one begins and one ends. The means through which many services are provided is often also a market (see Chapter V.2). The important point here is to identify the importance of different functions within a market; services and infrastructure are a key function.
    - The importance of services and infrastructure is growing rapidly. Information and knowledge are increasingly central to business competitiveness, allowing firms to specialise, reduce costs and innovate. The tertiary service sector now accounts for 60-70% of most industrialised economies. Fee based services alone account for typically 25-30% and this figure is growing.
    - Setting and enforcing the rules of the game is always a core role of governments and can be critically important in stimulating markets.
5. Improving the enabling environment is a complex, long and uncertain process. While donor-supported programmes can identify and promote good practices, changes often ultimately depend on the politics of a given country (Miehlbradt and McVay, 2005).
6. The risks of market distortions are reduced by:
    - Avoiding donor self indulgence to casually pursue their “own thing”. Especially in weaker economies, this will result in market-distorting interventions that will undermine the aim of the intervention strategy.
    - Having actions that benefit a number of players, so that unfair competitive advantage does not accrue to one player at the expense of the market system as a whole.
    - Organisations not subsidising directly the delivery of a service or product, but supported through assistance, for example, to develop capacity, new products, new business linkages, or collaborative arrangements. The end game of interventions is not performance (improved services, higher profits) from one firm per se, but more robust, contested markets.
7. Invest in appropriate capacity. Choices on roles to be played have inevitable operational implications. More specialised staff, knowledgeable of markets and the private sector will be required and will need to be invested in.

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II.3 Role of the Public, Private and NGO Sector in market development

II.3.1. Introduction

At a time when sustainability has emerged as one of the major issues facing societies and the world in general, the question of how this should be achieved remains highly debated. The chosen path will largely determine the outcome and that path is determined by the exchanges and interactions between business- and societal stakeholders (Van Tulder, Muller and De Boer, 2005).

Societies are becoming increasingly complex. Organisations can increasingly be identified as 'hybrids', whereby boundaries, drivers and coordination become blurred and even potentially conflicting. Much of this is related to the rise to prominence of the market, which refers to the increasing influence of market actors (companies) on government and society.

Markets are multidimensional and multi-player by nature. The essence of facilitation is working with these market players to create a "better" market system. More than the normal lip service of "stakeholder discussion", market development for poverty alleviation can only be successful when market understanding, a vision of the future and consequent actions are owned by key players. These key players for market development in developing countries are: the public sector, private sector, civil society organisations and donor organisations.

II.3.2. Public sector role

Governments and civil society organisations often question where they fit in a market. For them and for development agencies the answer is the same: ***nowhere***. Its role is as temporary facilitator, a provider of appropriate and focused assistance to build markets successfully. This facilitator role can be observing and analysing the market or identifying the benefits and constraints for the target group. Investing in understanding markets, including its enabling environment, is a starting point for building ownership and developing a consensus on how they can work better in the future.

The pro-market approach does not mean that governments should no longer be a player in the market. The government still has roles to perform with regard to the institutional and service dimensions of the market. In particular, the government can play a core role in stimulating markets by setting and enforcing rules. In general, governments are the main formal players in the institutional framework, setting and enforcing rules. However, the private sector through membership associations may be more effective in developing industry-specific regulations where ownership rests firmly with the industry.

During the last two decades, many public services have been privatised. In many countries, the state used to supply common goods such as drinking water, electricity and telecom facilities. Now they are often provided by the private sector within a framework set by the government. However, many of these public services are crucial to the poor like agricultural advice, road infrastructure and telecommunication. Important responsibilities of the government are also land registration, financial regulation, information provision and standards setting (Gibson et al., 2004). These responsibilities should be emphasised as their impact to the market access of the poor people is substantial.

II.3.3. Private sector role

Companies and the business sector in general are the main players in the core market and in providing services. Companies can help stimulate local markets and enable the poor to become active participants in these markets, both as customers and entrepreneurs. Many companies see a need to break out of mature market sectors. They are increasingly regarding the poor as an interesting group of customers (Prahalad, 2004). Global trends like improved communication systems are creating a favourable environment for companies to start engaging with the poor and doing so is more and more publicly expected (WBCSD, 2004).

The poor can fulfil different roles in the partnership with businesses or companies (see Figure 4). For some business activities, the poor will be customers. In this case companies' contribution to market development will be to supply appropriate products and services that meet local needs at appropriate prices. Companies will provide jobs to the poor as well. But their main focus will be to ensure the fulfilment of basic and often vital needs (water, electricity, sanitation and health care) on a sustainable and cost-effective basis. The poor may be business partners, suppliers, employees and/or distributors. By bringing small entrepreneurs and local small and medium enterprises into value chains, business can create employment and accelerate skill transfer (WBCSD, 2004).

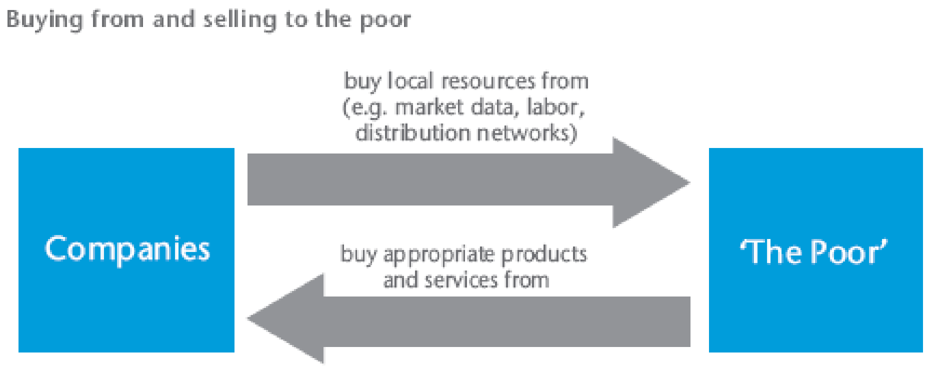

Figure 4: Roles of the poor in partnership with businesses
Source (WBCSD, 2004)

II.3.4. Donor role

Donors should not play a key role in the market. The market should be able to function by itself without being dependent on the support of donors. The role of donors is as a temporary facilitator to build markets successfully by facilitating others to do things. Facilitators need to be flexible, knowledgeable, close to market players and create a bridge between different perspectives. Most donor agency staff cannot play this role directly; they need to invest in the right entities that can. Direct transaction subsidies from facilitating organisations run the risk of disrupting prices and incentives more than less direct routes like support in capacity development and providing business linkages. To avoid unfair competitive advantage, the facilitator should work with a number of players (Gibbon, 2004).

II.3.5. NGOs/ Civil society organisations

Since the early nineties, with the advent of the bargaining society, NGOs have been calling companies to account for their social responsibilities in a variety of ways (Tulder et al, 2004). NGOs/ Civil Society Organisations (CSOs) have shown in numerous cases that they can force companies to action due to the power that they wield over public opinion. NGOs operate at two interfaces:

(a) between the state and civil society and
(b) between the market and civil society.

The first interface is the most traditional, reflecting the financial relationship between government and NGOs, which in such cases appeal to governments to obtain additional funding for projects they carry out. However, it is especially the second interface (b) that is undergoing change. Many NGOs believe that companies, more than government, are/should be able to address certain issues. Five strategies can be distinguished by means of which

NGOs intervene in companies and markets so as to make their influence felt (see Text box 1).

- *Anti-business campaigns*: effective in raising public consciousness about an issue and putting pressure on companies. Tend to be only effective against well-known branded companies on black-and-white issues.
- *Market intelligence*: still largely focussing on individual companies, a growing trend involves building market intelligence on companies and facilitating pressure from employees, customers, suppliers, investors, boards etc. for improvements in performance on key issues.
- *Business engagement*: engaging businesses in partnerships aimed at collaboratively addressing key issues.
- *Intelligent markets*: Potentially the most powerful way to intervene in markets is to try and do so at the level of the market – rather than with individual or groups of businesses. A few NGOs are attempting to do this by actively working to 'reframe' markets to reward positive behaviour and penalise negative behaviour.
- *Market dis*ruptions: come in the form of regulatory interventions or shifting liability regimes, to jump market frameworks to higher levels of sustainability.

According to Elkington and Fennell (1998), NGOs can assume four roles in this regard: (1) Sharks, (2) Orcas, (3) Sea Lions and (4) Dolphins. Sharks and Orcas are inclined towards polarisation and confrontation (see for a further specification of roles annex 1). They act more (Sharks) or less (Orcas) instinctively, strategically and in groups. By contrast, Sea lions and Dolphins are more inclined towards cooperation. Sea lions will accept sponsoring from companies (and tend not to criticise the hand that feeds them too much), while dolphins realise that companies can create important preconditions to achieve desired change but prefer to retain their independence in the process. Both confrontation and cooperation can be adequate strategies. Many NGOs start out as sharks: with direct action, debate and as much independence from companies as possible. According to a report by SustainAbility and the United Nations (2003), the categories of Orcas and Dolphins have gained in importance and appeal.

When NGOs operate more independently, their campaigns become less predictable for companies. Such campaigns are also almost always geared towards protest, debate and polarisation. In such campaigns, NGOs chiefly adopt a single-issue approach and focus almost exclusively on exposing the problems. If NGOs are more solution and product oriented and seek to operate as company representative (Sea Lions) or endeavour to carry out a joint project with companies (Dolphins), there is a great likelihood that they will focus on relatively simple (single) issues. In addition, their dependence on and predictability for companies will also increase. It is only when NGOs seek a 'mutually' dependent relationship with companies that it is possible to implement a more multi-dimensional approach in practice, by means of which problems and solutions can be linked with each other.

II.3.6 ICCO's role in intervention strategies on market access

If the list of Elkington and Fenell were applied to ICCO, the main driver for ICCO would be the "greater leverage" (Van Tulder et.al, 2006). This would be derived from ICCO's mission statement, structure, strategy and activities. According to ICCO, their main focus as a development NGO is on poverty alleviation and on civil society building in developing countries. This may be related to the Dutch covenant polder approach which emerged in the 80s and which has developed extensively ever since. This approach involves business and government jointly setting up environmental and social agreements which are based on consensus and consultation between government and industry bodies for the benefit of all.

ICCO as well as Novib and Cordaid are taking the lead in these kinds of partnership projects. Hivos is more involved in the accreditation and streamlining of CSR standards in the world.

A potential business partnership project other than the development of a micro-credit institution often develops as follows*: in the first instance, a CFO fulfils a technical expert role in mapping a commodity chain in a certain country or region. In addition, this CFO identifies potential (business) partners. Potential business partnership projects for credit financing or grant payment are identified. Based on this information, the CFO fulfils a broker's function in bringing "on board" interested corporate actors from both the developed country and the developing country in a stakeholders' dialogue after which potential partnership projects are developed.

The Northern CFO can then choose to finance the identified partnership projects through credit financing, grant financing or a mixture. Based on the type of financing, the NGO becomes more or less involved in a partnership project, either as a financier of credit, often in collaboration with a development oriented bank and/or as a grant provider of capacity building-related activities such as strengthening a farmers' cooperation or a processing unit. The CFO can also fulfil a technical expert role providing training to farmers or producers to increase the quality of their products. An example for this theoretical case is the ICCO-Reef partnership case below. From this provisional analysis, it appears that philanthropical sponsoring partnerships are common between CFOs and businesses. According to CFOs, business development partnerships seem to be a better and purer way of contributing to sustainable development, especially when it (the CFO) performs as a broker. In this situation, the CFO remains independent from the company. Further research is necessary to draw definitive conclusions. SFED mainly focuses on those activities that are **market-oriented.** SFED is concerned with the entire supply chain, within which processing and marketing occupy a central position. It is concerned with better, more equitable access to (local, regional and international) markets, paying a proportional amount of attention to sales opportunities for target groups that have little or no access to these markets. SFED links up with various alternative forms of employment and micro-enterprises in the rural community.

ICCO's role in SFED initiatives is one of donor, broker, capacity builder and lobby. As a donor, ICCO provides funds to partner organisations in developing countries for them to develop their intervention strategies in order to improve the market access for their target groups. As a broker, ICCO helps the different actors in supply chains get in contact with each other. Within the SFED-related projects, the underlying process and implementation strategy is based on a **chain approach**. From production to end buyer, a product often passes through various phases in the supply chain that have a significant influence on each other. This means that there is no point in concentrating exclusively on production if you have no insight into outlets. Nor is there any point in concentrating solely on processing if you have no insight into the supply of raw products and their quality. Consequently, chain intervention does not mean examining only one component, but examining the entire chain.

The point of departure with such chains is that **alliances are formed** wherever possible, whereby everyone adopts a role that is suitable to the agency or organisation in question. This applies to NGOs and producers (producer organisations), government bodies, companies, banking institutions and donors. For an alliance to work, each player should subscribe to the essence of SFED with regard to purchasing agreements, decent pricing, transparency, transfer of knowledge and working collectively to solve problems. These are essential components of SFED that give substance to the F in Fair.

* According to an interview with H. uit de Bosch and a Cordaid representative on 20/07/2004

ICCO's partnership with REEF, a Dutch logging firm in Cameroon

ICCO's relationship with Reef has existed for the past six years, with initiative coming from both parties. Reef came under increasing pressure from its customers (the national government and municipalities in the Netherlands) to deliver only wood certified in accordance with the Forest Stewardship Council (FSC). Furthermore, logging rights are granted in the form of government issued concessions (for which logging companies also pay a hefty fee) that are also contingent upon submission of a sustainable forest management plan. Reef was thus looking for knowledge of the local market and government practices through local partner organisations of ICCO, while ICCO was engaged in activities to improve the standard of living for poor local forest dwellers. The government of Cameroon, meanwhile, has two major priorities of its own: limiting the export of uncut logs and the introduction of a certification system in accordance with the FSC.

The costs of implementing such a certification scheme are enormous and continue to be pre-emptive and illegal and uncertified wood is a major share of all wood produced and exported. There are about twelve major players in Cameroon: firms from Europe, the Middle East and Asia. Reef is a medium-sized player (of which there are about 20). Not all support the certification efforts, arguing for example that certification (which carries a premium of 4-8 percent relative to uncertified wood) will drive the price of tropical wood as a building material right out of the market. The World Bank, the World Wildlife Foundation and the EU were instrumental in getting the government to take measures against a number of large loggers for their continued use of illegal wood. Reef also has a history in illegal logging, but from ICCO's perspective, it is more important that the companies remain active (so that the local population remains employed) than that the wood is legal or certified. For example, Reef recently purchased and commissioned a local sawmill, which allows for more local added value and income and apparently manages to run profitably. For ICCO, this was in itself an indication that Reef's intentions were good, despite being hindered by government corruption and obstinacy. In other words, illegal logging was a necessity in the face of government reluctance to issue new concessions.

ICCO describes Reef as a 'pioneer' in partnerships, in contrast to opportunistic firms eager for the positive image and brand spin-offs of partnerships but without any real intention of giving the partnership any body. Although the ICCO-Reef partnership does not involve a contract or any direct financial transfers (which would otherwise constitute a subsidy and therefore anti-competitive behaviour), ICCO does fund non-commercial activities such as the forest management plan required for logging concessions or AIDS prevention training of REEF employees. The forest management plan involves a three way contract between the government, the logging firm and the local employees. In this contract, taxes are established as well as the redistribution across federal and local governments. ICCO's local partners play a role in ensuring that the local population recognises it has a right to claim local government tax revenue for local infrastructure and socio-economic improvement. ICCO has no say in the determination of local employee salaries, but 'tries to ensure that people earn enough to shape their own existence'. ICCO's role is to improve their bargaining power – their income improvement remains the ultimate high priority.

- *based on interview with Margot Klute, June 30, 2004*

The chain approach means that one will be working with a variety of stakeholders in many cases, such as producer organisations, companies (in which producers may or may not be participating), knowledge institutions, (local) authorities and financial institutions. In a large number of cases, this will involve developing formal as well as financial relations. In other cases, it may be restricted to working agreements. In many countries economic activities take place in the informal sector. ICCO will, where possible, encourage partners to seek innovative solutions for **making contacts in the formal sector**, possibly in collaboration with the regular business sector or local or national government bodies. An active search will be made for new partners who can identify with the ICCO policy and are prepared to assume a pioneer's role in promoting an equitable economy in their region.

International trade often offers partners both opportunities as well as (trade) barriers.
The fact that ICCO is a Dutch organisation has, in the case of international trade, added value in the establishment of contacts with buyers in the North and for initiating discussions on trade barriers. In relation to **international trade**, ICCO adopts the role of broker in the development of innovative partnerships between producers in the South and potential buyers in Europe. In order to play this role well, it is necessary to channel energy towards just **a limited number of products**. The main reasons for this are:

- ✓ to be able to estimate markets and also potential,
- ✓ to build up relations in the sector concerned and to be able to identify reliable, interested partners,
- ✓ to gain experience through which a distinct profile can be created for ICCO.

Taking into account the history and reputation that ICCO has built up, as well as previous obligations and the problems and potential of a specific product, the products that are taken into consideration currently are **forest products** (including non timber forest products), **tropical fruit and organically produced cotton**. In recent years the main attention has also focused on **stimulating the access to local/national markets**. After all, the majority of economic programmes supported by ICCO depend on local marketing.

In this case, the choice has not been in favour of a specific number of products (these can vary markedly per region); the emphasis has been placed on the development of an action plan for a specific region and a set of instruments for the development of local marketing chains. In accordance with the present trend in policy developments, a more **sectoral approach** will be chosen to acquire better insight into the stakeholders that are required for the development of such a programmatic approach. Apart from funding and brokering, ICCO also works on capacity building and lobby and advocacy within the programmatic approach. The aim is that these different strategies are tuned to the specific situation and reinforce each other and thus maximize the leverage and impact.

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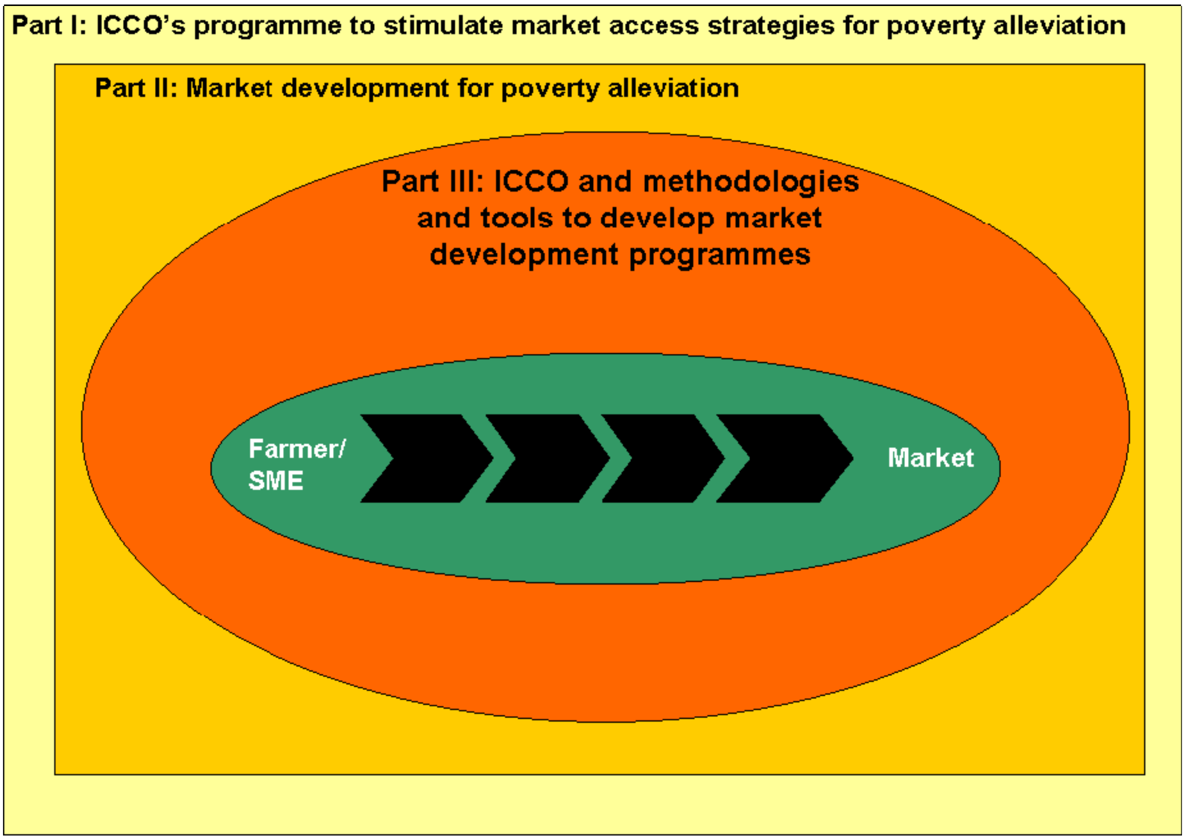
Part III: ICCO and methodologies and tools to develop market development programmes



A great variety of strategies are used to try to reach improved market access for the poor. It is ICCO's intention to cluster these strategies in strategic regional or sectoral development programmes. These programmes may consist of one or more projects that support specific intervention strategies.

This Part presents the most commonly used methodologies and assessments tools available to ICCO programme officers that may help them to identify opportunities and constraints for the development of local, regional or international market development programmes. The findings of these assessments enable ICCO programme officers to define their programme objective, to stimulate chain integration (Part IV) and identify partners to develop intervention strategies (Part V).

This section describes for each methodology why it is useful for ICCO employee, its importance regarding poverty alleviation and providing market access to smallholder farmers, terminology and key elements related to the methodology and points of attention when using the methodology. It is important to mention that the methodologies described are not to be applied by ICCO programme officers, but by partners and/or third party experts. The information of this Part will enable ICCO programme officers to select the appropriate methodology, define the expertise required, the objectives of the assessment, and the desired outcome.

In practice, when selecting a methodology it is important to know what you must know, what you don't need to know and what you cannot know (Roduner, 2006). How and when to apply each methodology depends on the experiences and thinking patterns of the user as well as the institutional settings. For example when choosing a Sub Sector Analysis (SSA) or Value Chain Analysis (VCA), external experts with public funding are more likely to implement an in-depth analysis; while NGOs or local consultants choose action research (AR). And entrepreneurs would most probably perform a rapid market appraisal (RMA) (see figure 5).

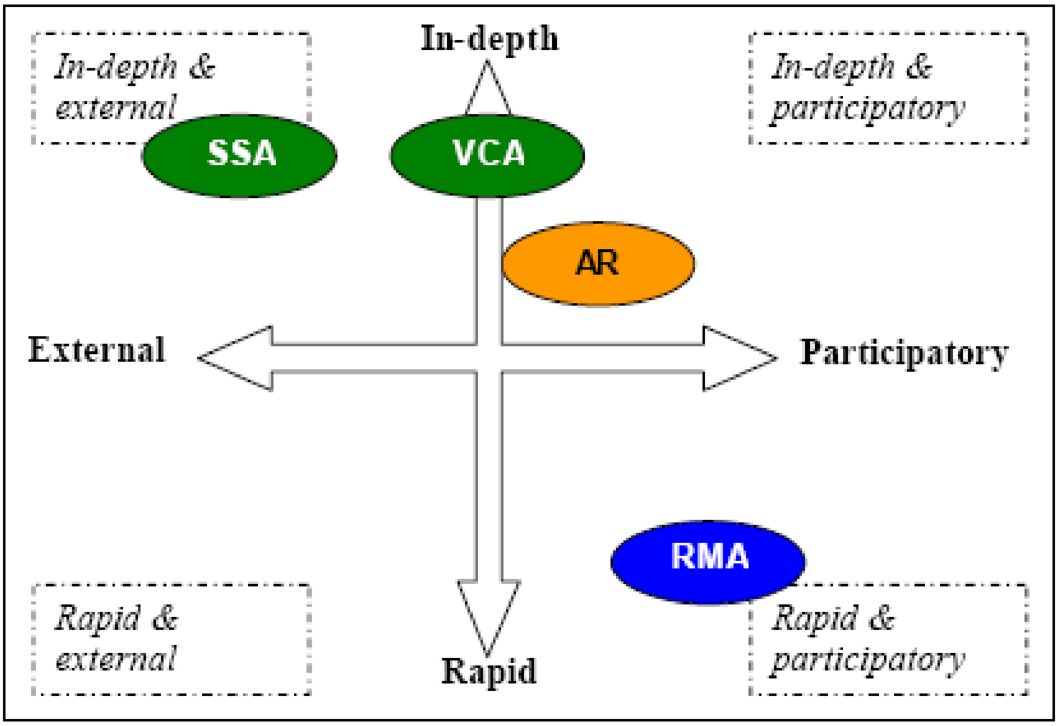


Figure 5: Market development assessments methods
Source: Roduner, 2006

Besides criteria such as time and availability, and the level of participation desired, selection is mainly based on the desired development strategy. That can either be more livelihood-oriented or more market-oriented. The first relates more to geographic assessments methodologies, while the last to sectoral analysis. Examples of geographical mapping methods (III.2) are market analysis and development (MA&D), local economic development (LED) and ECOLOC. Two main sectoral analyses are the Subsector Analysis (SSA) (III.3) and the Value Chain Analysis (VCA) (III.4). The basic information one would like to obtain through a subsector analysis and a value chain analysis can already obtained by conducting a rapid market appraisal (RMA) (III.1).

III.1 Rapid market appraisal

Why is rapid market appraisal useful to an ICCO employee?

A RMA is a relatively simple tool to explore market trends and opportunities. The technique essentially involves an informal, rapid, exploratory study of a specified geographical area designed to establish an "understanding" of local agricultural conditions, problems and characteristics.

The advantages of a RMA are:

1. Efficient in orienting production to the market demands
2. Practical tool in which the results can be directly implemented by the chain actors.
3. The implementation of likely to be successful due to the participation of the chain actors in the RMA.

III.1.1. Why is a Rapid Market Appraisal important?

Interest in the Rapid Appraisal (RA) grew out of frustration with lengthy, costly and management-intensive formal surveys in developing countries that rarely generated timely and policy relevant analysis. The Rapid Market Appraisal (RMA) is one type of RA. This appraisal method aims specifically on the identification of market development related information. The strength of the RMA lies in the short time required to obtain in-depth information for first level decision making on sharing regions and target groups for market access development programmes. Conducting a RMA is an efficient way to obtain policy-relevant and intervention-focused information about any sub-sector in a specific region. The method avoids the cost, delays and management burden of formal surveys while still providing the experienced analyst with a practical set of tools for identifying constraints and opportunities, cross-checking observations and planning or monitoring strategic interventions.

A RMA can help recognise the needs and opportunities present in the market place. When clients become a source of information, ideas for new and improved products can be exploited. If producers communicate with their clients, the demand for their (potential) product can be assessed so that only marketable products are produced. RMA can provide basic information on the feasibility of beginning a survey project in an area, particularly when one is intending to survey an area about which little is known.

RMA methods can also be a useful exercise at the start of longer-term programmes of applied research and testing of marketing system innovations. In addition, RMA can be used for focused study updates (of earlier formal surveys) and to complement a longitudinal, formal research programme. Finally, RMA surveys can be used to identify agribusiness opportunities as well as to design, monitor and evaluate donor-funded projects and policy reform programmes.

RMA is also useful for supporting decisions aimed at improving agricultural marketing systems in developing countries. For this RMA tools can be used. The role that Rapid Marketing Appraisal can play in this broad sense of marketing research lies in the identification and prioritisation of marketing problems and the evaluation of practical means of improving marketing functions, to meet the needs for expansion coupled with higher performance. A frequently stated benefit for people involved in RMA is the improved relationship with customers. These improved relationships lead to new customers and greater sales and profits. Another benefit of RMA is finding new business contacts, including suppliers and NGOs and information on new markets (ILO, 1999).

RMA methods have distinct advantages over survey-based research methods: they generally involve low costs, they are highly adaptable to different situations and they tend to facilitate the establishment of a rapport with local communities, making it possible to explore topics not easily studied otherwise or to bring out qualitative aspects that would be missed by close-ended surveys. They also favour analysis on the spot with local people, enabling verification of findings and enhancing the local relevance of results.

Developing local market development programmes for Bolivia and El Salvador

ICCOs new policies for Bolivia and El Salvador regarding the support of initiatives that enable small holder farmers and SME to improve their access to local and regional markets on economic development programmes created new challenges and opportunities. It was decided to conduct a rapid appraisal to obtain an overview of the main development agencies and local NGOs involved in the topic, the sectors they were involved in and their experiences in this field. This information could provide a good basis for ICCO to identify their opportunities for new initiatives in specific regions, sectors and areas of support and to help ICCO programme officers to decide about the next steps.

ICCO launched terms of references (ToR) to obtain proposals from local and international consultants, as well as existing in country partners who were interested in conducting the RA. In both cases, a local and foreign expert were selected. These were considered the most suitable team since they combined knowledge about local habits and networks together with knowledge about and experience with the methodology to conduct a RA.

The selected experts started to **collect data** on on-going programmes in the area of local market development for small-scale farmers in underdeveloped rural areas. Based on these data, the experts and ICCO jointly prioritised the **contact persons and organisation identified**. The more in-depth information was collected by **interviewing** a selected number of people based on a survey. In some cases, the *project site* **of the contact persons was visited**.

The consultants presented a report describing the results of the study. This report was used by the related ICCO programme officers to prepare their next visit to the countries and use the results for their meetings with new contacts. Also, the report helped to **define the next steps to develop the programme**. This enabled ICCO to obtain a general overview of entry initiatives and opportunities and constraints for new activities supported by ICCO.

For more information: Programme Officer for Bolivia en El Salvador.

The general principles of rapid appraisal methods are:

1. *Optimising trade-offs*: relating the costs of learning to the useful truth of information, having trade-offs between quantity, relevance, accuracy and timeliness of the information acquired, as well as its actual use. Trade-offs in this sense are not merely mathematical ratios; in the context of cost-effectiveness, they also entail alertness, observation, imagination and the ability to pursue serendipity.

2. *Offsetting biases*: through introspection, it is necessary to identify cognitive biases and deliberately offset those biases. The recommendations are: to be relaxed and not rushed; listening not lecturing; probing instead of passing onto the next topic; being unimposing instead of imposing; and seeking out the poorer people and what concerns them.

3. *Triangulating*: using more than one technique/source of information to cross-check answers, i.e. comparing and complementing information from different sources or gathered in different ways. It also involves having multidisciplinary members with the ability to approach the same piece of information or the same question from different perspectives.

4. *Learning from and with the rural people*: this means learning directly, on-site and face-to-face, gaining from indigenous physical, technical and social knowledge. Farmers' perceptions and understanding of resource situations and problems are important to learn and comprehend because solutions must be viable and acceptable in the local context and because local inhabitants possess extensive knowledge about their resource setting.

5. *Learning rapidly and progressively*: this means the process of learning with conscious exploration, flexible use of methods, opportunism, improvisation, iteration and cross-checking, not following a blueprint programme but adapting through the learning process. However, this is not intended to be a non-systematic way of conducting research.

Additional requirements particular to a RMA are:

1. *Client first.* It is the client who can best describe higher expectations of a product. The chain actor should always question “how to create the clients’ satisfaction”. As a result, a “middle-man” is as much a client as the “end consumer” of a particular product. RMA recognises the clients and the intermediaries as the experts in the market concerned. Their knowledge and experience is sought and considered important. The outsiders (e.g. the RMA team) see themselves as students, not as experts (Helvetas, 2002).

2. *Optimal ignorance.* Optimal ignorance means that only that information is sought which is required for a decision. It is accepted that a complete understanding of a situation and system is impossible or too costly for the particular product (Helvetas, 2002). In a subsector analysis, the aim is to understand a system as much as possible.

3. *Participation.* As a matter of principle, RMAs feed the collected information back to the stakeholders concerned. This is not only to validate the information but also to avoid turning an RMA into an extractive research activity. Usually Rural Business Development Services Providers such as an extension service, a development NGO or a farmer’s organisation are in charge of a RMA. They are

generally much closer to the farming community than a university institute or a specialised market research institute. Since the RMA tools are simple, they can even go a step further and include selected producers in the research team too (Helvetas, 2002).

III.1.2 Methodology of Rapid Market Appraisal

RMA is part of the Market Systems Research (MSR) group which views the consumer as the first and last point of contact for intervention design. This is in contrast to the Farming Systems Research (FSR) group, to which the Participatory Rural Appraisals (PRA) belong, that regards the farmer as the focus (Fleming, 1990). Direct observations and semi-structured interviews conducted within a structured framework are the most commonly used tools (Helvetas, 2002). RMA methods offer development workers a useful set of research and appraisal tools to quickly obtain information from local populations about their conditions and their needs. RMA methods also enable local people and outsiders to plan appropriate interventions together and evaluate the impact of development interventions after these have been carried out.

Table 1: Common rapid market appraisal methods

METHODS	Useful for Providing	Advantages	Limitations
KEY INFORMANT INTERVIEWS	--general, descriptive data --understanding of attitudes and behaviors --suggestions and recommendations --information to interpret quantitative data	--provides in-depth, inside information --flexibility permits exploring unanticipated topics --easy to administer --relatively inexpensive --takes 4-6 weeks	--does not generate quantitative data --susceptible to interviewer and selection biases
FOCUS GROUP INTERVIEWS	--customer views on services, products, benefits --information on implementation problems --suggestions and recommenda-tions for improving activities	--can be completed rapidly (5 weeks) --very economical --group discussion may reduce inhibitions, allowing free exchange of ideas	--does not provide quantitative data --discussion may be dominated by a few individuals --susceptible to moderator biases
COMMUNITY INTERVIEWS	--village/community level data --views on activities and suggestions for improvements	--permits direct interactions between evaluator and large numbers of individuals --can generate some quantitative data on community characteristics, behaviors, opinions --participants tend to correct each other, providing more accurate information --inexpensive and quick (5-6 weeks)	--can be manipulated by elites or monopolized by individuals --cultural taboos or norms may inhibit discussion of certain topics
DIRECT OBSERVATION	--data on physical infrastructure, supplies, conditions --information about an agency's delivery systems, services --insights into behaviors or events	--phenomenon can be examined in its natural setting --may reveal conditions or problems informants are unaware of --can be completed in 3-4 weeks	--suseptible to observer bias --act of observing can affect behaviors --distortions can occur if sites selected are not representative
MINISURVEYS	--quantitative data on narrowly focused questions for a relatively homogeneous population --when probability sampling is difficult --data on attitudes, beliefs, behaviors of customers or partners	--can generate quantitative data --reduces non-random sampling errors --requires limited personnel and is quick (5-6 weeks)	--findings are less generalizable than those from sample surveys --suseptible to sampling biases --requires statistical analysis skills --inappropriate for gathering in-depth, qualitative information

Source: USAID, 1996

A RMA is an iterative and interactive research methodology, which is used to better understand complex market systems in a short time (Young, 1994). RMA techniques rely heavily on structured informal interviews with key informants, knowledgeable observers of a subsector and a minimum number of participants at different stages of the subsector. These interviews provide an opportunity to clarify and probe, discover causal links and relationships and identify well-defined, but poorly understood areas for further formal research. See Table 1 for when to use which method and what their advantages and disadvantages are.

The first step of a RMA is to describe accurately and meaningfully the systems that exist. The next step is to evaluate structures and performance and the major forces responsible for changing their relationships.

Main steps to undertake in a typical RMA are:

1. Define objectives and strategies. Once the objective is known, the question is how to achieve it or what strategies are required. When choosing strategies, consider to include both traditional, existing products in the region and/or new, potential products exhibiting high demand growth, periodical scarcity, or which are imported into the region or where the region has comparative advantages (Lundy, 2002)
2. Develop a research plan. The research plan ensures the efficient fulfilment of the objectives established and should include:
    a. Secondary and primary information requirements
    b. Research approach
    c. Methods of contact
    d. Sampling plan (sample unit, sample size, sampling procedure, selection of probability or convenience sample)
    e. Research tools (questionnaire and interview guide)
3. Processing and analysing data, including the determination of the first market option portfolio
4. Final report on the rapid market survey

Whenever ICCO programme officers plan to contract an external expert to conduct an RMA, a number of basic issues must be considered in relation to the people who will work with it, including:

1. *Training and selection of personnel*

The skill of fieldworkers is critical to the success of RMA methods. These skills are quite different from those required by formal surveys. Firstly, there is the emphasis on social skills: controlling dominant personalities in group settings while seeking the participation of silent participants - all of this without imposing one's opinions - requires superior communication abilities. Another distinctive attribute is that, unlike survey enumerators who collect data for analysis by outside researchers, RA fieldworkers have to collect, analyse and validate the data themselves. They are the researchers. Hence they need a sound understanding of the aim of the research so that they can change the instrumentation used, if necessary, without losing sight of the final objectives. Being a good interviewer in an RMA context requires the following skills:

- sensitivity to social and cultural conventions
- listening attentively rather than lecturing
- asking clearly phrased, concise questions (avoid jargon)
- avoiding leading questions
- the ability to pick up on subtle nuances in responses and follow up with probing questions
- sensing how far to probe in questioning an informant and know what types of questions are off limits (where a respondent is unwilling to answer or might be offended or embarrassed by the question)

2. *Establishing contact*.
Community life is complex and care must be taken from the start not to unwillingly alienate groups or individuals by associating too closely with the "wrong" person(s). It is useful to make unannounced visits to a village before the first official visit, in order to learn the basic "political language" of that community. This can be done by sending one fieldworker to the village, who establishes informal contact with anyone he/she meets. Avoiding local authorities is preferable, although not always possible. Free-flowing discussions are initiated with the people encountered. In contrast to this first informal visit, an official visit is well announced and involves local authorities as well as high-ranking officials in the project. This visit is preferably not used for working sessions. The aim is rather to explain the project goals and the type of work to be done, request permission from local authorities, arrange dates for workshops and establish an understanding about who will be invited to attend.

3. *Timing of the workshop and sequencing of instruments*.
Project personnel must look for ways to minimise the disruption of people's lives. If possible, the meeting is held in periods or seasons of low activity; otherwise, field personnel must look for a time of day when people are back from their daily activities. This increases the likelihood that people will actually respond to the invitation and attend the meeting. The sequencing of instruments during the workshop should normally follow a logical flow.

4. *Choice of informants*.
Initially, all community residents are viewed as potential informants. Some of the exercises – for example mapping, concept definition - can be done without being selective about informants insofar as they know their community well and are honest in their responses. Soon, however, target groups need to be identified and individuals from these groups must play the central role in the discussions. Furthermore, within identified target groups, subgroups usually need to be considered. Typical subgroups are stratified by gender, livelihood strategy, for example farmers versus ranchers, age group, ethnic/caste affiliation, etc. Separating groups may also be necessary if putting them together creates social tensions. Finally, just as informants are selectively identified for specific exercises, conversely the choice of method must take into account informants' profile, i.e. if literacy levels are low, the method should not require reading skills.

5. *Triangulation*
Triangulation refers to the comparison of data between sources to improve its validity and reliability. This is particularly critical with RMA data as it is easily manipulated by informants, although group meetings tend to reduce this problem. The important point is that no data should ever go unchecked, especially if it is used for making important decisions. The quality of RMA information may be verified in several ways: replicating the exercise with other groups, exploiting alternative sources of information (e.g., aerial photos or prior surveys), comparing results against predicted values from mathematical models, "ground truthing" by walking transects and so on.

6. Key Informant Interviews.
Identifying and interviewing a small but purposively selected sample of key informants is a critical element of RA. Small samples of informants need to be chosen at each stage of the research. What they say needs to be cross-checked against what they do, how they behave, what analysts observe about their operations and what other key informants think about the constraints and opportunities they identify. Cross-checks are done with other individuals or firms at the same stage or at adjacent stages in a technique known as *mirror-image interviewing*. This involves asking informants at adjacent stages (food processors and wholesale distributors, for

example) the same set of questions. Strong divergences of opinion and in responses may require expanding the samples at particular stages. During *triangulation*, analysts achieve a better understanding of an issue or topic through successive approximations by interviewing informants with different perspectives and capacities to understand particular subsector features.

7. *Structured informal interview guidelines.*
The guidelines should be prepared for use in interviewing different types of key informants in the commodity subsector. These can be as simple as a checklist of key topics and sub-topics to cover, or several series of sequenced questions, designed for probing inquiry in a logical, step-wise fashion. Using these guidelines helps make the interviews more consistent (with each other), systematic and focused.

8. *Direct observation.*
No RMA would be complete without selective visits to important parts of the researcher to production or marketplace facilities. A key reason for doing this is to cross-check what informants say with how they behave and their usual practices. A site visit can also help a trained analyst estimate the scale of operations of a facility if good data are unrecorded or unavailable.

A knowledgeable observer is a person who does not currently participate in the researched process or who has never participated but who has studied it and understands it in a systematic way. Such an observer might be an academic or other researcher, a retired food industry manager, a trade association official, a subject matter specialist working for an association or perhaps a government agency. Sometimes these people are identified late in the process; meeting them earlier can save time and energy. You are more likely to identify one or more knowledgeable observers early on in the institutes, associations or agencies noted above. With them, you can carry out several open discussions, similar to brain-storming. The observer can provide a good reality check against possible biases. Any observer will have biases as well, but these will become more obvious once the team begins to interview key informants.

III.1.3 What are the points of attention when doing a Rapid Market Appraisal?

- The selection and training of fieldworkers is much more critical than for conventional enumerators. The quality of an RA depends heavily on the training, experience and calibre of the analysts who participate in the study. The experts should at least have knowledge of and experience in business development activities, private sector development, small-scale farmers and poverty alleviation programmes. This combination sometimes makes it necessary to contract more than one expert.
- RMAs are best implemented by multidisciplinary teams composed of “outsiders” and “insiders”. Prior to the fieldwork, the RMA team should be fully aware of RMA principles and techniques and the nature of market systems to be investigated. A search of secondary data sources should also precede any primary research activity (Helvetas, 2002).
- It is helpful to work with experts who are already part of the ICCO network, since this allows an open exchange of information during the whole process.
- The appraisal consists of different research and decision making steps. It is recommended that ICCO is involved in the decisions to be made during the process.
- Having strong local RMA collaborators helps in conducting interviews and sensitising expatriate analysts to local customs and conditions. Local experts also have better access to data, contacts and other required information.
- It is important to obtain a clear overview of the different actors involved in market access strategies. Be careful not to limit the study to existing initiatives of producer

organisations and university programmes but also to incorporate private sector development initiatives.

- ICCO programme officers should understand that the rapid appraisal only provides an initial overview that can be used to focus newly planned intervention strategies. In many cases, the rapid appraisal should be followed by a specific analysis.
- The relationship of the rapid market assessment of new products to the application of rapid reconnaissance techniques to subsector analysis should be noted (Clevenger, 1989).
- Be aware that the findings of a RMA are difficult to generalise and lack clear validation procedures and are therefore susceptible to manipulation by informants.
- The qualitative focus of RMA methods limits researchers' capacity to transform the data, thus constraining the analysis to what is reported by local informants.
- Because of the use of "participatory-type" methods, RMA's tend to raise expectations among the population about programme activities. Goals must be carefully explained from the outset to avoid misconceptions.
- Farmers, development projects and governments often tend to concentrate their efforts on the production side only and neglect the absorption capacity of the markets. This often leads to situations where markets are saturated and small producers start competing for a smaller and smaller portion of a limited market sector. Producers rarely ask their clients how they could improve or change their products and therefore seeking new markets.
- In some cases, there is an overlap between knowledgeable observers and key informants, who typically have a stake in the study. Such key informants may be able to look beyond their personal interests and views to provide a system perspective.
- In a broader scope, research must analyse the changing strategic role of marketing in the development process. In order to understand market systems, quantitative information is usually required. Market experts such as traders generally have a good arithmetic ability and can communicate numerical terms very easily. In the heads of traders there is usually a wealth of market information (Helvetas, 2002).

III.1.4 References

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III.2 Geographical mapping

Why is geographical mapping useful to an ICCO employee?

When entering a new region to stimulate private sector development, it certainly pays to first analyse the regional economic situation and business climate. Based on this information, one can select an analytical approach that requires minimal investments.

However, an analysis can be costly, lengthy and very detailed or quick, fast and partial. If the results are very uncertain, it is not efficient to invest a lot of money in a detailed and deep analysis. Therefore a quick and partial analysis, such as geographical mapping, allows you to act on the basis of what you *do* know about the region's business climate and local economic situation and prevents risks such as:

a) investments and developments do not have the desired effect or have been lost,
b) farmers and entrepreneurs lose interest in participating,
c) advisors or advisory institutions will lose confidence (Joss et al 2002).

III.2.1 Why is geographical mapping important?

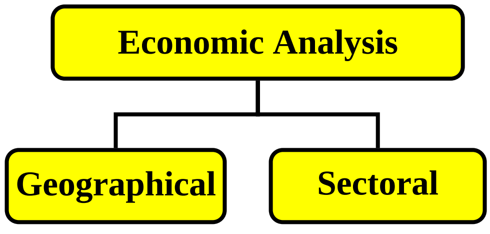
Geographical mapping (or geographic analysis) focuses on a particular geographical or spatial area for economic analysis and its interventions are often designed with a specific geographical focus. It gives the user more insight into the constraints or possibilities in a certain locality, city or region. The geographic mapping can be performed in an extensive way but also more rapidly using the rapid appraisal explained in the previous chapter.

The choice of sector development versus territorial development is part of a traditional bipolar discussion in many countries. Sector development is about priority policies towards certain economic sectors that should act as engines for national economic development. Backward regions with little or no economic activities belonging to these "chosen" sectors could receive subsidies to survive and preferably grow (Posthumus, 2006). Territorial development is related to integrated development of a region or locality by creating conditions for sustainable economic growth. The territorial development paradigm is about relying on endogenous factors and actors as well as about being competitive compared to other regions or localities or even countries and therefore interesting for external investments.

The described methodologies in this chapter are more or less suitable for different (needs in) regions. It offers a first step to obtaining more information on the region or locality. This kind of analysis might be followed by more detailed analysis in order to obtain subsector specific (Chapter III. 3) or value chain specific (Chapter III.4) information.

III.2.2 What is Geographical mapping?

Geographical mapping is a method that analyses the regional economic situation. Geographical mapping is one of the two economic analysis commonly used to gather more information about the economic environment (Posthumus (2006). The other analysis is the **sectoral analysis**. The subsector analysis and the value chain analysis (described in Chapters III.3 and III.4) are parts of the sectoral analysis.



Geographic mapping of RAAN and Zona Seca region of Nicaragua

In 2002, ICCO initiated a new programme on sustainable economic development for Nicaragua. Before defining its intervention strategies and approaching new partners, it was considered important to conduct an analysis of the current economic activities of the intervention area. First ICCO collected existing information on the national governmental plans for economic development and its national poverty alleviation strategy. Based on this information, ICCO decided to focus its programme stimulating the links between rural activities and urban demand, including the possible relationship with the processing industry. Also, two specific intervention areas were selected, the RAAN area and the Zona Seca, a dry rural area in the north of the country.

At this stage, ICCO initiated a tender procedure to contract experts to help it conduct a geographic economic analysis. The aim of the study was to identify prosperous agricultural sectors within the two areas offering economic growth opportunities for small-scale farmers. As a result, a local and a foreign expert were selected to elaborate this study. They collected information on the main agricultural activities, their links with small-scale farmers, other actors involved, related governmental policies and development initiatives and market development trends.

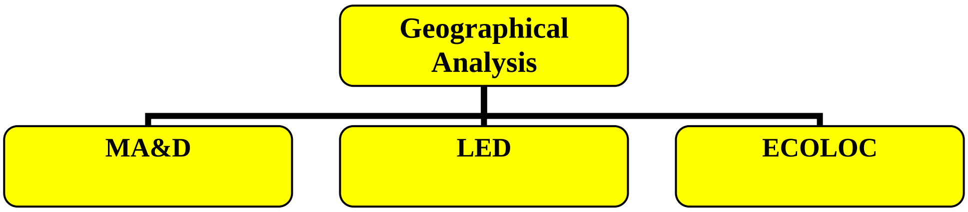
Based on this analysis, the first 10 sectors with growth potential were selected. For these sectors, more detailed subsector analysis were elaborated, which allowed ICCO to select the 5 sectors that fitted best with the development goals of its programme. The main selection criteria for this second analysis were: the importance of the sector for small-scale farmers and existing market opportunities. The 5 sectors selected were sesame, cocoa, cotton, (processed) fruits, non timber forest products.

The study helped ICCO obtain up to date information about the region's economic development initiatives and perspectives, without depending on specific development initiatives already being developed in the regions. The involvement of the local consultant from the start of the programme helped establish good relations with local government representatives. The involvement of the foreign experts allowed more critical reflection and prevented local bias. The study helped ICCO relate its own intervention strategies to local policy plans, which enabled it from the start to support chain development initiatives as well as initiatives to improve the enabling environment of the selected sectors.

For more information: ICCO programme officer Nicaragua.

In the field of geographical mapping three specific methodologies have been developed; market analysis and development (MA&D), local economic development (LED) and ECOLOC (Posthumus, 2006). These three methods focus on a specific geographical area, but each has its own importance. MA&D for example is more focused on income generating activities and sustainable maintenance of natural resources, while ECOLOC is focused on public and private partnerships. These methodologies are useful for agents of development cooperation programmes, as they facilitate the initial selection of intervention strategies to be used in a specific development region of interest. Due to their importance, this chapter focuses on the description of these methodologies[9].

[9] More information on each methodology can be found in the SNV Reference Guide on Economic Analyses.



III.2.2.1 Market analysis and Development (MA&D):

MA&D is more focused on income generating activities and sustainable maintenance of natural resources. The method has been developed by the Food and Agriculture Organisation (FAO) with the support of the Regional Community Forestry Training Centre (RECOFT) in Thailand and SNV Netherlands Development Organisation in Nepal. A field manual has been developed to guide facilitators who will assist people in conducting the MA&D process.

The main challenge for natural resource based enterprise development is to achieve sustainability of both the resource and the income derived from the resource. The MA&D methodology integrates conservation of the resources with income generating activities. The underlying assumption is that communities and forest users will feel more motivated to conserve and protect forest resources if they receive the economic benefits from sustainable forest use.

The goal of MA&D is to assist local people in developing sustainable income generating activities while conserving natural resources. The objectives are to strengthen the capacity of entrepreneurs to:

- Identify and assess opportunities and constraints in the market system in order to shortlist a range of most viable products and design effective strategies;
- Develop a business plan and implement an enterprise.

The MA&D methodology is mainly intended for use at grassroots level to help (potential) entrepreneurs develop income-generating activities. MA&D has been used as a follow-up to social mobilisation processes through group formation. The methodology has been instrumental in supporting group members to move from social development to economic development by taking into account market, environmental, social, institutional and technological issues. Facilitators will assist local communities in conducting the MA&D process. These could come from the private sector, the government or from NGOs that support sustainable development of enterprises.

III.2.2.2 Local Economic Development (LED)

Basically LED is about the creation or enhancement of a business-enabling environment in the locality. The key element in local and regional economic development policies is the willingness of relevant private and public actors to cooperate. You need people with vision and an open mind, not hindered by political or cultural preferences or distrust and who are willing to think and act around the strengthening of the local/regional economy. One of the main pre-conditions is the presence of a local entrepreneurial culture which will carry this economic development in a sustainable manner.

A local entrepreneurial culture can be defined as an environment in which there has been a tradition of small and medium sized entrepreneurs in one or more specific (sub)sectors. Elements that characterise such an environment are:

- ✓ Strong confidence in its own strength
- ✓ Individual entrepreneurial pride
- ✓ Distrust of (local) authorities interfering with their business.

The LED methodology or policy can be applied whenever there is room for political decentralisation, with a few basic conditions, which are:

1. A certain agro-ecological coherence and a common awareness of structural problems related to the development of the locality or region
2. Presence of local leaders with vision and an open mind
3. A (small) professional team of experts in the locality to facilitate the process
4. Absence of profound political or cultural-ethnic contradictions.
5. A local entrepreneurial culture

Both public authorities and relevant private economic actors are involved in an LED. They have to reach consensus on the scope, expected results, responsibilities and methodologies applied in this process. Secondly, attention is directed to local entrepreneurs to participate actively in discussions and eventually in the approval and implementation of the process. NGOs and other support institutions must also be willing to participate and act according to the defined results (e.g. a local training institute adapting its curriculum to the needs exposed by local entrepreneurs). Finally, national governments must be willing to listen to the demands made by local or regional economic (public-private) platforms with respect to facilities that are indispensable for LED enhancement, such as infrastructure, security, legal rights, etc.

III.2.2.3. ECOLOC

ECOLOC is a methodology that, broadly speaking, aims at reviving local economies in developing countries by making a local economic development plan based on locally available data. In 1997, the Club du Sahel and the Municipal Development Programme (MDP) for West and Central Africa launched ECOLOC in order to support the current decentralisation process in the region. The methodology was designed for second-rank cities in the national urban hierarchy, either by population (between 100,000 and 300,000) or by their function as regional capitals. ECOLOC kicked off with a series of pilot studies on the economies and hinterlands of 8 second-rank cities in West Africa.[1] These case studies showed that it is indeed possible to produce a realistic and exhaustive description of the local economies and their links with other economic areas at a reasonable cost and speed. The ECOLOC studies not only comprise economic analyses but take into account the spatial, temporal and social dimensions of development (Posthumus, 2006).

As ECOLOC is designed to support government programmes and to strengthen local entrepreneurship, both the local public and private decision makers must have a genuine interest in order for ECOLOC to help building consensus on the strategy to follow. This means that study should not be started during a pre-electoral period when very little municipal authority is implemented. Once the need to set up development strategies and strengthen local entrepreneurship has been expressed by the local public and private decision makers, ECOLOC helps build consensus on the strategy to be followed. Local public and private actors must have sufficient information on their environment to be able to define leverage points that can improve the competitiveness and quality of the social services within their local area. What is needed is a shared future vision based on objective information to arrive at a sustainable local development strategy.

III.2.3 Methodologies for Geographical mapping

III.2.3.1 Methodology for Market Analysis and Development

The methodology of MA&D consists of three phases (Posthumus 2006):

Phase 1: Assess the existing situation
Phase 2: Identify products, markets and means of marketing
Phase 3: Plan enterprises for sustainable development

Figure 6 and Table 1 illustrate the three phases. Table 1 indicates the specific steps and outputs of each phase. Figure 6 shows how the entrepreneur starts by considering a wide range of possible products and gradually reduces them through a filtering process to a few highly potential enterprise ideas.

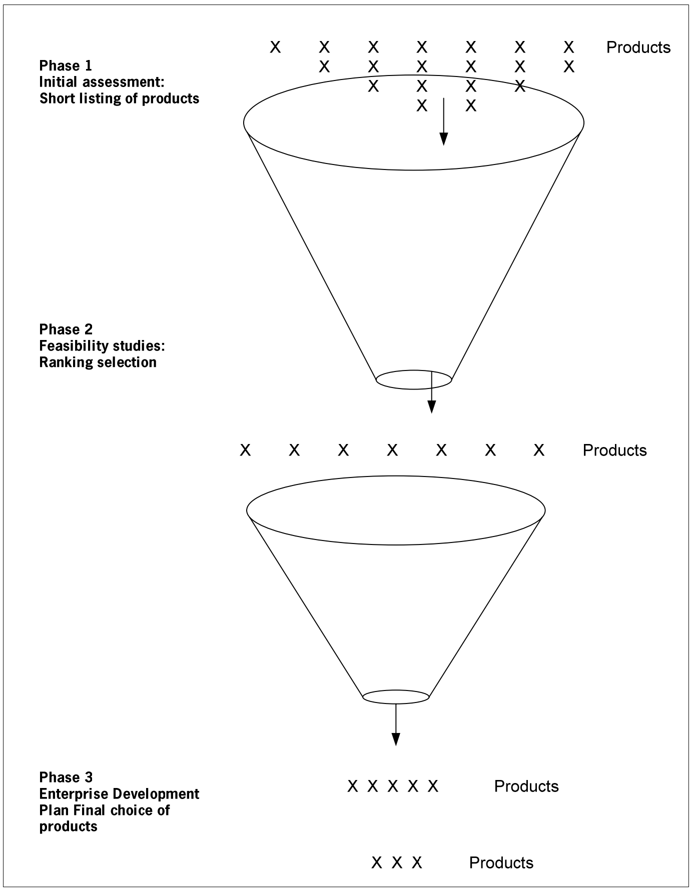


Figure 6: The Process of Market Analysis and Development
Source: Posthumus, 2006

Table 1: MA& D steps.

Phase 1	Assess the existing situation
Steps	1. Identify the target group 2. Determine the financial objectives of the target group 3. List existing resources and products 4. Identify key constraints of the existing market system 5. Shortlist a range of products 6. Raise awareness of the benefits of working together
Outputs	✓ A list of products to be evaluated in the next phase of MA&D ✓ Understanding the constraints of a range of products for the four areas of market, social, environmental and technical enterprise development ✓ A team of target group members formed to undertake Phase 2
Phase 2	**Identify products, markets and means of marketing**
Steps	1. Analyse the four areas of enterprise development (market, ecology / environment, social /institutional and technology) 2. Select the most promising products 3. Create interest groups for the selected products
Outputs	✓ The most promising products and information for the business plans identified ✓ Interest groups formed for the selected products to undertake Phase 3
Phase 3	**Plan enterprises for sustainable development**
Steps	1. Examine the business environment of the selected products and enterprises 2. Define the mission, goals and objectives of the enterprise 3. Develop strategies in each of the four areas of enterprise development 4. Formulate action plans to implement the strategies 5. Make financial projections for the enterprise 6. Obtain financing, as specified in the capital needs statement of the financial plan 7. Initiate pilot phase and training 8. Monitor progress and deal with change
Outputs	✓ An enterprise strategy for the selected products formulated ✓ An action plan developed ✓ Specified capital needs financed ✓ A monitoring and planning system implemented

Source: Posthumus, 2006

III.2.3.2 Methodology for LED analysis

There are many approaches and methodologies on *how* to implement a LED analysis. According to Meyer-Stamer[10], many LED methodologies have their origin in developed countries and more discussion is needed to prove their replicability in developing countries.

The different dominant approaches to LED implemented by developing country governments (national and local) and donor agencies are the following:

a. **Strategic planning of local development**; frequently used in Latin America. This method is characterised by high costs and high level of required skills.

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[10] idem

b. **Creation of Local Economic Development Agencies** (LEDA) as promoted by the ILO; institutionalised public-private cooperation, mostly implemented from "above".

c. **Cluster promotion policies**; promoting market-oriented cooperation of sector related local and regional entrepreneurs to reach higher levels of competitiveness, reducing market failures. Chambers of Commerce and Trade Promotion Organisations often opt for such promotion policies.

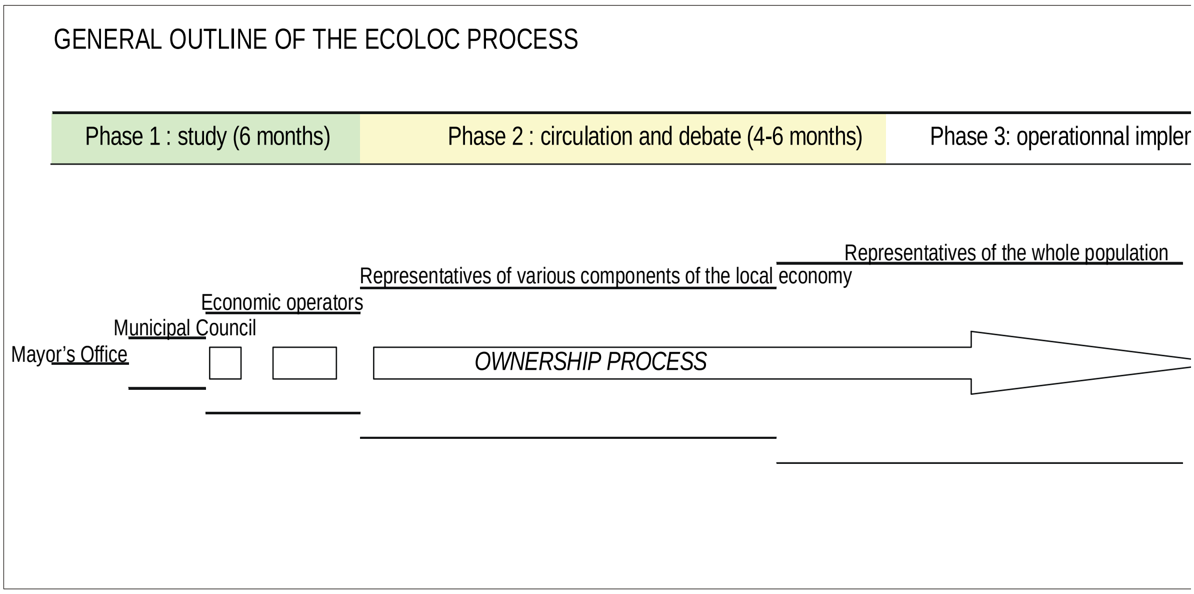
d. **Participatory Appraisal of Competitive Advantage** (PACA), a GTZ introduced approach from a bottom-up, pragmatic and immediate action-oriented concept.

Although each methodology has specific distinctions, there are some common denominators that each method takes into account. One of them is that *both public authorities and relevant private economic actors are involved* in an LED analysis. They have to reach consensus on the scope, expected results, responsibilities and methodologies applied in this process (For more information on LED see also Chapter V.6. Cluster development and strategic alliances for local economic development).

The methodologies mentioned have been applied in different places, but a comparative impact analysis has not yet been made. American countries have been executed by ECLAC-GTZ (Aghón, Alburquerque & Cortés, 2001) and analysed by Bert Helming (ISS, The Hague)[11]. There is an on-going debate regarding the conditions under which an LED could be started and be successful[12], e.g. the critical mass of a locality (number of inhabitants) and its relevant economic actors.

III.2.3.3 Methodology for ECOLOC

ECOLOC can be defined as a methodology that processes locally available information and turns it into an operational decision-making tool in the form of a local economic development plan. Its main aim is to contribute to the current discussion on the definition of decentralised or localised development strategies. The emphasis is on the monetary side of poverty alleviation, or more precisely the activities, income, transfers and expenditure of households, private operators and local authorities. Due to the participatory design of the methodology, it stimulates local ownership and builds capacity by creating new forms of collaboration between local actors and promotes the exchange and transfer of (local) knowledge.



[11] "Partnerships, Meso institutions and Learning; New regional and local economic development initiatives in Latin America", Bert Helmsing, ISS, June 2001.

[12] See: "Why is Local Economic Development so difficult? Draft for discussion " (Meyer-Stamer, April 2003)

Figure 6: General Outline of the ECOLOC Process
Source: Posthumus, 2006
The ECOLOC methodology consists of three partially overlapping phases (see Figure 7):

1) A study phase (4-6 months);
2) A dialogue and consultation phase (4-6 months);
3) A revival-of-the-local-economy-phase (by nature this phase has no limit in time).

(1) The ***study phase*** starts with a preliminary analysis as a first output. This phase aims to conclude with the delivery of a set of coherent data on the local economy, its local actors, issues and trends. These data must be presented in quantitative, qualitative and spatial terms, summarised in a reference document called: *Profile on the local economy*.

(2) The second phase of ***dialogue and consultation*** leads to the adoption of strategic guidelines for local development, the so-called *Local Development Framework*. This framework can be considered as a policy that should ultimately make it possible to:

- Define coherent action programmes;
- Mobilise the local and external financial resources, as well as the human resources, needed to implement these programmes;
- Identify local coalitions with stable consultation frameworks including democratic procedures.

This phase is facilitated by the local authority supported by the research team and is designed to widely disseminate the knowledge gained in the study, compare it with the perceptions of local people and enable the various components of local (civil) society to express their opinions and expectations for local economic development.

(3) The goal of the third phase is the actual ***revival of the local economy*** by implementing the adopted policies and the affirmation of local autonomy and political will to manage the local economy. It must clearly mobilise all actors for practical action.

The availability of directly accessible and applicable local data, both in terms of quality and quantity, as well as recent, current or planned urban or regional projects that may have a huge impact on the city and its hinterland, add to the success of the process. The latter can be a good source of information and its budget might be mobilised to finance the study.

III.2.4 Points of attention for Geographical mapping

1. MA&D has been specifically designed for forestry communities to generate income while conserving tree and forest resources. To find this balance is not easy and even more difficult in situations where nature conservation has few or no opportunities for the local communities to be combined with income generating activities.
2. Stakeholders need to be interested. In the case of LED, attention is directed to local entrepreneurs to participate actively in discussions and eventually in the approval and implementation of the process. NGOs and other support institutions must also be willing to participate and act according to the defined results. Finally, national governments must be willing to listen to the demands made by local or regional economic (public-private) platforms.
3. To execute an LED analysis successfully, you need people with vision and an open mind and the presence of a local entrepreneurial culture which will carry this economic development in a sustainable manner.
4. Discussions on decentralised approaches to economic development include the concern of the difference between local and regional economic development (RED). It is difficult to define the critical size of an economic area to reach a spin-off after an intervention programme. In addition, there is also a common point between localities and regions in relation to the national level; the first two cannot influence key

variables of economic development, such as interest rates, exchange rate or foreign trade regimes. So, there is no real difference between “LED” and “RED” and a given type of intervention programme may thus be used at both the local and the regional level.

5. To apply ECOLOC genuine interest by the local authorities is required.
6. The decentralisation process of ECOLOC requires that local actors (mayors, civil society) possess information about their economies. At present, statistics are mainly produced from a national point of view

III.2.5 References

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III.3 Subsector Analysis

Why is subsector analysis useful to an ICCO employee?

If you need to start from scratch in a region where ICCO is introducing a development programme on improving the market access for small holders, the subsector analysis offers a hands-on method with clearly described steps to follow to develop more insight into the (sub) sectors and the growth potential of the chosen area.

A subsector analysis reveals a lot of information about the specific economic activities of a number of subsectors in a selected area. The information that is gathered according to the relevant criteria for the programme can serve two purposes. On the one hand it can be used to make a suitable selection of a high potential subsector or the investment opportunities within a subsector. On the other hand, an SSA can be used to assess certain reforms that have been made. A subsector approach requires a structure, conduct and performance model and gives insight into the organisation, behaviour and performance of a subsector. By studying these over time, the impact of certain policy reforms on certain subsectors can be assessed (Holtzman 2002).

III.3.1 Why is subsector analysis important?

If interventions into markets are to have maximum impact and yet be cost effective, key points of leverage must be identified. A useful tool for identifying such opportunities is subsector assessment (SSA). The SSA can be used for this type of research, because it clearly illustrates where change can have the most significant impact on the subsector (Land and Uliwa 1997, Boomgard et al 1986).

SSA is a well known methodology for Small and Medium Enterprises (SMEs) programme design. Small and medium enterprises can play an important role in economic development strategies. This was recognised in the early eighties and there was a growing demand for operationally useful small enterprise research, fed by concerns of equity and evidence of small enterprise efficiency (Boomgard et al 1986).

The objective of a Subsector Assessment (SSA) is to analyse all of the participants, their links and influential factors in the agribusiness system in order to identify constraints and opportunities for growth. SSA is a powerful tool for project designers and decision-makers because it clearly illustrates where change can have the most significant impact on the subsector. While the more generally oriented economic mapping approach (as described in Chapter III.2 Geographical mapping) a subsector analysis brings us one step closer to the identification of a potential intervention area on sustainable economic development. A next step could be a Value Chain Analysis (Chapter III.4) (Posthumus 2006).

Also, a subsector analysis can be used for comparative static analysis, examining the implications of alternative development patterns, policy change or project interventions. It goes beyond more traditional economic impact assessment where the impact is measured by comparing the welfare of producers and consumers before and after the implementation of the programme.

III.3.2 What is a subsector analysis (SSA)?

A **Subsector** is defined as a vertical grouping of enterprises involved in the production and marketing of one well-defined product or several closely related products. The network of firms supply raw material, transform them and distribute finished goods to a particular consumer market (Miles, 2004, Haggblade and Gamser 1991). To avoid confusion about sectors, subsectors and supply chains, Figure 7 might be helpful. For example; a sector can be ‘horticulture’, the subsector ‘fruits’ and a value chain (or supply chain) ‘bananas’.

Subsector

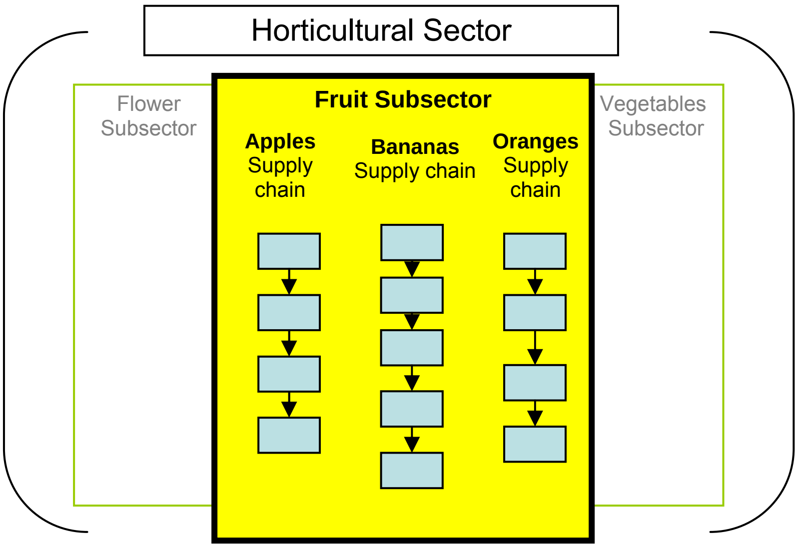

Figure 7 Focus of the subsector analysis (simplified)

SSA assumes that SMEs operate within a larger production, distribution and marketing system. To develop appropriate interventions and to promote growth of SMEs, it is necessary to look at the whole subsector, including larger firms, the different channels and the related competitive relationships (Miehlbradt and McVay 2005, Posthumus 2006, Shaffer 1973). The scope and comprehensiveness of an SSA is exactly what makes it unique. The research area is defined to include both the vertical (for example between farmer and trader) and horizontal relationships[13] (for example among fertiliser companies themselves) in a significant part of a sector and is worked out in a number of clear steps (Land and Uliwa 1997, Shaffer 1973).

The *subsector analysis* is a systems approach. In a systems approach the different components of a system will act differently when isolated from their environment or other parts of the system. Systems thinking is about gaining insights into the whole by understanding the links and interactions between the elements that comprise the whole "system". The elements are affected by the environment in which they exist. Regarding the subsector as a system also means that a change in one area of a system can adversely affect another area of the system. It thus promotes organisational communication at all levels. System thinkers consider that:

- A system is a dynamic and complex whole, interacting as a structured functional unit
- Information flows between the different elements that compose the system
- Information flows from and to the surrounding environment via semi-permeable membranes or boundaries

An important aim of a subsector analysis is to analyse all the participants, their links and influential factors in one or more agribusiness systems in order to find out where to direct the limited resources to obtain the best match between the programme intervention objectives and the existing sector development opportunities in the intervention area. Secondly, the analysis can be useful to assess the impact of policy reform on the subsector. Furthermore, an SA can be useful to identify policy interventions.

[13] Vertical and horizontal chain relationships are further discussed in Part IV on Chain integration strategies

A subsector analysis includes producers, traders, processors, importers/exporters, consumers and other important participants in the subsystem and identifies the different channels within the overall subsector and then looks at the competitive relations between those channels (Miehlbradt and MacVay 2005). The fundamental basis of a subsector analysis is built on four key concepts. Together, these lead to a schematic search for growth opportunities and performance improvements in the subsector, see Figure 8 (Land and Uliwa 1997, Posthumus 2006).

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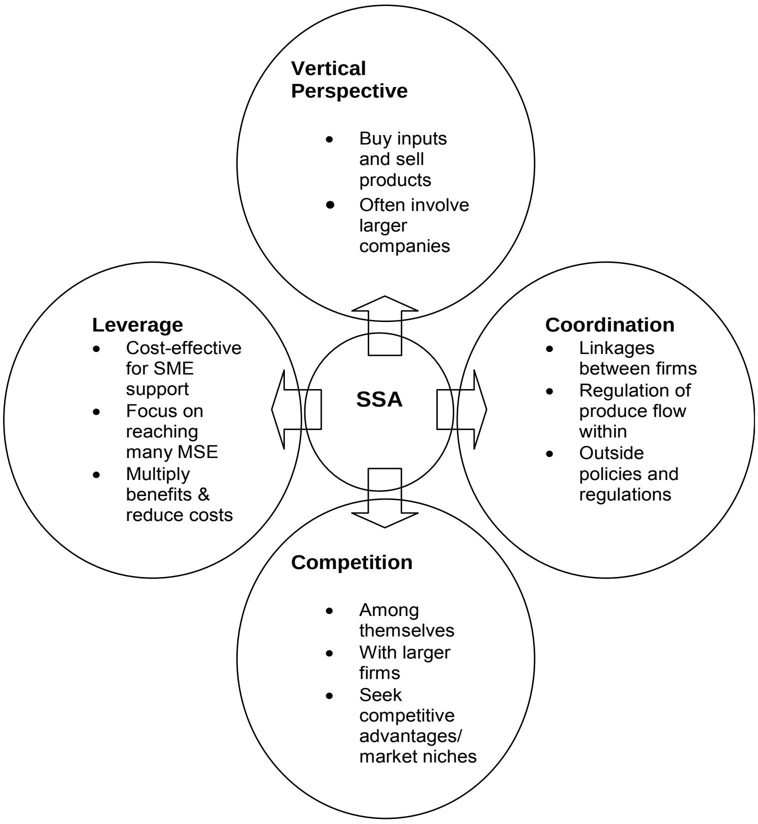

Figure 8: Basic concepts subsector analysis
Source: Posthumus, 2006

1. ***Vertical perspective.*** Most small businesses work in vertical supply chains. They purchase inputs and market output through others, often through larger firms. This vertical perspective is an important element of the assessment because it shows who the subsector participants are and illustrates where they function in the marketing system (Land and Uliwa 1997, Miles, 2004).
2. ***Competition.*** Small firms compete among themselves and they compete with medium and large firms using different technologies. Understanding one's competitors, domestic and international, can shed considerable light on the problems in the subsector, as well as illustrate the techniques that successful enterprises are using (Land and Uliwa 1997, Miles 2004).
3. ***Coordination mechanism.*** Coordination defines how firms within the subsector are linked and how they affect one another. It examines the impact that participant actions have on the various aspects of the subsector. These actions can be formal, such as government policies and regulations or informal, such as internal self-regulating mechanisms (Miles 2004). Uncertainty in agricultural production, the perishable nature of agricultural commodities (limited storage and shelf lives) and increasingly stringent quality and phytosanitary requirements are strong incentives for subsector participants to devise effective coordinating institutions and arrangements (see also Part IV)

4. **Leverage.** Leverage is the ability to affect large numbers of subsector participants with the least action. Subsector assessment aims to find cost effective opportunities where this aim can be accomplished. These are known as points of leverage. The point of leverage can be a starting point to access credit, a law that is preventing access to or expansion of a subsector, or a new technology that would dramatically improve production capabilities (Miles 2004).

III.3.3 Methodology for undertaking a subsector analysis.

Subsector assessment is an iterative process. Subsector information to consider can be collected from interviews, surveys and/or workshops with key informants who have good general knowledge of the local economy. This primary data can be supplemented with secondary data from sources including government agencies, donors, financial institutions and other development organisations. Multi-lateral agencies are also a good source for country-specific data on various industries and sectors[14]. Small Enterprise surveys, if they exist, can also provide a wealth of information about different subsectors and assist in ranking their relative attractiveness for business service development programmes (Land and Uliwa 1997, Posthumus 2006).

Throughout the assessment the following questions must be considered:

- ✓ Who are the key players in the industry?
- ✓ What channels exist and which ones are growing faster?
- ✓ What is helping or impeding this growth?
- ✓ Where do opportunities exist for future growth and expansion?

The procedures detailed here are intended as a basic guide. The description is based on the 'classical GEMINI approach' from Land and Uliwa 1997[15].

Establish Initial Understanding
Step 1. Define subsector for study
Step 2. Familiarisation with the subsector
Step 3. Draw preliminary subsector map
Step 4. Specify the environment affecting participants
Refine Your Understanding
Step 5. Refine the subsector map
Step 6. Quantify overlays of particular interest
Identify Leveraged Interventions
Step 7. Analyse dynamics
Step 8. Identify sources of leverage
Step 9. Explore opportunities for leveraged intervention

Step 1. Select subsector for study.

The objective is to identify subsectors where intervention will yield the highest pay-off. The first step is to make a list of subsectors. If this information does not yet exist, it can be gathered by conducting interviews, surveys and/or workshops with key informants. Drawing the selection criteria is an important step in the programme design. It depends on the aims of the agency executing the SSA what criteria will be taken into account (MDF, 2005). For example, some development organisations primarily base their selection criteria on growth potential but the criteria will probably differ if the selection of a subsector is based on (Boomgard et al 1986)

a) where you want to create employment (rural or urban areas),
b) the percentage of people involved in a sector,

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[14] The websites of the International Trade Centre of the UNCTAD/WTO (www.intracen.org/menus/countries) and the World Bank (www.worldbank.org/html/extdr/regions) are two examples.
[15] For a more detailed description of these steps the paper by Theresa Miles (2004) can be consulted.

c) the main focus of an area/whether there are other possibilities.
For more detailed examples of criteria, see MDF 2005 (p.2) and Holtzman (p. 7-8).

Step 2. Introduce yourself to the subsector.
The goal is to describe the supply chains in which SMEs participate, to understand how the overall production and distribution system are linked. Therefore, it is recommended that analysts read everything valuable about the subsector and, above all, visit participants and observing their operations.

Step 3. Draw a preliminary subsector map.
The map summarises the initial understanding of the subsector and, although conceptually simple, it is a powerful tool for describing the knowledge acquired about a set of related business activities. It identifies the subsector's principal functions, participants and channels. An example of such a map is presented in Figure 9. Drawing a preliminary subsector map is a useful exercise to think through the different stages of the subsector and product, financial and information flows.

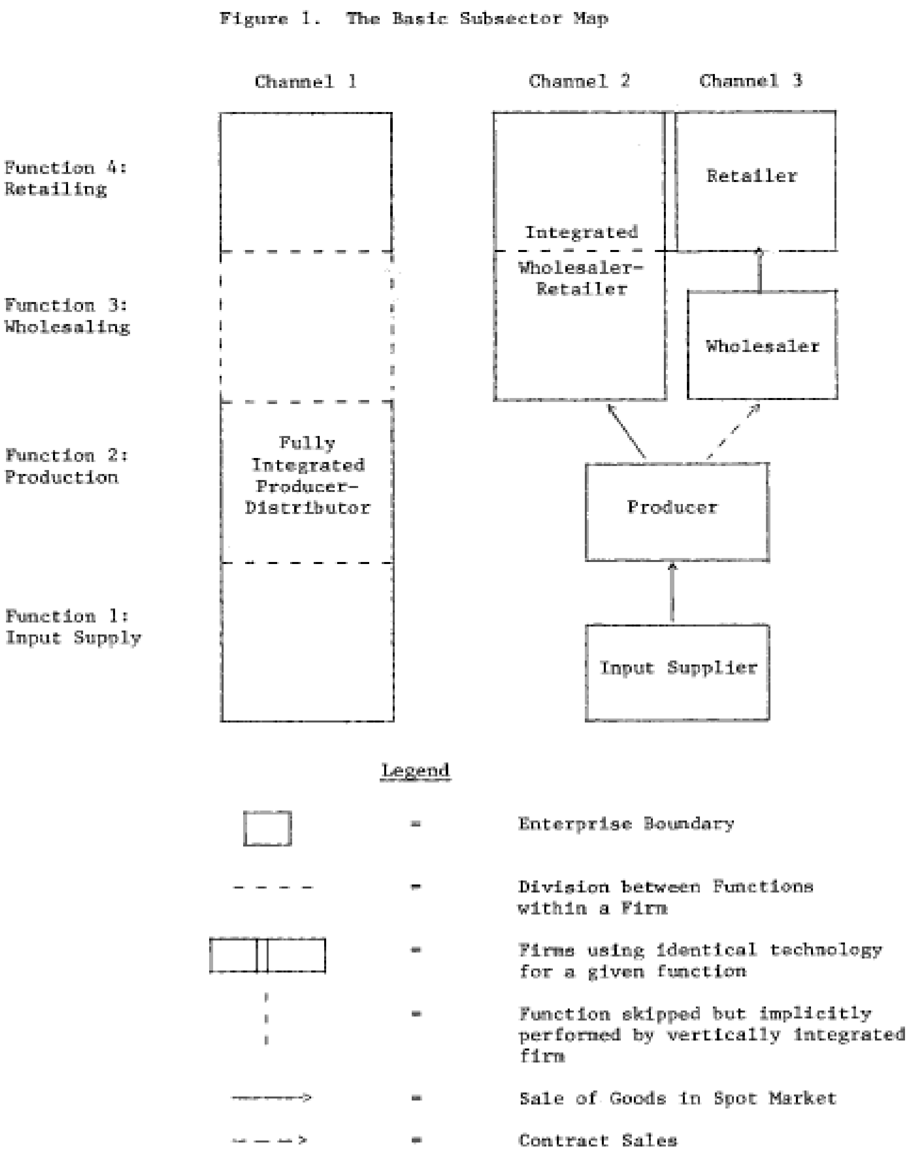

Figure 9: Subsector map
Source: Boomgard et al 1986, p 4-5

Step 4. Specify the regulatory and institutional environment affecting participants.
The environment in which participants operate includes the rules affecting firms in the subsector as well as the organisations that exist to support them. The rules may be formal or informal and the support organisations and programmes may cover a range of different groups. The output in this step is an improved understanding of the way the business environment affects the dynamics and competitiveness of different channels.

Step 5. Refine the subsector map.
To refine the understanding of subsector flows, ambiguities and uncertainties revealed by the preliminary subsector map must be cleared. The procedure is to target the second round of interviews at segments of the subsector map where your understanding is least clear. The improved understanding will help to revise and simplify the preliminary map.

Step 6. Put quantitative data into the subsector map.
The basic subsector map can serve as a foundation supporting any number of quantitative overlays. These overlays summarise information in a way that is easy to understand. Although any data can be displayed as an overlay, they most commonly relate to size, income and its distribution, efficiency, leverage and target groups. If data are available for quantifying the numbers of firms and the product throughput at each stage, this is useful information that can help the analysts and the client understand where market power and subsector control is likely to be concentrated. (See Miles, 2000 and Haggblade and Gamser, 1991).

Step 7. Analyse dynamics.
This step is vital for moving from analysis to action. By understanding how the subsector is changing, the opportunities and pitfalls will be revealed. Deeper understanding of the forces driving this change often reveals the key opportunities for SME growth.

Step 8. Identify sources of leverage.
Leveraged interventions are those that influence large numbers of small firms at a single stroke. Sources of leverage can be identified by looking for system nodes, points where large volumes of product pass through the hands of a few actors, geographic clustering or policy constraints.

Step 9. Explore opportunities for leveraged interventions.
To determine which interventions offer prospects for leveraged delivery, the convergence between the opportunities for intervention and the available leverage can be explored.

III.3.4 What are the points of attention when using a subsector analysis?

1. Defining clear assessment and selection criteria before the start of the SSA helps compare different potentially interesting subsectors in a specific region in a more objective way. The defined criteria will help the ICCO programme coordinator compare the results of the SSA for the different sectors and select the sector(s) that fit best with the programme objectives.
2. To commit stakeholders and ensure follow up the aim of the subsector analysis, i.e. to generate more income through a development programme, it is important to use the internal staff of a potential implementer of the programme as main SSA analysts (Land an Uliwa 1997).
3. The use of local key informants is strongly recommended. A critical condition for a successful project design as well as implementation is the early commitment of local organisations with a stake in the subsector. These organisations can range from farmer co-ops and NGOs to trade associations, but they must play a substantial role in the subsector and be involved in the implementation once the assessment is done (Miles 2004).

4. Subsector studies require the interviewer to understand the research methodology in order to ask the right questions for the open-ended questions in the interviews (Boomgard et al 1986).
5. Capacitating Sector Analysis, CAPSA, is an attempt to develop a structural approach to this problem. It combines capacity building and sub-sector analyses to train participants in the general aspects of small enterprise development and provide them with a methodology and instruments to use in conducting a sub-sector analysis (Posthumus 2006).
6. There is no blueprint for a subsector analysis. Although steps as presented by GEMINI can be used as a good guideline, it might be necessary to adapt your steps to the local situation.
7. A subsector is part of domestic and international markets and as such understanding the markets is essential when performing an assessment (Miles 2004).
8. A subsector analysis can be applied in any environment where enterprises exist. However in an environment where small, medium and large enterprises co-exist, the SSA is more appropriate than in a state controlled economy (Posthumus 2006).

III.3.5 References

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III.4 Value Chain Analysis

Why is value chain analysis useful to an ICCO employee?

A value chain analysis can help an ICCO employee gain more insight into the constraints of developing a sustainable value chain. These insights should help ICCO solve chain development constraints together with ICCO partners. In this process, ICCO employees must take into account the importance of stimulating the chain development rather than directly intervening because cooperation in the value chain is crucial also when ICCO has left the picture again.

Value chain analysis addresses the nature and determinants of competitiveness and helps producers (whether at company, region or national level) to gain insight into their own and interconnected firms. The analysis and identification of core competences can allow the actors to outsource their weaker competences. Furthermore, the mapping of inputs and outputs gives a firm insight into what else has an impact on its success.

Value chain development can be used to give small enterprises access to the global market. Value chains are also used when chains have to deal with quality issues, new legislation, voluntary standards and labels. Quality issues, legislation, standards and labelling are all recent issues and developments that can be found in most sectors and markets. A value chain analysis is therefore a relevant analysis to execute.

III.4.1 Why is value chain analysis important?

It is not so much a matter of whether to participate in economic development processes, but how to do so in a way which provides sustainable income growth for poor people and poor countries. In these circumstances, policy needs to address processes of production and product development, including both intra-firm organisation and the relationship between firms. It also needs to address the ways in which poor producers and poor countries connect with producers and consumers in the global economy. Value chain analysis - which includes the whole chain of the organisation, production and delivery of products from inception to use and recycling - provides a tool to do so. A value chain analysis provides important insights into the policy challenges confronting both private and public actors. The focus is on all links in the chain and all activities in each link; by doing so it helps identify which activities are subject to increasing and which to decreasing returns.

There are three main sets of reasons why value chain analysis is important for poverty alleviation strategies:

1. With the growing division of labour and global dispersion of the production of components, systemic competitiveness has become increasingly important.
2. Efficiency in production is only a necessary condition for successfully penetrating markets, especially global markets.
3. Entry into markets which allows for sustained income growth requires an understanding of dynamic factors within the whole value chain.

Also, globalization does not only patch up market gaps and brings producers and consumers closer together; it also brings regional and international competition into local markets. For instance, any agricultural produce not consumed by the farmers' families is a product in the market (local to international) and competes today with products coming from nearby or far away. Therefore, all farmers offering their produce for sale are instantly part of a value chain. Reasons for a donor-funded project or program to intervene may include the following:

1. Some people need support for becoming actors in existing value chains.

2. More important than belonging to a value chain is the role people play in it, i.e. their negotiation power in the value chain.
3. Some actors are stuck in value chains that exploit low income possibilities. They require support to explore new opportunities.
4. By strengthening one actor in a value chain there is the possibility of creating competitive advantages for the whole system. In such a case a large number of people competing in local, regional or global markets can benefit from these advantages.

Finally, value chain analysis is important because it helps understand the advantages and disadvantages of firms and countries specialising in production or services. It also shows that the way in which producers are connected to final markets may influence their ability to gain from participating in the markets. A value chain analysis treats the whole cycle of production, including governing connectedness to final markets. This forces the analysis to consider not just the efficiency in the production link in the chain, but also those factors which determine the participation of particular groups in final markets.

III.4.2 What is a Value Chain Analysis?

The value chain describes the full range of activities required to bring a product or service from conception, through the intermediary phases of production (involving a combination of physical transformation and the input of various producer services), delivery to final consumers and final disposal after use.

The value chain is a concept from business management that was first described and popularised by Michael Porter in his 1985 bestseller, Competitive Advantage: Creating and Sustaining Superior Performance. The value chain categorises the generic value-adding activities of an organisation. The costs and value drivers are identified for each value activity. The value chain is regarded as a powerful analysis tool for strategic planning. Its ultimate goal is to maximise value creation while minimising costs.

The terms “value chain” and “supply chain’ are sometimes used interchangeably and are sometimes used to describe two different processes. Hobbs et al describe the differences as: “A supply chain refers to the entire vertical chain of activities, from (farm) gate to plate, regardless of how it is organised or how its functions”.

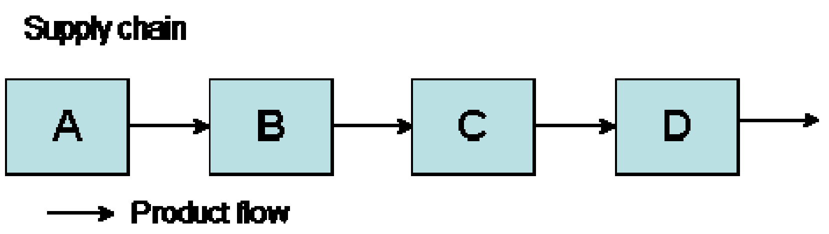

Figure 10: Basic design of the supply chain

A value chain is a type of supply chain: “the value chain refers to a vertical alliance or strategic network between a number of independent business organisations within a supply chain”. According to Hobbs et al. the independent members in a value chain recognise the need for each other, they share a vision, they share benefits and risks. Trust, (long-term) commitment and cooperation between value chains members are essential. A value chain is demand driven and is responsive to consumer needs. It should be taken into account that in real life value chains are always complex, with many links and with various producers probably being involved in more than one value chain (Kaplinsky and Morris, 2000).

Subsector analysis (see Chapter III.4) and value chain analysis are closely related and the definitions may be confusing. The tools, methods and procedures for both analyses can be very similar but the difference lies in the focus. A value chain looks at one market channel, while a subsector analysis identifies the different channels within the overall sector and then looks at the competitive relationships between those channels (Miehlbradt and McVay, 2005). For example, one can say that vegetable is a subsector and potatoes are a value chain. However, for this specific crop one can look within the value chain to different product-market combinations as the crop can be related to different market segments, such as fresh markets and processed potato for potato chips. Each of these segments has different requirements on pricing and absorption capacity and influences each other.

The systemic view of the approach integrates three important levels within a value chain network and allows discovering potentials and bottlenecks within these levels and in the dynamic interactions between them.

Value chain actors:	The chain of actors who directly deal with the products, i.e. produce, process, trade and own them.
Value chain supporters:	The services provided by various actors who never directly deal with the product, but whose services add value to the product.
Value chain influencers:	The regulatory framework, policies, infrastructures, etc. (at the local, national and international level).

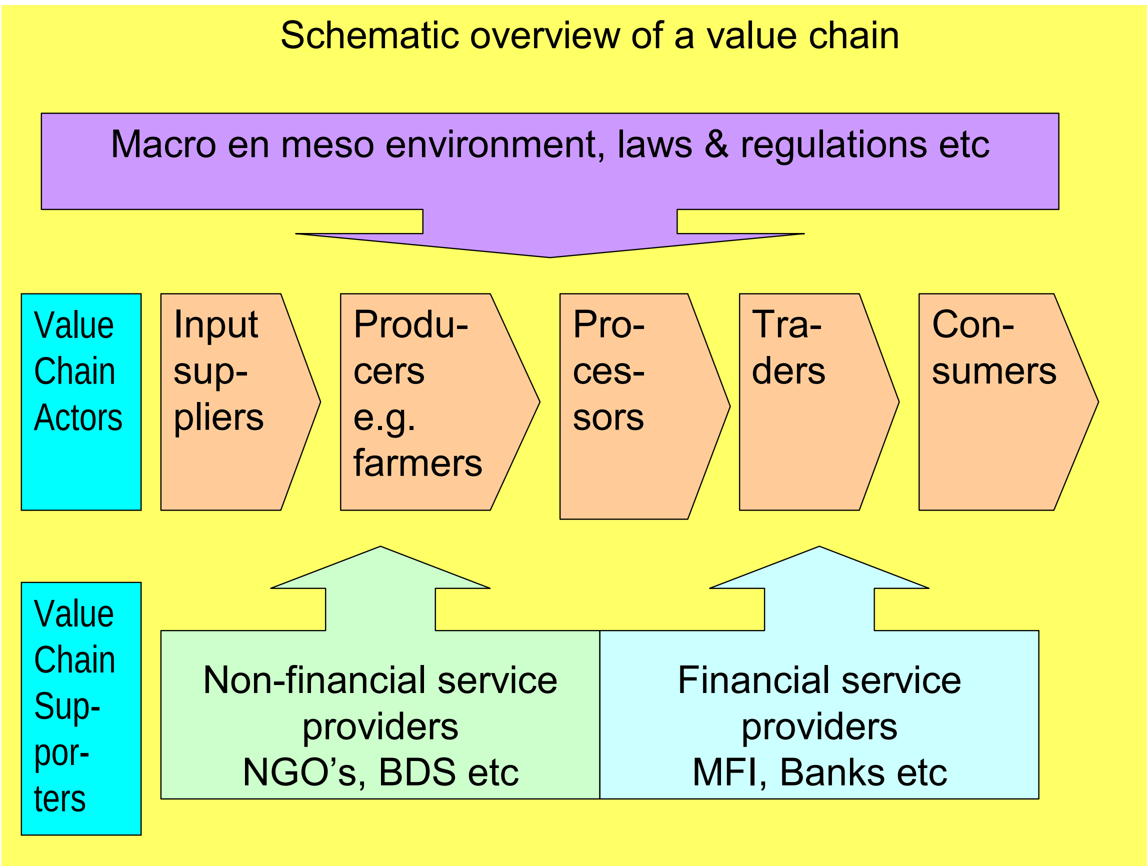

Figure 11: Basic design of the value chain

One important objective of a value chain analysis is to identify opportunities for sustained growth and income for the chain actors. Especially when wishing to enter the global market, it requires an understanding of dynamic factors of the whole value chain. Globalisation has had a positive effect on those who know how to enter the global market but not on those who lack that knowledge, skill or potential. Thus, in order to benefit from market development trends like globalisation, one needs to know how it works and what needs to be done. A value chain analysis is a helpful methodology for answering those questions.

Considered in this way, the value chain analysis framework can be considered as a tool to generate data and to provide important insights into the determinants of income distribution and the identification of effective policy forces to prevent a more unbalanced income distribution.

There are three important components of value chains which need to be recognised and which help create an analytical tool (Kaplinsky, 2000) and are explained in more detail below:

1. Value chains are "storehouses" for rents and these rents are dynamic
2. Effectively functioning value chains involve some degree of governance
3. Effective value chains arise from systemic as opposed to point efficiency.

III.4.2.1 Value chains are "storehouses" for rents

Economic rent is generally defined as the difference between the income in the current use and the absolute minimum required to draw into a particular use (from no use at all or from the next best use). Scarcity is an important factor in determining rent. The economic rent arises from unequal access to a particular resource, also known as "barrier to entry". But scarcity can be influenced and constructed. The entrepreneur plays a unique role in creating new ideas and possibilities by combining factors/resources differently. The amount of rent that the entrepreneur creates depends on the income from the new factor combination and the required costs to develop the new combination (adapted from Shumpeter, 1961). But this is not a static situation. Due to the introduction of a new combination, the entrepreneur receives a surplus that is called a producer rent. When this combination is copied, the producer rent decreases, prices fall and the innovation expands to the advantage of consumers. But all this stimulates the search for a new combination in the continual search for producer surplus.

In short, it can be concluded that;

1. Economic rent arises in the case of increasing productivity of factors (searched by entrepreneurs) and scarcity.
2. Most economic rent is dynamic in nature; rent decreases because of increasing competition.
3. The process of competition fuels the innovation which drives economic development forward.

What is the relevance of economic rent to small producers?

One can assume that economic rent can usually only be achieved by investing in the development of a new product or process. Small producers by definition do not have the resources to do this on their own account, so they would have to be supported in achieving this. If one supports small producers to create economic rent, two aims can be obtained. The first aim is that small producers achieve part of the economic rent and the second aim is that consumers obtain the product or service for a lower price. The losers in this process are the larger producers who now have lower economic rents (due to more competition), who might start looking for other opportunities to increase their producer rent.

Access of small holder quinoa growers to export market

Quinoa originated in the Andean region of South America, where it has been an important food for 6,000 years. Its name is the Spanish spelling of Quechua. Quinoa is generally undemanding and altitude-hardy, so it can be easily cultivated in the Andes up to about 4,000 meters. Even so, it grows best in well-drained soils and requires a relatively long growing season. The Incas, who held the crop to be sacred, referred to quinoa as “chisaya mama “ or “mother of all grains” and it was the Inca emperor who would traditionally sow the first seeds of the season using “golden implements”. During the European conquest of South America, quinoa was scorned by the Spanish colonists as “food for the Indians” and even actively suppressed, due to its status within indigenous non-Christian ceremonies. Quinoa is of great nutritional importance, being secondary only to the potato and followed in third place by maize. In contemporary times, this crop has become highly appreciated for its nutritional value due to its very high protein content (12%–18%). Unlike wheat or rice (which are low in lysine), quinoa contains a balanced set of essential amino acids for humans, making it an unusually complete foodstuff. This means it takes less quinoa protein to meet one's needs than wheat protein. It is a good source of dietary fibre and phosphorus and is high in magnesium and iron. Quinoa is gluten free and considered easy to digest. Because of all these characteristics, quinoa is being considered as a possible crop in NASA's Controlled Ecological Life Support System for long-duration manned spaceflights.

In Bolivia quinoa is mainly grown by small-scale farmers. The cooperatives Anapqui or CECAOT represent 1600 of these small-scale quinoa producers. Besides representation, the cooperatives also provide processing and sales services. The growing demand for quinoa in the international market has increased competition within the quinoa chain and the entrance of new actors, mainly providing services in storage, processing and sales activities. These initiatives are not always favourable for the position of the farmers within the chain. Consequently, Anapqui and CECAOT want to improve their position within the sector, to strengthen the position of their members in the chain. Since 2001, ICCO has supported Anapqui and CECAOT in improving its competitive position. Firstly, an external expert was hired to conduct an in depth value chain analysis. This analysis was carried out in a participatory way by mapping the current functioning of the chain based on interviews with the different chain actors. The information was subsequently used to identify the opportunities and constraints for each chain actor. It provided insights into the relationships between chain actors, the intervention strategies used, the importance of environmental management and the strengths and weaknesses of each actor. Based on this information, a SWOT analysis was conducted for each cooperative. This information helped the cooperatives identify the activities to be developed in order to help their members improve their competitive position in the chain.

For more information: Programme officer Bolivia

III.4.2.2. Effectively functioning value chains involve some degree of governance

Coordination of responsibilities in the different activities within a chain is required, especially with increasing complexities in the chain and increasing distance between production and final consumption. This coordination is not only important for logistic reasons, but also in relation to the integration of components into the design of the final products and involved quality standards.

It is possible to distinguish three forms of governance (Gereffi, 1998):

1. *Legislative governance*, which relates to the basic rules for participation in the chain. Examples: environmental and child labour standards.
2. *Judicial governance*, which relates to the need of auditing to check compliance with the basic rules. Examples: specialised firms monitoring conformance of ISO standards or labour standards.
3. *Executive governance,* which relates to a proactive governance providing assistance to value chain participants in meeting the operating rules Examples: specialised service providers or government industrial policy support.

Very often this distinction in types of governance is ignored, resulting in confusion about which party actually governs a particular value chain and a reluctance to recognise that other parties may engage in different forms of governance in the same chain. Building on these concepts of governance, Gereffi (1999) has made a very useful distinction between two types of value chains; buyer driven chains and producer driven chains.

Buyer driven chains are characterised by labour intensive industries such as footwear, furniture and toys. Usually retailers, marketers and branded manufacturers play the pivotal roles in setting up decentralised production networks in a variety of exporting countries, typically located in developing countries. Production is generally carried out by networks of contractors that make the finished goods in developing countries for foreign buyers. The specifications are supplied by the large retailers or marketers that order the goods.

In producer driven chain the key producers in the chain coordinate the various links. In these producer driven chains, transnational manufacturers usually play a central role in coordinating production networks, including their backward and forward links. This is characteristic of capital and technology-intensive industries such as automobiles, aircraft, computers, semiconductors and heavy machinery. Here producers take responsibility for assisting the efficiency of both their suppliers and their customers. In both buyer and producer driven chains, production is affected to a varying degree by the three forms of governance.

Recently, a more comprehensive theoretical framework for the identification and explanation of governance patterns in global value chains has been proposed by Humphrey and Schmitz (2004) and Gereffi *et al* (2005). The framework draws on three approaches: transaction cost analysis, production networks, and technological capability and firm-level learning. The main thrust of the theory is (1) that chain governance is located on a continuum between a markets situation (little governance) and a hierarchy situation (high governance combined with a high degree of vertical integration), and (2) that three variables determine that location: the complexity of inter-firm transactions, the ability to codify these transactions, and the capabilities of suppliers to meet requirements of buyer. Using these variables, five basic types of value chains can be distinguished (see table 2).The 'Captive', and 'Hierarchy' value chains are demand-driven; the 'Modular' and 'Relation' chains resemble most of what used to be producer-driven chains. The 'Markets' chain type tends to be the least driven.

Table 2: Typology of Global Value Chains

Global value chain type	Governance features
Market	Transactions easily codified, specifications relatively simple, and suppliers capable of producing the products. Little chain coordination required. Switching costs are low for both suppliers and buyers.
Modular	Suppliers make products to specifications of buyers. Modularity rises with increasing codification of specifications (through technical standards). Suppliers capable of internalizing tacit information. Coordination and switching cost remain low
Relational	Codification difficult, which makes interactions complex. Suppliers and buyers are mutually dependent because of complexity. Relational value chain governance is to be expected because a lot of tacit knowledge must be exchanged. Outsourcing is likely to benefit from capabilities of supplying firm. Mutual dependence regulated through reputation, social and spatial proximity, family and ethnic ties, etc.
Captive	Ability to codify and complexity product specification are high, but supplier capabilities low, then governance tends toward captive type. High degree of monitoring and control required of the lead company. Suppliers are dependent on buyers. The chain is 'captive' because switching costs for suppliers are high.
Hierarchy	Products are complex and specifications cannot be codified. Capable suppliers cannot be found, then core firms develop products in-house. Vertical integration. Dominant form of governance: managerial control, from managers to subordinates and from HQs to subsidiaries and affiliates.

Sources: Gereffi et al (2005), Humphrey and Schmitz (2004)

It is important to take into account that:

1. Some value chains exhibit very little governance at all, or at best very thin forms of governance.
2. In most value chains there are multiple points of governance. At any point in time, a number of different parties may be setting rules, auditing performance and assisting producers to achieve the required standard.
3. Some chains may embody both producer and buyer driven governance.

What is the relevance of governance to small producers?

Many value chains are no longer only governed by national actors or stakeholders but rather by international ones (e.g. the many standards a product has to meet in order to be exportable). Hence, there are two main challenges to be faced, firstly to gain access to governance in the national setting and secondly to acquire influence at international level. For the first challenge, the development of interested organisations or production associations is important; for the second challenge access to an international lobby is important. ICCO develops activities at both levels, though still rather broadly. The challenge will be to define opportunities for increasing small producers' access to governance value chain specific as well.

III.4.2.3 Systemic efficiency

A third important element in the value chain analysis is that the focus shifts from point (individual) to systemic (value chain) efficiency. As value chains become increasingly integrated, the ability to make an impact on the competitiveness by improving the efficiency of individual links in the chain has become more and more limited. Therefore, a systemic approach is necessary which means that different parts of the chain need to be taken into account and not just one smaller part.

Systemic integration involves closer cooperation between links in the chain and this often involves enhanced responsibilities for governors, as well as more trust between the different links in the chain.

What is the relevance of systemic efficiency to small producers?
Rural producers regard the lack of competition among traders as the main cause for receiving low prices. However, low prices are more often a result of small and irregular volumes of trade, lack of access to finance (barriers to entry for potential traders) and other constraints which prevent a more competitive market. Thus circumventing the traders by developing alternative trade mechanisms might not be a sustainable answer to the problem of low prices if other inefficiencies in the value chain are not addressed.

Fruit, vegetable and grain value chains in the Kyrgyz Republic

Set in the mountains of Central Asia, the Kyrgyz Republic was one of the lower income republics of the former Soviet Union, although it had a relatively diversified economy and well-educated labour force. The country has a population of 5.1 million people, more than 65 percent of whom live in rural areas. About 41 percent of the population is still below the poverty line. Agriculture is the most important sector of the economy, accounting for 34 % of GDP and 53 % of the employment. In 2004 Helvetas and ICCO decided to collaborate in agricultural value chain development to assess and develop market opportunities in Osh Oblast. After a first mission and inception phase, it was concluded that farmers in this area have a comparative advantage in the fruit & vegetable and dairy sectors. Bottlenecks at the levels of production, processing and marketing, as well as opportunities for improving these chains were identified. In August 2005 a social-economic study of three supported value chains was conducted.
The scope of the study was:

a) to formulate the priority areas in which the project will work in future (F&V, dairy)
b) to develop a model intervention strategy for product and market development for small farmers
c) to initiate two commodity chains in the F&V subsector and one in the dairy sector in order to gain insight into key issues and questions which need to be further elaborated for the planning of a three-year programme intervention (action & research)
d) to develop a project document for a three-year intervention.

In general, the findings of the study confirmed an earlier hypothesis that only farmers with certain resources and producing surplus can be involved in value chains. Another important finding was that only one quarter of the land is used for labour intensive and very profitable crops such as vegetables, melons and gourds due to lack of technical knowledge and growing skills among farmers.
The main recommendations of the study were:

- Facilitate the development of long-term contractual relationships and networks within a value chain.
- Evaluate internal and external markets.
- Develop training programmes for growers.
- Improve the quality and safety of products in the chain
- Combine advice, credits and inputs
- Coordinate study tours for stakeholders within the chain
- Identify ways to address the challenges for the poorest farmers

Based on these findings the next phase of the programme was defined.

For more information: Programme officer Kyrgyz Republic

III.4.3 Methodology for undertaking VCA

Value chains differ both within and between sectors but national and local contexts also differ. Therefore each chain will have particular characteristics, whose distinctiveness and wider relevance can only be effectively captured and analysed through an understanding of the broader issues which are involved. It goes beyond the objective of this road map to explain in detail the methodology for elaborating a value chain analysis. For this we refer to more specific guidelines and manuals, where these methodological issues are discussed further (see literature references at the end of the chapter).

In brief, value chain analysis begins with understanding the nature of final markets, since these are increasingly the driver in many value chains. Recommended steps to be taken into account while studying a value chain are:

1. Define the point of entry for value chain analysis, as this will define which links and activities in the chain should be subject of special enquiry. For example, if the focal point is design and branding activities, then the point of entry might be design houses, or the branding function in key marketing companies.
2. Map the value chains, to put numbers and values to the variables under investigation. All value chain analyses will gain from constructing a “tree” of input-output relationships which include primary general accounting identities.
3. Define product segments and critical success factors in final markets. Contemporary markets comprise critical components such as the different market segmentation having their own market characteristics which need to be documented.
4. Identify producer access strategy to final markets which consist of the identification of the key buyers in a particular chain, the dynamics of the buying function, to chart the critical success factors, specify the strategic judgments about the specific sources of the supply.
5. Benchmark production efficiency, which helps analyse the productive efficiency of different parties in the value chain set against the challenges which confront the firm.
6. Define governance of value chains by analysing the power which any party may have in the chain and the extent of chain power which can be based on a number of indicators related to firm size, sales size, profits, buying power etc.

In the making markets work for the poor approach, extra attention is paid to how to include the poor in value chains. Four strategies are described:

1. Firstly, *improved interfirm cooperation*: the focus is on quality improvement. This requires trust and long term commitment, by which small enterprises (SEs) can gain more respect and improve their position;
2. Secondly, *increased competition*: here the aim is to increase the number of market channels for SE’s;
3. Thirdly, *proactive policy*: sometimes governments might intervene and set criteria for large firms to do business with SEs, for example;
4. Fourthly, *confrontation*: if all the above-mentioned strategies do not work some ‘chain facilitators’ (those who manage the supply chain) choose to confront powerful market players directly.

In the conceptual framework of ICCO value chain initiatives, intervention strategies are mostly focused on **developing and upgrading** a VC, as we assume that a VC, however poorly operating, was there before the intervention is initiated. The process of upgrading cannot easily be separated from those of rent, barriers to entry and distribution. This is because upgrading has a comparative component. The four forms of upgrading are:

a. *Process upgrading*: either within the firm or as a result of a series of linked actions in the relationships between firms.
b. *Product upgrading*: either within the firm or as a result of a series of linked actions in the relationships between firms. This requires both internal change and adoption in the chain.

c. *Functional upgrading*: by adjusting activities undertaken within a particular link or moving to activities taking place in other links. This requires consent and adoption of other chain members.
d. *Chain upgrading*: moving out of the value chain into a new value chain.
In the rare case of initiating a new value chain, there is usually a driving force behind the formation of the chain. This is called a "chain initiator". It can be anyone in the chain and it does not matter much who it is, as long as all members acknowledge that there is a common goal.
    - The chain initiator might organise an umbrella group
    - If necessary a third party facilitator might be attracted
    - If there is enough trust, a formal agreement can be signed
    - A value chain manager should be employed (or agreements should be made about sharing responsibility for the management)

Management of the value chain would involve:
- consulting and negotiating with other organisations about market expansion
- sourcing products and services from other businesses
- market analysis
- encouraging the development of new products and services
- fostering cooperation in the chain

III.4.4 What are the points of attention when using VCA?

a. The value chain analysis assumes that a subsector analysis has been performed to create a broader picture. If this is not the case, you risk focusing on a detail of the value chain without having an overall picture of how the specific detail is connected to other parts of the chain and the overall interconnections in the chain.
b. As a value chain spans different economic and sectors, effective analysis requires the participation of different disciplines.
c. Upgrading the performance of an individual firm in a region may have little impact if its surroundings are very inefficient. (Kaplinsky and Morris 2000).
d. After above mentioned ability to differentiate between activities with increasing and decreasing returns, policy makers can formulate appropriate policies.
e. Chain facilitators are often confronted with *a choice* between two types of value chains: either a more formal chain, consisting mostly of large-scale buyers or the more informal chain characterised by a complex web of interrelated and competing SMEs. Usually chain facilitators choose to integrate the SMEs in the more formal chain, which often has good results in the short term but can cause problems in the longer term due to a difference in available and required competences. It is best to let the SMEs choose who they wish to cooperate with in the value chain. (Miehlbradt and McVay 2005, page 33)
f. There are value chains in which small-scale producers have a comparative advantage over large scale producers. This is mostly the case for value chains of handicrafts, for example, or when there are specific growing conditions of crops (Miehlbradt and McVay 2005)
g. As more and more parties become involved in the value chain, the internal costs of managing the value chain become higher and it becomes increasingly difficult to reach a consensus on mutually beneficial objectives. (Hobbs et al. 2000)
h. There is no blueprint for how to conduct a value chain analysis or how to set up a value chain. There is therefore no mechanistic way of applying value chain methodology. Each chain will have particular characteristics, whose distinctiveness and wider relevance can only be effectively captured and analysed through an understanding of the broader issues involved. (Kaplinsky and Morris 2000, Hobbs et al 2000).

i. Value chains are often transformed in periods of crisis when industries feel threatened. When the quality of a product is at stake, e.g. with BSE (mad cow disease), producers are more tempted to cooperate in a value chain, adapt to new legislation and secure their income. (Hobbs et al 2000).

III.4.5 References

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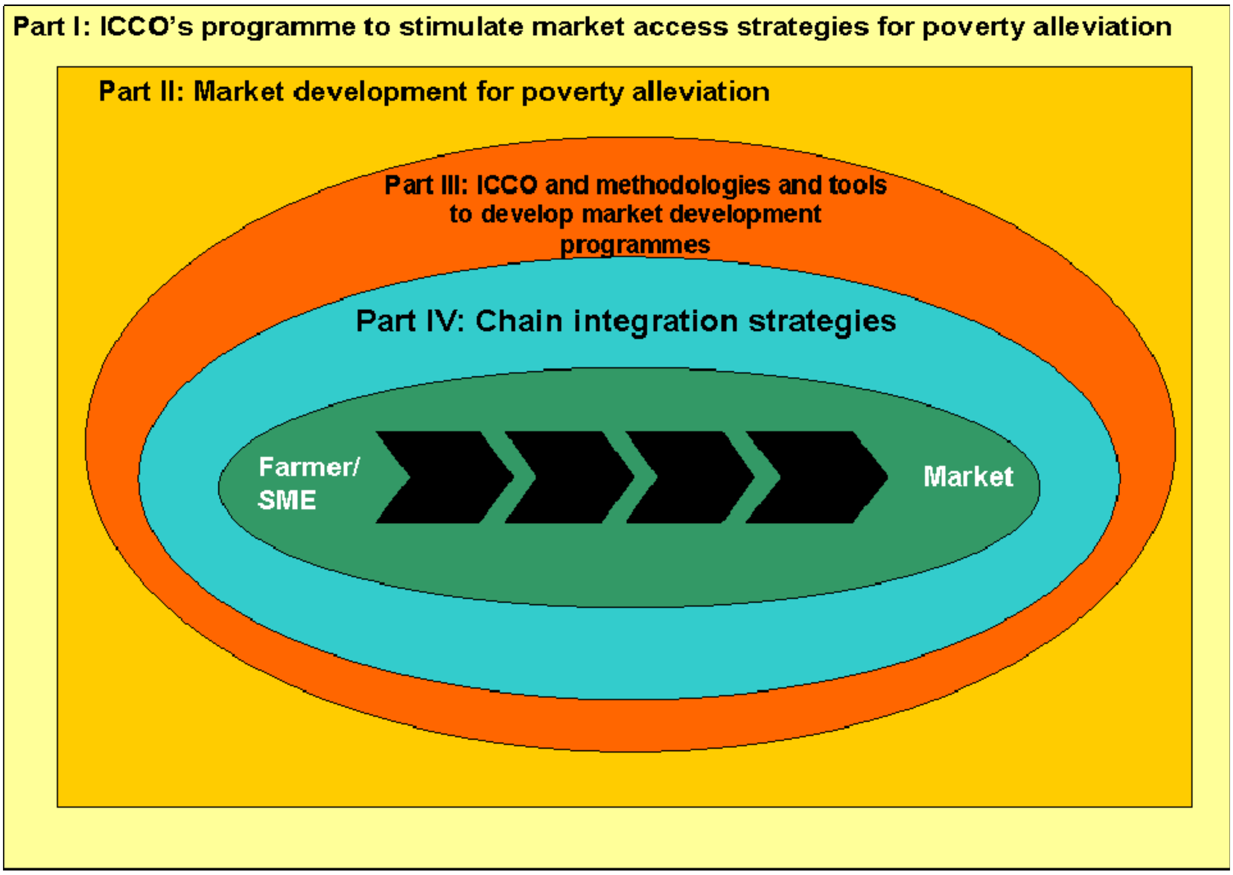
Part IV Chain integration strategies



In Part III we provided an overview of methods that can be used by ICCO programme officers to identify opportunities and constraints for smallholder farmers and small and medium-sized enterprises to gain access to the market. This information can be used to design a regional or sectoral development programme. It became clear that there is an interdependent relationship between actors in the chain that enable or obstructs the market access. Hence effective cooperation among these actors is key for our target group to improve its market access. For this, Part IV describes the basic theory behind chain arrangements and explains how this facilitates smallholders and micro, small and medium enterprises to become integrated into the chain and improve the connection to their final market.

After a brief introduction on the topic (IV.2), the process of upgrading and the four channels to connect smallholders to final markets are presented (IV.3). These four channels connect producers to final markets. In practice, such cooperative relationships have been successfully employed in both vertical relationships (between chain members) and horizontal relationships (between competitors). For this, IV.4 and IV.5 describe in more detail the characteristics of horizontal and vertical integration strategies.

IV.1 Chain Integration strategies

Why are chain integration strategies useful to an ICCO employee?

The growing market liberalisation and integration, the growth in the retail sector and the decline of government support and intervention in agriculture and rural areas are trends strongly influencing the position of smallholders. These trends influence smallholder strategies for achieving economies of scale in marketing, their bargaining power on margins, opportunities for reducing transaction costs and risks and the alliances for improving competitiveness through upgrading of produce quality and aggregated value (Bijman & Ruben, 2005). Therefore development agencies, donors and NGOs are placing more emphasis on enabling farmers to increase their level of competitiveness and produce for an identified market, and this implies stimulating an improvement in their position in the chain.

IV.1.1 The rise of chain and network arrangements

The terms “chains” and “networks” have become common used when talking about economic developments activities. Both terms are used to indicate new relationships between organizations/ entities. In the past 35 years the content of the chain concept has undergone change. The chain concept first developed in the course of the 1970s. At that time “supply chain management” had a principal significance to distribution issues: the integration of supply management and transportation. This development was driven by efficiency considerations: how can we improve our yield through cost reductions? And it was concentrated on internal structural changes.

During the 1980s the emphasis was laid further on the total restructuring of the costs of the supply chain. Primary orientation was still on efficiency. This orientation only changed by the end of the 1980s, when more emphasis was laid on the importance of the client in the supply chain. During this period the concept was largely of a managerial nature, limited to the domain of organizations that were concerned with physical goods. But rather rapidly service producers and organizations in the non-profit sector discovered the importance of value creation via the supply chain.

The transition from chain configuration to chain reconfiguration is the transition to a network point of view. In the case of a chain one can refer to a value stream through a chain of previously established partners. There is still an issue of a certain linearity of activities, services, information and value addition. Whenever there is an issue of reconfiguration, the participants in the chain change, and one can observe entities that are either active or inactive in the chain. There is a case of non linearity but also of changeability in the role of the participants in the network.

The vocabulary identifying these modes of organisation is fairly unstable and used extensively, such as networks, hybrids, supply chain systems, alliances, etc. The diversity of terms may indicate theoretical confusions about the object, but they also clearly reflect an increasing interest for these arrangements. The three main motivations for creating alliances are (Kogut, 1988a):

1. Transaction costs resulting from small numbers bargaining;
2. Strategic behaviour that leads firms to try to enhance their competitive positioning or market power and a quest for organisational knowledge or learning that results when one or both partners want to acquire some critical knowledge from the other
3. One partner wants to maintain its capability while seeking another firm’s knowledge.

There are two different schools of thought that frame the debate. On the one hand, there are advocates that argue that alliances, joint ventures and other forms of collaboration are largely pro-competitive because they help related economic actors reduce risk, lower costs and provide the opportunity for organisational learning through knowledge sharing (Best, 1990, Teece, 1992). Similarly, other advocates suggest that cooperation among economic actors enhances welfare by promoting collective innovation. On the other hand, detractors of cooperation among economic actors argue that these collaborative activities may be anti-competitive because of the risk that the cooperation may lead to outcomes harmful to consumer welfare (Rindfleisch and Moorman, 2003).

The lessons learned from these dynamics are also very important for smallholder activities in a developing context. Over the past two decades, cooperation among economic actors has emerged as a significant area of managerial practice and academic inquiry. In practice, such cooperative relations have been successfully employed in both vertical relationships (between chain members) and horizontal relationships (between competitors). Traditional marketing strategy depicts economic actors as engaged in a zero sum game in which cooperation is both infrequent and undesirable. This traditional economic-based view has given way to a relational perspective that suggests that interfirm cooperation is both frequent and desirable (Dwyer, Schurr and Oh, 1987).

Four major forms of incorporation of smallholder producers and small and medium- sized enterprises to the market can be identified (Humphrey and Schmitz, 2000):

a. Arm's length trading relationships between producers and buyers, which are essentially impersonal in nature;
b. Network relationships between "equals", for instance producers holding complementary assets and selling into final markets;
c. Quasi hierarchical relationships, with a dominant governor coordinating global production and exchange but with no or only weak equity links;
d. Hierarchical relationships involving close equity ties and foreign direct investment.

IV.1.1.1 Arm's length relationships

This is the most common relationship that small producers use to sell their produce or service to the nearby local market. However, even in local markets this is a rare situation, since issues such as production volume, credit ties, transport costs and logistics and permissions to sell easily create a barrier for producers to sell at arm's length.

In the case of production for arm's length relationships for more distant markets, these relationships can be described as transient and impersonal. The export of many primary commodities, such as coffee and cotton, is an example of this form of incorporation in the global market. In this case, the following major buyers can be identified:

a. Final retailers;
b. Independent specialised buyers in the country of consumption;
c. Large international firms sourcing products from many countries, either as independent buyers or through their own global production networks;
d. Local buyers and export agents;
e. Large producing firms acquiring products and other inputs from other local suppliers.

IV.1.1.2 Network relationships

Although much of the global trade is conducted through networks of large firms and their suppliers, small producers and micro, small and medium-sized enterprises (SME) have not been entirely absent from the stage. The most well known of these networks are industrial clusters in Italy and Spain, but there are also a growing number of success stories from developing countries.

The problems of small producers and firms are often related to their size, since this limits them to acquire inputs cheaply, find a labour force with the required skills, gain access to the finance required to serve distant markets or acquire technology. These disadvantages are often overcome when SMEs cluster together. At a minimum they gain from the unintended consequences of proximity, but more when these are complemented by joint actions to achieve collective efficiency. Cooperation between SMEs appears to be much easier when it involves vertical value chains than when it requires cooperation between firms doing similar things (Nadvi and Schmitz, 1999).

IV.1.1.3 Quasi hierarchical relationships

In an increasing number of cases, producers sell into final product markets which are characterised by either weak or absent equity links, but which do not involve arm's length relationships. Global production networks are coordinated by key firms in the chain which determine who is incorporated into global production networks, what standards these producers need to achieve in order to participate in these chains, who monitors these standards and who will help producers achieve them. These "governors" play an increasingly important role in the modern era of globalisation, which can be distinguished from nineteenth century internationalisation due to the complex and coordinated role in which global production networks operate (Gereffi, 1994).

Gereffi has made the useful distinction between two types of value chains based on the locus of governance in these chains, being buyer driven chains and producer driven chains (see also Chapter III.5.4.2.). From the perspective of producers in developing countries, the role played by these governors is important in order to determine:

a. Whether they are to be incorporated in global value chains;
b. Which market segments they will serve in these value chains;
c. Which functions they will undertake in these value chains;
d. In which areas they will be allowed to upgrade these capabilities.

IV1.1.4 Hierarchical relationships

The final major category of ways in which producers are inserted into global markets is through the channel of foreign direct investment (FDI). This may be either as subsidiaries or affiliates of transnational companies (TNCs), or by feeding into the operations of TNC subsidiaries. In the 21st century, a dominant factor for influencing the location of FDI is just in time production. This means that proximity of suppliers and final manufacturers has grown in importance and clusters of FDI are co-locating to achieve systemic efficiency in production (Kaplinsky and Readman, 2001).

From the perspective of smallholders and SME the implications are clear; they need to develop the capability to serve TNC/TNC subsidiaries not just with low labour costs but with low total costs and to deliver these networks on a just in time and total quality control basis. But there are other trends which are simultaneously affecting the way in which SMEs are being incorporated into the global economy. There is an increasing trend for large firms to retreat from production and to buy-in products made to their tight specifications. In these sectors, global producers are therefore moving to become global buyers. In order to achieve this shift, these global buyers are required to introduce global standards and ensure that their suppliers meet the quality standards which they require, as well as the environmental and social standards which their consumers require. In these cases, SMEs may be able to feed directly into global product markets or to do so by locally owned firms.

A third trend, found more in producer driven chains, runs in the opposite direction where TNCs move away from outsourcing production to independent suppliers towards increasingly insisting on controlling the production process themselves. A good example is the automotive sector. This is referred to as global sourcing (Kaplinsky and Readman, 2001). In this case, there is diminishing scope for locally owned firms. Here SMEs feeding into global product markets will need to link themselves more directly into hierarchical, TNC controlled value chains.

IV.1.2. Common chain linkages

Since the 1980s, there has been a dramatic growth in both the number of alliances (in general) and the diversity of these alliances within the private sector. Nationalities of partners, motives and goals in entering alliances and in the organisational structure of the alliances have become increasingly varied (Gulati1998). At the one end are the *joint ventures,* in which partners create a new entity based on equity and which most closely replicates the hierarchical control features of organisations. At the other end are alliances with no sharing of equity that have few hierarchical controls built into them (Gulati1998).

Figure 1. The nature of alliances.

Figure 12: The nature of alliances
Source: Gereffi (1998)

Gereffi describes three forms of possible alliances in which smallholders tend to get involved to improve their position in the final markets:

1. *Horizontal alliances.* They can also be described as cooperation amongst competitors (Rindfleisch 2000).
2. *Vertical alliances* can be defined as cooperation among channel members (Rindfleisch 2000). The arrangements between chain members are voluntary and are made with a view to mutual gain. It involves exchange, sharing or code-development of products, technologies, or services (Gulati, van Duren et al).
3. *Diagonal alliances* can be established with non-profit organisations, as in public private partnerships; they can also take the form of partnerships for joint research and development with local, state or national governments (Volery and Mensik 1998).

Horizontal and vertical alliances are the most commonly used strategies to improve the position of smallholders by creating alliances among private sector actors. Diagonal alliances consist of alliances among public and private sector actors and are mainly aimed at improving the enabling environment. For this, they can be considered a supporting alliance strategy to the first two.

IV1.2.1 Importance of horizontal and vertical alliances for smallholders

Farmers can have different type of strategies depending on their position in the chain. Some farmers may be excluded from any decision making about issues that affect them – even about what crops they grow or what animals they raise. At the other end, farmers may have a high degree of control over management: they may be able to decide how much they sell, to whom and at what price. Farmers moving into a position of more participation in chain management are more horizontally integrated in the chain. Farmers with more activities rather than a particular specialisation are more vertically integrated in the chain. The Figure below shows the different strategies and farmer groups according to the level of participation in chain management and diversification of activities (KIT, 2006).

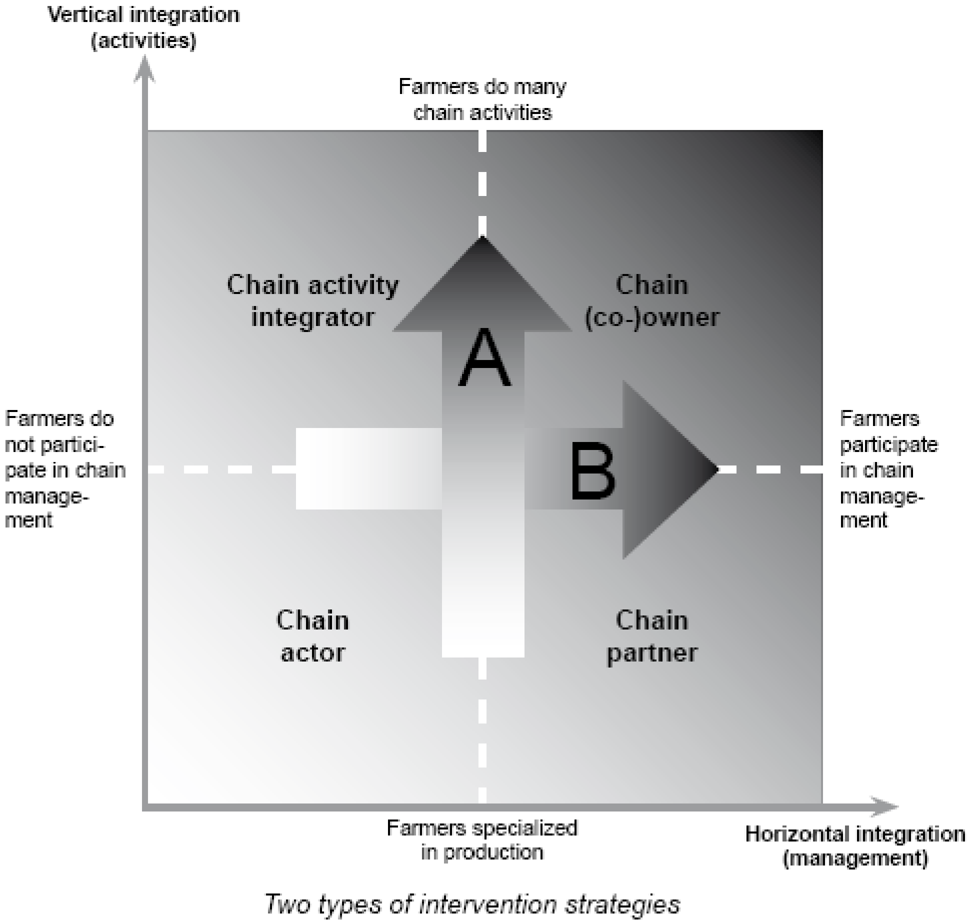


Figure 13: Vertical and horizontal integration strategies
Source: KIT, 2006

The best chain position for the farmer depends on the specific situation and may change over time. As farmers evolve from chain actors into chain owners, they add "economic rent" to their business (they increase their share of benefits), increase their control over the chain and protect themselves better from competition. But this involves greater risks and responsibilities which farmers should be able and willing to bear. The costs may outweigh the benefits.

There are also overlaps as a supply chain is created from vertical and horizontal alliances (Woods, 1991). Farmer organisations can play a key role in organising economic activities beyond local boundaries. They can build up relationships with various chain actors and create commitments from various actors to cooperate on mutually beneficial actions and investments and thus create value chains. Vertical integration thus incites adjustments in horizontal cooperation mechanisms in such a way that information, risks and revenues can be shared amongst different stakeholders.

IV.1.2.2. Horizontal alliances

Horizontal integration aims at more involvement in managing the value chain itself –for example by farmers improving their access to and management of information, their knowledge of the market, their control over contracts or their cooperation with other actors in the chain.

Horizontal alliances in value chains can take many different forms. Some groups of smallholders will have the form of an informal network with little ‘fixed’ routines of working together and fluidity with regard to who are members of the group. An example of this is a group of farmers that regularly assist with extension workshops. Other groups will be more structured with common rules and practices (e.g. farmer field schools, contract agriculture) and can be called informal organisations. Once they formally register themselves and elect persons to represent them, the legal format becomes important and they will become formal organisations.

Horizontal integration can involve the following:

1. Acquiring activities dealing with similar products to reach economies of scale. A group of farmers can grow enough produce to meet a buyer’s volume requirements. The buyer can deal with the group as a whole rather than with individual farmers.
2. Acquiring activities dealing with different products but sharing common resources to reach economies of scope. A group of farmers can pool their resources, access credit and services to develop the technology and skills needed to produce more sophisticated products. A group is more able to take risks than an individual.
3. Acquiring activities that are substitutes for one’s products.
4. Acquiring competitors to reduce the threat from competition.
5. Completing the product range which is expected by customers. A group finds it easier than an individual to ensure a consistent supply of produce in terms of volume and quality. Group members can arrange among themselves to grow crops that mature at staggered times, thus ensuring a constant supply for the buyer. They can pool their resources to acquire the technology they need to achieve consistent supply. They can also buy produce from other farmers to cover shortfalls in their own production
6. Increasing negotiation power and getting more leverage over powerful suppliers or customers.

The early establishment of cooperatives by smallholder producers in developing countries has been largely promoted in the framework of acquiring land rights and interest representation *vis-à-vis the state* (Munckner, 1988). In subsequent periods, attention has gradually shifted towards joint service provision and improved access to factor markets (for inputs, credit and extension). With the declining role of the state in rural development, many third world cooperatives disintegrated or even totally collapsed (Deininger, 1993). The classical defensive functions of agency cooperation therefore became less relevant and farmers started to search for alternative forms of collective action that could better serve their purposes.

Information management
Often farmers are at a disadvantage with regard to information. They have no information about the performance of their own organisation, let alone of the market. By contrast, companies downstream in the chain tend to have elaborate information systems. For example, supermarkets register the daily buying behaviour of their customers, while processing companies register the yields, volumes and prices of major crops. The more information someone manages, the better he or she can manage a company. Some elements of farmers' information management are:

- ✓ **Record-keeping** of the use of labour and farm inputs. This is necessary to generate proper understanding of the costs involved, to base farm management decisions on information and to create the ability to negotiate the price of the product.
- ✓ **Traceability** This means keeping records to guarantee the source of the product and the inputs for the buyer.
- ✓ **Market information** This involves knowing prices and trends in the market so that the farmers can bargain with potential buyers. A group finds it easier than individual farmers to obtain the information that members need to grow for a particular market. At the same time, other chain actors find it more attractive to deal with a group than with numerous small scale producers.

Quality management
Quality management assures that both the product and the production processes satisfy the consumer. It assures that the farm product can find its way into the market. Quality can be a unique selling point through which one group of farmers can differentiate themselves from other suppliers. Quality increases the appeal of farmers as business partners, hence their bargaining power. Some aspects are the following:

- ✓ **Grading** of the product into homogeneous quality grades, each with a different price, each for a different market segment.
- ✓ Implementation of **quality control systems** at critical points in the production system.
- ✓ Implementation of **quality certification schemes** that are demanded in the market such as Food Safety Certifications and GLOBAL-GAP[16]. A group can set rules specifying quality standards and can appoint members to enforce them. The group can access extension and marketing advice that would be impractical to provide to individual farmers. And it is worth paying for certification and inspection procedures so the group can sell produce to high-value export markets.

Innovation management
Often innovation is steered from actors at the end of the chain and being closer related to the market. For instance, new technologies are brought to the farmers by extension officers from contracting companies or the public sector. However farmers have detailed knowledge of what works best in their fields. They can share these experiences among each other, identify best practices, start experimenting, etc. They can make study trips to large scale farmers, research institutes and experimentation centres. In this way, formal scientific knowledge will be combined with practical knowledge from the ground. This will not only boost innovation in the chain, but also make the farmers more attractive business partners.

The functions and structure of producer organisations in food supply channels are subject to large adjustments. Recently, many theoretical and empirical studies have identified options for restructuring agricultural cooperatives (van Bekkum, 2001; Bijman and Hendrikse, 2003; Chaddad and Cook, 2004). Most studies apply organisational and management theories (notably transaction cost, agency, property rights/incomplete contracting approaches) to understanding structural cooperative change. The current debate has resulted in a series of

[16] Before called EUREP-GAP

typologies of different organisational models for restructuring cooperatives (Chaddad and Cook, 2004; Birchall, 2003). In terms of ownership, options range from the traditional member-based producer organisations (with members having full residual control and claim rights) to investor-owned firms (where investors hold ownership rights). Given increased membership heterogeneity, various options for improving organisational efficiency and performance can thus be perceived.

IV.1.2.3 Vertical alliances

The aim of building vertical alliances is to reduce risk and uncertainty and increase cooperation and reliance between chain members, in order to create long-term mutual gain. To achieve chain alliances, three things are important (van Duren et al):

- Firstly, there must be a common **goal** amongst chain members, a shared understanding of what the participants in a vertical alliance want from the relationship. The aim is set on long-term gains. For both partners there should be a mutual gain.
- Secondly, there must be a **desire** to achieve the goals. This gives the relationship energy and commitment. Each organisation should be dedicated to meet the partners' wishes.
- Thirdly, the **process** of building an alliance is intertwined with the goal and the desire.

One important question is how to select a partner. Research has shown that availability (however simple that may sound) is vital, as are complementary, interdependence, reputation and social networks (Gulati 1998). But as Van Duren et al mentioned, there must be a common goal, a desire to make the alliance work and there needs to be trust. Because the arrangements have a long-term perspective, it becomes attractive to invest more in other chain members both in time, information sharing and money. Vertical alliances are often mentioned alongside supply chain management or the organisation and coordination of chains.

There are two schools of thought on how alliances can best be built to minimise risk. One school is focused on: the motivation for building a relation is based on building **trust.** Trust is defined as *"a willingness to rely on an exchange partner, in whom one has confidence"*. Trust supports exchange between chain members (Rindfleisch 2000). To build trust, competence and character are required (Van Duren et al). Openness and honesty are very important, as is the sharing of relevant information, reliability, fairness and the use of technical business skills.

The other school is focused on establishing **contracts** to reduce risk. A contract can be used to mediate the relationship between partners. However if there is trust, organisations may not choose to rely on detailed contracts to ensure predictability (Gulati 1998, Volery and Mensik 1998). As Gulati (1998) describes it: *"a detailed contract is one mechanism for making behaviour predictable and another is trust"*.

In developing countries, the building of vertical alliances mainly occurs in export oriented sectors (Van der Meer, 2006). These export oriented chains are usually chains in which standards, high quality or specialty play a part. The end product must meet certain requirements and all chain members must contribute to obtaining them. So theoretically, if one chain member fails to deliver the required standard, the whole chain fails. This implies that chain members are more dependent on each other and that, because of the required (end) standard, one supplier cannot be exchanged by just any other. In those cases, it might be useful to reduce risk in the chain by building a vertical alliance, either by increasing trust, by formulating a contract or by doing both.

An important question is whether coordinated chains that include small scale farmers can compete with coordinated chains of commercial farmers (Van der Meer 2006). In other words, under what circumstances will small scale farmers be selected as partners in a vertical alliance? (Swinnen 2005)

1) The most straightforward reason is that companies sometimes have no choice. In some cases, small farmers represent the vast majority of the potential supply base.
2) Case studies also suggest that company preferences for contracting with large farms are not as obvious as one might think. While processors may prefer to deal with large farms because of lower transaction costs in collection and administration, for example, contract enforcement may be more problematic and hence costly with larger farms. Processors repeatedly emphasised that farms' "willingness to learn, take on board advice and a professional attitude were more important than size in establishing fruitful farm-processor relationships".
3) In some cases, small farms may have 20-40% lower costs (van der Meer 2006). This is particularly the case in labour intensive, high maintenance production activities with relatively small economies of scale. Also, when access to land is the limiting factor small scale producers usually have an advantage.
4) Processors may prefer a mix of suppliers to prevent becoming too dependent on a few large suppliers.
5) Processing companies also differ in their willingness to work with small farms. Some processing companies continue to work with small local suppliers even when others do not. These companies have been able to design and enforce contracts which both the small firms and the companies find beneficial. This suggests that small scale farmers may have future perspectives when effectively organised

Development specialists fear that small farmers in developing countries are excluded when vertical alliances are shaped. There are three main reasons why small farmers are likely to be excluded from the chain alliance (Swinnen 2005).

1) Transaction costs favour larger farms in supply chains, since it is easier for companies to contract with a few large farms than with many small ones.
2) When some investment is needed to contract with or supply to the company, small farms are often more constrained in their financial means for making necessary investments.
3) Small farms typically require more assistance from the company per unit of output.

At the same time it is recognized that the building of vertical alliances is important since small scale producers lack knowledge and experience regarding access to more distant or more sophisticated end markets. If these linkages are not built, the main weaknesses of small scale farmers such as the lack of knowledge about modern markets, technologies and modern inputs and the heterogeneity in product quality and supply quantity are very difficult to overcome (Van der Meer 2006). Swinnen (2005) warns that in some cases when the processors need to invest in the suppliers, they tend to only go 'so far' and have a long-term strategy to upgrade part of their supply to larger, more efficient and fewer suppliers.

IV.1.3 Points of attention when looking at alliances?

1) The creation of vertical alliances is a private sector business; however there are various ways in which the public sector (policy makers or development organisations) can enhance their emergence and their functioning (Van der Meer 2006). By doing so, the public sector can influence whether it is more or less interesting to involve small scale farmers in the alliance. Van der Meer (2006) mentions four fields of intervention for when there is no level playing field for large companies and small scale producers:
   a) The government must provide adequate laws and regulation for doing business. Important areas of attention are regulation on pesticides and veterinary drugs but also property rights and contract enforcement
   b) Independent facilitators have a role to overcome lack of experience and lack of trust between companies and small scale farmers. This can be overcome by contributing

well-documented information about arrangements and experiences that have worked well elsewhere

c) The promotion of producers' organisation. In many countries, legislation discourages the formation and development of producer organisations
d) Support can be given in the development of Good Agricultural Practices (GAP). Preferably the chain leader takes the lead because the results are directly related to market success and provide some sharing in costs

2) Furthermore the sequence of events in alliances gives a good understanding of the behaviour and strategy of firms. Which firms enter alliances and who do they choose as partners? What types of contract do they use to formalise the alliance? How do the alliance and the partners evolve over time? There are also performance related questions: What factors influence the success of an alliance? What is the effect of the alliance of firms entering them (Gulati 1998)? By finding an answer to these questions it may become clear whether an entrepreneur does or does not fit into a certain alliance and vice versa.

3) With the emergence of coordinated supply chains, the competition is increasingly between supply chains rather than between individual firms (Van der Meer 2006).

4) In developing countries, vertical alliances and coordination of chains are mainly present in export oriented markets and specifically for perishable products and sensitive processed products. In bulk and commodity markets vertical alliances are virtually absent.

5) The market served by coordinated supply chains is more visible than traditional markets, but in most countries it still constitutes a relatively small share of production. It is an emerging and more profitable part of the agricultural sector but also a small part that receives a lot of attention (Van der Meer 2006)

6) There is nothing wrong with the fact that small scale farmers cannot be competitive in all products and all markets, even if they are well organised. There *is* something wrong if small scale farmers are discriminated against or neglected because they are in a weak position due to market or policy failure (Van der Meer 2006)

7) With regard to horizontal integrations in particular, attention needs to be paid to:
   a) Synergies which may be more imaginary than real. Connections between activities do not necessarily imply realistic economies of scope.
   b) Difficulty of acquiring substituting activities. To do this successfully is complicated and a huge and lengthy management challenge.
   c) Anti-trust issues as a result of reduced competition or even a monopoly situation.
   d) It takes several years to build chain partnerships. Just identifying a good partner may take a year. Another year is needed to get to know each other, develop trust and shared visions and agree on a joint business plan. Then comes implementation of the joint business plan. A real partnership is only in place after 2 or more years of mutually satisfactory implementation. Hence building a partnership will take at least 4 years.

8) With regard to vertical integrations in particular, attention needs to be paid to:
   a) Traders and processors will be willing to include small scale producers if they expect the benefits to outweigh the costs (Van der Meer 2006), i.e. when the situation is such that the small scale farmers have benefits over larger scale farmers.
   b) Processors will not be very interested in small scale farmers if the (quality) supplies of larger farms are sufficient (Swinnen 2005).

c) Companies seem to be most likely to reach out to small farms when they face a supplier base which is dominated by small farmers unable to supply the commodities they want and least likely when there is a heterogeneous farm structure with some farms able to deliver the desired supplies (Swinnen).

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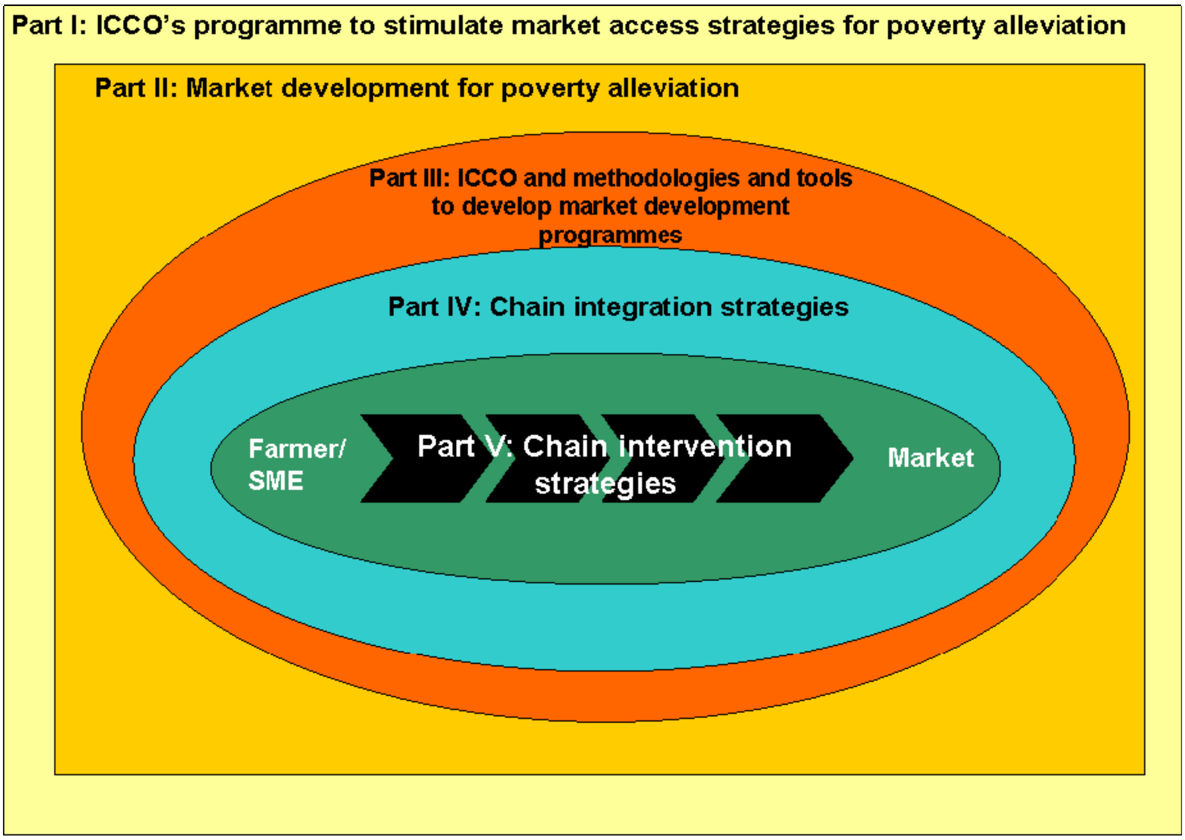
Part V ICCO and Chain Intervention Strategies



The information provided in Part I, II, III en IV creates the framework ICCO programme officers can use to design a programme on market access development for poverty alleviation. This helps ICCO programme officers to select and facilitate their partners, and develop together one or more intervention strategies to enable this market development strategy. Part V presents the most commonly used intervention strategies developed by ICCO partners in order to improve the integration of small scale farmers and SME into chains and networks. These strategies were identified by ICCOs local market access advisors based on an inventory made of the activities currently developed by ICCO partners in the period 2005-2006 (see Figure 14).

For each intervention strategy, it is explained why it is useful for an ICCO employee, why it is important with regard to poverty alleviation and providing market access to smallholder farmers, a brief summary of the aim the strategy encompasses and points of attention when using the strategy.

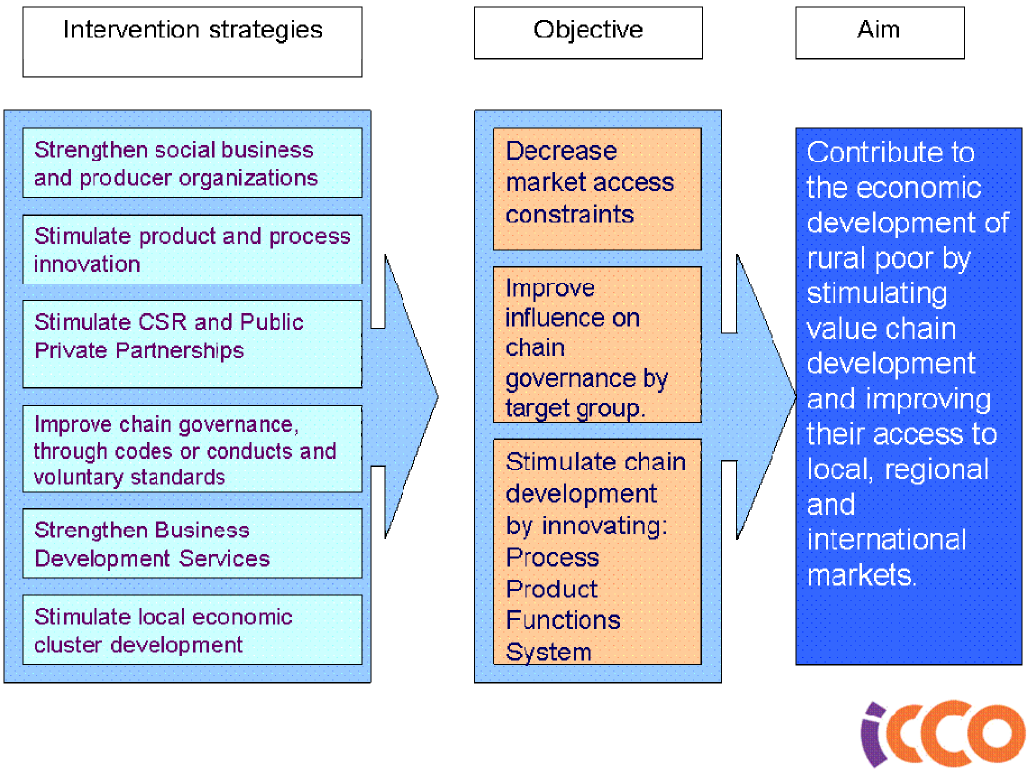


Figure 14: Intervention strategies used by ICCO partners to work towards SFED through market access strategies

This part should be regarded as an extension to conceptual issues raised in Part III and a practical specification of the general concepts of horizontal and vertical integration strategies explained in Part IV. For example, the ECOLOC methodology explained in Part III has a strong focus on linking private ideas to public institutions. This is just one methodology that emphasises public-private links. This Part elaborates further on Public Private Partnerships. Other intervention strategies used mainly to stimulate vertical integration are Clusters and strategic alliances, Codes of Conduct and Standards and Corporate Social Responsibility. But the most dominant strategy stimulated by ICCO partners is creating social business and producer organisations. For this, Part V starts by describing briefly this intervention strategy. The creation and/or development of Business Development Services (BDS) described in V.2 is an intervention strategy that can stimulate both horizontal and vertical integration. BDS is strongly related to geographical economic analysis and local economic development tools as described in Part III. Cluster development elaborates further on the geographical analysis methods presented in Part III. Cluster development, Corporate Social Responsibility and following certain standards and Codes of Conduct are strategies which can be used to strengthen the position in a certain value chain, or access other value chains, related to high value market segments. The role of NGOs becomes stronger and stronger in developing these strategies and by using the media they receive a lot of attention. As a result, consumers are also rapidly becoming involved.

V.1. Social enterprise development

Why is social enterprise development a useful intervention strategy for ICCO employee?

As explained in Part I, ICCO approaches market and economic development issues from the perspective of disadvantaged target groups in developing countries. The majority of the economic activities supported by ICCO take place in the rural context and focus on smallholder agricultural activities or other agricultural related small and medium-sized enterprise activities. In most developing countries, smallholder farming is important in terms of agriculture and food security. Most smallholders are vulnerable to economic and climatic shocks and spread their risk by diversifying their sources of livelihood, often including significant off-farm income.

Complete subsistence or self-sufficiency does not exist and there is at least always some form of local market in which smallholders trade their surplus. But these markets are not very remunerative and offer limited opportunities for price negotiation. Finding and entering markets that will provide them with better prospects can be extremely difficult. For this, ICCO has a long tradition of supporting partners that stimulate the development of horizontal alliances through the establishment and strengthening of social enterprises.

The concern of ICCO to stimulate sustainable economic initiatives has become an urgent item on the agenda. For some development actors engaged in organizing marginalized sectors for their socio economic upliftment, ensuring sustainability is about economic empowerment. They want to see marginalized groups gain control over strategic resources and market processes so that these groups can be self reliant in undertaking development in their own communities. In this context, social entrepreneurship is a useful conceptual framework.

V.1.1. Why is social enterprise development important?

Horizontal alliances in value chains can take a lot of different forms. Some groups of smallholders will have the form of an informal network with little 'fixed' routines of working together and fluidity in who are members of the group. An example form a network is a group of farmers that assist regularly to extension workshops. Other groups will be more structured with common rules and practices (e.g. farmer field schools, contract agriculture) and can be called informal organisations. Once they will formally register themselves and elect persons to represent them, the legal format becomes important and they will become formal organisations. Social entrepreneurship involves the promotion and building of enterprises or organizations that create wealth, with the intention of not benefiting just one person or family, but a defined constituency, sector or community, usually involving the public at large or the marginalized sectors of society. This intervention strategy has grown in importance since it marries two powerful concepts, enterprise profitability and social mission.

The strategy is the result of an important market development change that took place during the last decade of the past century when virtually all developing countries revised their industrial policy regime and regimes of protection and subsidies were overturned, with increasing rapidity and pervasiveness. This change was partially stimulated by the positive experience of some East Asian countries which had promoted vigorous outward-oriented growth. Furthermore multilateral agencies and bilateral donors exerted increasing pressure. As a result, local governments of developing countries dismantled incentive systems (liberalisation) and forced local producers to operate on a global platform (globalisation).

But the operation of pure market forces in a global context does not in itself provide conditions for sustained income growth. Global competition is so intense that unless deliberate policies are introduced to foster a systematic programme of upgrading, producers in developing countries may engage in a race to the bottom, entering a trajectory of increasing growth in which economic activity expands, but real incomes fall since producers face intense competition (Kaplinsky and Readman, 2001). Besides that, globalisation and liberalisation of markets have led to the emergence of new players in the value chains for agricultural products. Demographic factors, particularly urbanisation in developing countries, have influenced consumer preferences, which in turn have impacted on domestic markets and supply chains. Parastatals have been replaced by multinationals and local private traders in the agricultural export trade and input distribution, while supermarkets and large-scale retailers become increasingly important in both developed and developing countries. The role of other players such as service providers, NGOs and community based organisations has also grown.

Generally speaking individual smallholders are unable to supply sufficient produce to meet the needs of a trader and processor. These need sufficient quantity and quality to generate sufficient rent to their activities. Logistic requirements are often the most obvious reason for pooling from different suppliers, e.g. truckloads, containers, minimum processing volume to break even, etc. The negotiating power of individual smallholders towards these value chain operators (segments of the chain) will therefore be limited, resulting in low prices or markets will be absent. Collective action of producers is therefore necessary to improve farm gate prices by reducing logistic inefficiencies, reducing transaction costs along the chain and strengthening producer bargaining power. Initial access to premium price markets, like export markets or national supermarkets, requires a threshold number of producers to pool production and create sufficient volume to meet logistic and transport costs (Bosch, Eychenne et al. 2001; Chirwa, Dorward et al. 2005).

The development of intervention strategies focused on the establishment and strengthening of social enterprises obtains every time more the interest of national and international aid organisations. Already in its World Development Report of 2001, the World Bank emphasised on the need for institution building for markets and stressed the importance of agricultural cooperatives and formal business associations for market supporting functions (policy development and advocacy) and market-complementing and –substituting functions (setting up factor markets, developing alternative marketing channels, engaging in supply chains). And the coming 2008 World Development Report stresses the importance of governments and donors to enhance the effectiveness of the participation of producer organisations in consultative policy processes. The main reason for this growing interest, are the profound changes the economic and political context of agricultural markets in developing countries has undergone over the last few years. Government policies are moving away from the direct management of agricultural markets and focus more on indirect regulation for markets to work for the poor (WDR 2001). These policy initiatives define the context within which farming business can be done, as well as the framework within which smallholder farmers' economic organisations and institutions can be developed.

Three types of social enterprise development strategies have been observed among exemplary practices studied, which are *empowerment strategies, intermediation strategies, and resource mobilisation strategies* (AIM and Cafo, 2004). These three may be broadly differentiated according to objective or intent. Empowerment strategies address ownership and control of social enterprises by marginalized sectors. Intermediation strategies primarily address the need to provide access to products and services among a critical mass of marginalized sectors. Resource mobilization strategies aim to generate surplus income from selling products or services, and to use such surplus income to finance the core program of operations of their respective development agencies.

Oromo Self Reliance Association (OSRA), Cereal Banks & Access to Markets, Ethiopia

Since 2002, ICCO and the French development organisation CIDR (Centre International pour le Développement et la Recherche) support the establishment and strengthening of producers organisations interested in creating cereal banks. At the start this was done by providing Financial support to the NGO Hundee. The main aim of these activities was directed at improving food security. By time the focus has changed towards development of local markets with the aim to contribute to the livelihood of poor rural farmers in general and food security specifically. Also, more NGO’s have become interested in the work of Hundee and the methodology they developed together with CIDR.

Since 2006 ICCO supports 5 NGO’s that have created an informal consortium. They receive technical advice and training by FFARM (Facilitating Farmers Access to Remunerative Markets) a private company, without profit aims, created by the staff of a number of NGO's that participated in the programme. The objective of FFARM is to create fair market access conditions for producer organisations. For this, the company provides technical advice to producer organisations and related NGOs, training of staff and establishing contact between producer organisations and buyers. If required and desired, FFARM facilitates in the establishment of processing facilities. The producers are the share holders of these activities. FFARM receives technical, methodological and Financial support of CIDR.

ICCO provides financial support to the consortium throughout the strengthening of 150 existing and 80 new producer organisations united in 12 informal networks and representing approximately 25.000 members. Besides this the market access will be improved by organising auctions at network level, developing 3 new processing facilities and facilitating the producers establishing contracts and developing tenders. ICCO provides this support, since it creates good opportunities for providing an effective contribution to the improvement of living conditions, food security and the capabilities of ICCOs target group. Besides this, working as a consortium creates opportunities for the NGOs to learn from each other and to work together in advocacy activities.

Further information: ICCO programme officer for Ethiopia

V.1.2. What is a social enterprise?

V.1.2.1. Introduction

Social entrepreneurship involves the promotion and building of enterprises or organizations that create wealth, with the intention of benefiting not just a person or family, but a defined constituency, sector or community, usually involving the public at large or the marginalized sectors of the society. This definition of social entrepreneurship has many elements. First, if focused on wealth creation for development ends. We are dealing with organizations that operate in the market, a place where the exchange of goods and services take place. In this sense, it excludes development initiatives that do not involve wealth creation. Secondly, it does not include all wealth- creating endeavours, particularly those of business enterprises whose main reason for being is to generate profits for the enrichment of a few individuals or their families. Social entrepreneurship's primary stakeholders are the marginalized sectors of society.

A social enterprise is different from a private or traditional business enterprise. In the traditional business enterprise, the primary stakeholders and beneficiaries are its stockholders. These are usually individuals and their families who own the capital invested in the enterprise. In contrast the primary stakeholders and beneficiaries of the social enterprise could be a sector, a community, or a group, usually involving the marginalized sectors of society, who may or may not own the enterprise.

In terms of primary objectives, the traditional business enterprise has a clear bottom line; profit. The social enterprise, in contrast, is characterized as an enterprise with a double or triple bottom line. Like its business counterpart, it needs to generate surplus or profit. But such a financial sustainability objective is not the bottom line. Depending the nature of its constituency, the social enterprise may have a second bottom line: to achieve social objectives such as the capacity building of empowerment building of a sector or group, or the empowerment of their quality of life. A third bottom line, such as an environmental sustainability objective or the preservation of cultural integrity, may also be part of these primary objectives.

In terms of enterprise philosophy, the traditional business enterprise is accumulative, while the social enterprise is distributive. The traditional enterprise minimizes costs and maximizes profit to enrich the beneficiaries. In the process, the costs of doing business more often than not exclude social and environmental costs. In contrast, the wealth derived by the social enterprise is distributed to a broader segment of society. At its best, the social enterprise generates profit or surplus with due regard to social and environmental costs, and makes a pro-active contribution to resolving social and environmental problems as part of its reason for being.

Business enterprise can be social enterprise. Best practice in corporate social responsibility among businesses actually approximate social enterprises. But the social enterprise concept is distinct to corporate social responsibility (CSR). CSR is a tradition emanating from the business community. A number of business leaders and entrepreneurs have been driven by their personal values and vision to set up companies with a clear social mission. But the spread of CSR was also a response of the corporate sector to the clamor from civil society organizations and the public at large for business to be more accountable. Many companies also joined the CSR bandwagon as a result of a regulatory environment that encouraged corporate giving and penalized corporate practices deemed harmful to society (see also Part V.4). Even as they serve important social objectives, practices in CSR do not usually address the issue of ownership by marginalized sectors of the enterprises themselves, while this has become an important agenda of social entrepreneurship. This has evolved from the entry of development institutions, practitioners, and advocates into the market place.

Smallholder vegetable cooperative linking to high quality markets

In Guatemala the alliance OPCION/ AJ-TICONEL provides technical support in productive, commercial and organisational processes aimed at improving the income and life quality of smallholder farmers in extremely poor regions of the country. The alliance consists of the NGO OPCION and the private actor Aj Ticonel, both founded in 1999.

The main responsibility of Aj Ticonels is to commercialise non-traditional vegetables produced by smallholder farmers to the local and international market. Currently, the alliance works with 93 farmer groups and farmers' organisations. They represent a total of approximately 2000 families, of whom 400 supply their produce to Aj Ticonel on a regular basis, i.e. three times a week. 87% of the farmers cultivate less than 1 ha and the majority did not have previous experience in the cultivation of this particular produce. The support of OPCION-Aj Ticonel enabled them to install small scale irrigation systems, which allow them to cultivate three cycles a year, compared to only one before the scheme started. In addition, OPCION provides the farmers' groups with credit (at 5% interest rate per cropping cycle), technical support and extension services, planning sessions and coaching of agricultural diversity strategy, product development and increased market access. All services are free of charge and the credits are paid from donations received by the NGO. AJ Ticonel trades non-traditional vegetables at both national and international levels (8% Guatemala, 2% Costa Rica, 20% Europe and 70% USA of the volume). The buyer pays for the transport. Municipalities are involved in improving access roads in order to transport the produce to the markets. The access to appropriate technology and technical support enables the farmers to comply with high product quality requirements. The quality enables Aj Ticonel to negotiate a good price, which stimulates the farmers to continue supplying their produce to Aj Ticonel instead of selling it directly at the local market.

Further information: ICCO programme officer Guatemala

Three main type of social enterprise strategies have been indentified: empowerment strategies, intermediation strategies and resource mobilization strategies.

Empowerment strategies

Empowerment strategies have the objective of making the primary stakeholders own, control and manage the enterprise or enterprise systems. This strategy may be self initiated by the primary stakeholders and led by the social entrepreneur. There are two types of empowerment strategies; the direct empowerment strategy and the devolutionary strategy.

In the direct empowerment strategy the social business is substantively owned, controlled, and managed by the primary stakeholders at the point of inception. Depending on the actual condition of the primary stakeholders, social entrepreneurs need to provide a gestation period of capacity building and capital building among the primary stakeholders before the social enterprise can be actually set up or becomes operational. Direct empowerments strategies work well in changing the market structures and conduct agribusiness marketing systems.

The devolutionary strategy shares the perspective of making the primary stakeholders own, control and manage the enterprise system. But it tries to speed up the process by making the primary stakeholders avail of the services they need. Here, the social entrepreneurs raise the capital necessary and become the owners, decision makers and managers of the social enterprise in the beginning, to allow the primary stakeholders to immediately avail of the services. A capacity building and capacity build up program is then put in place, the success of which determines the length and nature of the divestment and devolutionary process. This strategy has actually evolved in response to the reality that it takes time for the poor to build the confidence and develop their capacity to become owners and managers of social enterprises.

Intermediation strategies

Intermediation strategies are mainly concerned with providing primary stakeholders access to critical services in their numbers. The social entrepreneurs in this context set up a social enterprise they own, control, and manage and make it grow. Such a social enterprise then acts as an intermediary organization providing a growing number of the concerned primary stakeholders immediate access to one or a combination of services, such as product development and marketing, as well as financial, technological and in some cases comprehensive services for enterprise and business development. Intermediation strategies are more concerned with scale or extent of outreach rather than ownership by the primary stakeholders of the social enterprise. However, ownership by the primary stakeholders may be incorporated as a secondary agenda.

There are two variations of intermediation strategies: functional and progressive. The functional type has the objective of providing a service or a set of services to which the primary stakeholders have otherwise little or no access. The progressive type recognizes and makes the provisions that address the need of at least a segment of the primary stakeholders to develop as part owners of the intermediate organization, or as independent social enterprise that would no longer need assistance from the intermediary organization in the future. Intermediary organizations could start as functional intermediation strategies, but over time shift to a progressive intermediation strategy. The essential difference between the progressive intermediation and the devolutionary empowerment strategy lies in the extent to which divestment and management are turned over to the primary stakeholders over time. The progressive intermediation strategy allows only minority shareholdership and control, while the devolutionary empowerment strategy allows minority to full shareholdership and control.

The PRADAN approach: livelihood for the poor perspective in India

Professional Assistance for Development Action (PRADAN) is a large NGO in India with over 20 development projects and 250 staff, mainly in the central, northern and eastern part of India. PRADAN's development approach is innovative: new products are tried out at a scale big enough to learn from, small enough to be adaptable (usually between 300 and 1,000 households). The focus is very much pro-poor, as the target group is the casteless and tribal population. The general philosophy is that productive activities should be with the lowest risk and investment possible and best returns for the producer.

The producer cooperatives are an important mechanism in the Pradan approach, as they allow scale economies to be achieved as well as spreading risk through price stabilisation. These cooperatives are set up for input provision and marketing under professional management, initially funded by Pradan, while other costs are borne by the cooperative. As soon as the cooperative reaches a preset turnover/profit target, salaries are paid by the cooperative as well. Pradan continues to play a role on the Board in order to empower the board membership vis a vis the manager.

Besides the cooperative model, Pradan also applies the business model in servicing (tasar silk worm rearing, mushroom spawn production) and marketing (TASAR the marketing organisation for fabric). The latter is registered as a company with the Associations of producers as shareholders and board members. One of the exemplary Pradan initiatives has been the promotion of yarn production. Women used to produce yarn by hand, causing irritation and sometimes infection to the thigh as women continuously roll the hand reel along it. PRADAN introduced reeling machines to women's producer groups. The government provided subsidies for the buildings, some of the investment and a loan to the producers. The producer groups are registered as a company rather than a cooperative and each of them is aided by a local manager who is recruited and paid by the producers. Most producers operate foot propelled machines, which contributes to better quality but implies extra costs due to the extra fuel required for the generator. Women are paid for yarn produced minus costs of cocoons, power if used, manager's commission (he is not paid a salary but a commission depending on the grade of the yarn). Women make between 35 and 45 Rp per day (6 to 7 hours) through this activity, which adds up to an income of some 1,000 Rp per month, depending on their skill, productivity and quality as they are paid per kg of yarn produced. Currently some 600 women are producing yarn in independent production groups of 20 to 30 women.

Further information: Programme Officer India, Local Market Advisor Asia

Resource mobilization strategies

Resource mobilization strategies are market engagements undertaken by development agencies, to generate income, surplus or profits from charging fees for services rendered or from enterprises purposely set up for such an objective. Here the income, profits or surplus generated by the resource mobilization program or social enterprise are channelled back to the development agency's coffer to help finance its core development program or operations.

V.1.2.2. Producer organizations as specific example of social enterprises

One example of social entrepreneurship with significant importance is the economic producer organization. ICCO has a long history of facilitating the establishment and development of producer organizations, especially in Latin America. These experiences are also used for inspiration in Asian programmes and slightly in Africa. Due to its importance, this chapter presents the commonalities and main differences of producer organizations.

General characteristics of Producer Organizations.

Economic producer organisations (POs) are a specific business model within a supply chain, different than other business models (private companies, one-person economic agents, etc.). They used to have roles and interests that are qualitatively different than the sum of individual interests of their members. It has other, but complementary, interests than individual smallholders' producers. Not the farm gate price is their prime concern, but the margin on commercialisation of production. Profit is not their prime objective; instead they look foremost to ways to maximize the turnover of products from their members. Generating profit (or surplus) on economic activities is however a necessity as they struggle to meet ends as an intermediary enterprise: pay staff; pay organisational expenses of member consultations; pay taxes; etc. Their commercial activities are mostly realised in straight competition with private actors in the chain (middlemen). This makes that marketing skills in trading and processing of these economic producer organisations are qualitatively different with the skills that individual farmers need to have. They will look at higher margins and low transaction costs, while individual farmers will look for higher prices and better marketing outlets for their primary products).This inherent tension between maximising members profits (trying to pay fair prices for inputs) and maximising the PO's profits (looking for high margins) is a special feature of the POs distinct from the commercial business model. In a competitive market with much competition and small margins between consumer and producer prices, the only way for a PO to resolve this tension is to commercialize high volumes.

Every country has its own legislation related to associations, cooperatives and commercial enterprises. These differences tend to obscure the fact that in many cases they are working in just the same way. In several countries there are 'labels' to bring all these formats under one and the same umbrella. Rural Agro-enterprises (Colombia - (Kaganzi, Ferris et al. 2005), Associative Rural Enterprises (Ecuador, Peru - (Camacho, Marlin et al. 2005)), Economic Peasant Organisations (Bolivia - (Ton and Bijman 2006), Rural Specialised Economic Cooperative Organisations (China), Solidary Economy (Venezuela), etc. are all labels that aim to define this sector of horizontal alliances that are present in the rural reality of developing countries, but these labels are seldom unambiguously defined in legislation. It is important to realise that in many former socialist and communist countries the label "cooperative" has a very negative connotation, which is not easily overcome.

Differences between producer organizations

Different types of rural producer organisations have been distinguished based on different criteria like the type of farm or firm that the members hold and the function that the organisation has for its members, their legal formats, and their levels of aggregation.

Differences in function

Another useful distinction can be made between community-based associations on the one hand and commodity based organisations on the other hand. Community based associations, sometimes called self-help groups, are built around customary principles and ideas of promoting and protecting individual as well as collective well-being. These POs combine economic, social and political functions and represent the wider interests of the community in which they are based. Commodity-based organisations, like marketing cooperatives, primarily concentrate more on their economic function. This function is usually the marketing (and processing) of products generated by the members' farms. Sometimes a PO is established to support the production and marketing of one single cash crop (like the single-purpose cooperatives). Often, however, the PO mirrors the diversified farming systems of its members, taking care of marketing (and processing) of the different products coming from the members' farms and providing a range of services to their members, from the supply of inputs to the marketing and processing of farm products, (like the multi-purpose cooperatives.

Differences in legal formats
When a horizontal alliance is in the process of structuring itself, formalisation of the group in rules, by-rules and legal registration is not necessary and can even be very unproductive. In this initial stage, farmers will have to get to know each other and explore the reason for collective action and the potential problems involved. In this initial stage, some people will be convinced of the added value of the horizontal alliance; others will not and stop participating. However, once the vision and mission of the organisation is clearer and relationships with third parties become important, this formalisation will often be a must. Support from donors, contracting with market parties and other stakeholders, collective credit obligations, etc. are no longer based on trust and social norms, but will be regulated by laws and regulations. The most urgent problem of informal organisations which may sometimes force them to a premature formalisation is the need of third parties to know exactly who they can talk to as a representative of the group. A board has to be elected and the responsibilities of these board members will have to be defined. When they submit a proposal or sign a contract, it must be clear who they are, who they represent and who can be held responsible if problems arise (Mendoza and Ton 2003).

Especially when there are financial responsibilities and liabilities, the formal recognition of the group is a must. Especially the issue of 'who responds when the contract provisions are not fulfilled as agreed?' is a central concern in contracting. The group then becomes a 'legal person' instead of being just a group of 'natural persons'. In most countries, three different legal codes exist that can provide this legal 'backup' of their internal organisation and relations with third parties of groups of farmers:

- ✓ Association (Civil Code)
- ✓ Cooperative (Cooperative Law)
- ✓ Company (Code of Commerce)

These laws and regulations differ between countries and especially the differences between 'associations' and 'cooperatives' in internal organisations can be quite small. In legal terms the differences can be big, as most countries have legal restrictions for engaging in commercial transactions for associations and the three categories used to be treated differently in the tax regime. There can also be important differences in access to credit and financial support. Furthermore there are generally obligations regarding the internal organisation and rights and obligation of members/shareholders and board or hired management. An important and often decisive factor for choosing one of the three legal formats is the financial responsibility towards third parties and the need for member capital to start operations. The differences between the three legal categories can be summarised as in table 3.

Table 3: Functionality of the main legal categories of POs

	Members financial contribution	Members financial Risk	Works best with strategic function
Farmers' association	+	-	Services to members
Farmers' Cooperative	+	+	High volume marketing for members
Joint private enterprise	++	++	High profit rate for share holders

Differences in levels of aggregation

Another typology can be made on level of aggregation. Figure 15 distinguishes between five different types:

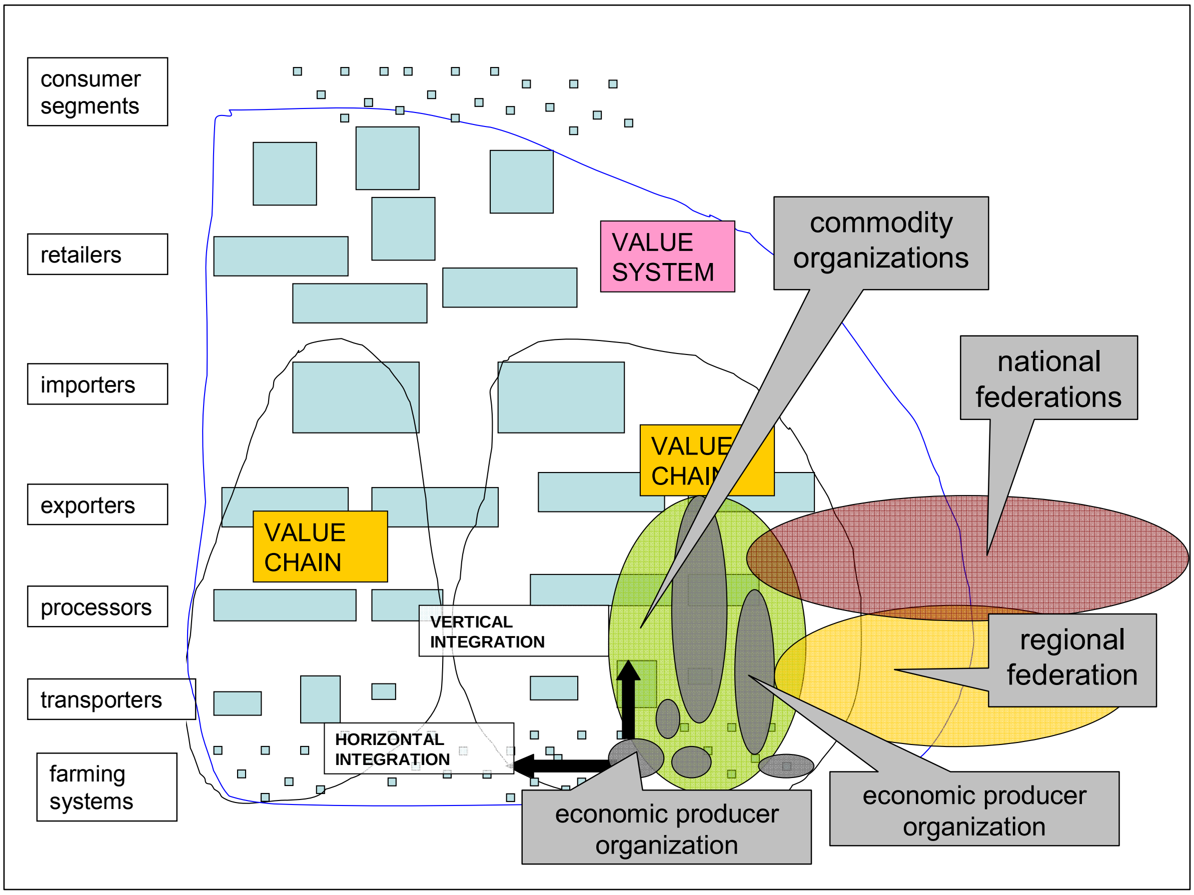


Figure 15: Different types of producer organisations in chain development

- First tier economic producer organisations are the most common feature of farmers' organisations in value chains. They have economic activities related to marketed commodity output in the value chain. They can have second tier commodity organisations, but also second tier regional interest representations.
- Second tier commodity organisations represent the economic producer organisations on commodity issues towards the government
- Second tier sector interest representation federations are generally territorially or administratively organised and group farmers' organisations among different commodity chains
- Third tier national confederations or networks are the usual interface with national and international governments and institutions. They generally have no economic services to their members, but focus on advocacy, training and organisational

strengthening of their members. Some of them have a mix of second and first tier organisations.

- o Exceptional case: Farmer-led chain networks. In chain networks or chain platforms (in French: *Interprofessions*) different chain operators are organised to tackle chain specific issues. These organisations or networks group primary producers with other chain operators and are therefore generally not considered to be genuine farmers' organisations. Farmers' organisations with strong vertical integration activities, however, can eventually become the dominant actor in the chain network, making it a farmer-led organisation. An example of this is the FNC (National Federation of Coffee Producers) in Colombia.

Differences in founding history

Producer organisations with direct membership of farmers can emerge as a result of different processes. Wennink and Heemskerk 2005 distinguish different farmers' organisations according to their origins and aims:

- ✓ Farmers and other village groups created on the initiative of state services or non-profit private-sector entities; often still evolving under their supervision. In Africa, they were often created during the colonial era or just after independence, with a cooperative-like constitution and a mix of social and economic objectives. They developed according to prescribed and/or imported models, with outside interference in management.
- ✓ Producer groups organised by parastatals or private enterprises to handle logistics for agricultural input supply and the marketing of export-destined cash crop products. They were often created by parastatals that were cash-crop based but had a rural development mission.
- ✓ Producer groups, such as outgrowers' associations and organisations initiated with the assistance of externally funded agricultural diversification projects.
- ✓ Community groups formed under village leadership with a strong community development focus. They attract funding and other support from outside. Some are firmly rooted in the village community, others result from outside intervention, for example community driven development programs.

V.1.3 What are the points of attention when developing social enterprises?

- ✓ When developing social enterprise initiatives tensions are bound to arise. One strives to increase the bottom line of a social enterprise, the main purpose of uplifting the lives of its intended beneficiaries might blur because enterprise performance and the salaries of the managers could become the main preoccupation rather than the mission. At the other end, if one focuses too much on the social mission, the sustainability of the enterprise might get sacrificed along the way.
- ✓ It might be useful to have an overview of the existing organisations in a country or intervention area. This overview will give ideas on potential partner organisations and the organisations that can be 'networked' in support of existing partner organisations. The following format may help grasp the diversity of social enterprise organisations in a country. It stresses two dimensions: levels of aggregation and type of service provisioning. It leaves out the issue of legal format.

Table 4: Typology proposal for RPO sector overview

	financial services (e.g. SACCOs)	economic services (e.g. marketing)	political services (e.g. advocacy)	social and technical services (e.g. training)	special services for women (e.g. gender)
First tier (local direct membership organisations)					
Second tier (regional federations/platforms)					
Third tier (national federations/platforms)					

In each cell you can write down the name of the organisation. However no strict interpretation must be given and organisations might well be placed in more than one category. If necessary a subdivision in each cell can be made according to the commodity in question. Direct membership organisations working at grassroots level will be mentioned in a generic sense. Organisations at regional and national levels are identified in the matrix with their abbreviation. Each cell/column can be described in a paragraph with a qualitative assessment of the importance of each category according to some points:

- o Importance of the (aggregate) social enterprise sector in relation to other actors (e.g. private companies, individual households, NGOs, state services, etc.) considering their importance as service providers.
- o Internal linkages and competition between the different social enterprises active/working in the same category
- o Relative size of the organisations related to their coverage of the target population. The target population will be captured twofold: the population targeted by the social enterprise (e.g. women, ethnic group, commodity); and the population targeted by the NGO (smallholders, poverty, etc.). Many organisations do overlap in coverage (many farmers are members of more than one social enterprise as they may provide different services), so graphic comparisons of organisations on 'coverage rate' or 'importance' will have to be used very carefully.

✓ ICCO programme officers will often be in contact with social enterprises that are being supported or that want to receive support, with or without a NGO as intermediary. There is a risk of external support interfering with the necessary internal reflections in the social enterprise on their 'raison d'être' and inclining them to engage in services/function that are not the most strategic and essential. The ICCO programme officer must have an idea about the broader sector and the history of the organisation to prevent this pitfall. Not all social enterprises are suited for support, particularly not when this support is intended to contribute to the value chain development and market linkages.

✓ It is important to take a critical stance towards social enterprises when they request support for value chain development (or when they are presented by others as partners in value chain development). It is quite difficult to get a solid idea of the functioning and performance of a social enterprise from a grant proposal. Additional information/informants might be necessary. It is useful to let the social enterprise defend the reason for its existence beyond a mere description of membership and legal situation, such as explaining:

- o the experiences that convinced it about value chain development
- o the ways in which it has resolved the inherent tensions between collective commercial entity and individual opportunistic behaviour.

- o the internal procedure it has to increase ownership, participation and transparency

Opportunistic behaviour and free riding

- ✓ Most social enterprises in developing countries do not have a monopoly in the market. Their members can sell their product to intermediaries other than their social enterprise. This tension between the collective interest, being member of the social enterprise and/or economic producer organisation and the individual interest of the farmers points to the central challenge in organisation building of social enterprise/economic producer organisations: prevent members' individual interest prevailing above the collective interest of the organisation at large. Opportunistic behaviour of members must be tempered by institutional arrangements within the organisation. Some examples:
  1) When the organisation needs member capital by membership fees or some sort of shareholding by members, this must be done in a convincing way. Members who provide that capital must see sufficient benefits from doing so, compared to the alternative that they do not. This 'incentive' can be achieved by various institutional arrangements: giving them interest on capital; giving them more shares in the distribution of profit; condition marketing possibilities to the effective payment of the capital (e.g. it entitles them to market a specific quota of production); giving them access to special services (e.g. credit); etc.
  2) When the organisation contracts with a trader, processor or exporter, it must deliver quantity and quality in exchange for an agreement on price. In some cases, a better price can be paid by other intermediaries to a selective group of members (e.g. those close to the village/city). Side-selling by members to third parties, not through their social enterprise, used to be a major problem especially when staple products were involved. Institutional arrangements that have emerged to tackle this are various: explicit prohibition with severe sanctions (fines, forced resignation); provide additional services to villages that perform better; field level registration systems for improved detection; etc.

As these examples show, the problem of opportunistic behaviour is inherent in all forms of horizontal alliances but the institutional arrangements to 'resolve' these tensions can vary considerably. Learning by organisations through analysing experiences in other areas, or even other countries, can be an important support activity to prevent them reinventing the wheel.

Ownership and participation

The degree of control by the members of their organisations is difficult to assess at first glance. However, several aspects can give some idea.

- o A good check is to ask for the founders of the organisation. If the organisation has been founded by the present board members, this can indicate a problem of member control or failing internal democracy. However, this is not necessarily the case. Many social enterprises, especially of smallholders, have a limited number of qualified people to take on the role of external representation.
- o Membership used to be voluntary. However, many organisations do register new members. The existence of a membership registration is an indicator of the organisational strength. However, many social enterprises do not have a proper mechanism for de-listing members who leave the organisation. Good organisations will have experiences with members that decided to leave the organisation. Often these stories give an idea of the members' ownership of

their organisation, e.g. forcing members to leave the social enterprise generally indicates organisational strength and ownership, not the reverse!

- Many social enterprises work with paid staff. If these are members, it is important to know who contracted the members and whether the organisation has sufficient capacity to supervise him/her and terminate the contract if necessary. If the paid employee is not a member (the usual situation) but a hired professional, it is good to check the responsibilities of him/her relative to the board members. A good organisation can specify moments in time when the distribution of tasks between board and management were defined or contested.
- Social enterprises will almost always manage some funds. The management must report to the board; the board has to report to the members. The existence of minutes of a meeting (usually the General Assembly) where the financial reports have been discussed gives some idea about the degree of participation and ownership of the members and the transparency of the organisation.

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V.2 Business Development Services (BDS) for the development of rural enterprise

Why is business development services a useful intervention strategy for ICCO employee?

Any business needs certain services (like telecommunication, transport, bookkeeping, etc) to be able to operate, grow, compete and function well. Business Development Services (BDS) specifically focus on the development of rural enterprises (also) using these services.

The development of a healthy private sector and, within this aim, supporting small entrepreneurs has been an important element of development strategies implicitly or explicitly for a long time. At first, this was seen as a way of assisting the unemployed and under-employed, who tried to make ends meet in the so-called informal sector. The first programmes set up for this purpose concentrated on financial services. The success of micro-finance programmes and institutions demonstrated that there was a need for these services and that they could have a positive impact on both poverty alleviation and income generation.

However, it soon became clear that financial services alone were not the solution, as many small entrepreneurs lack skills and access to markets and information, to name just a few shortcomings. All these shortcomings considerably reduced the effectiveness of the financial services, sometimes to the extent that they became counterproductive. For example, if an entrepreneur can increase his/her production thanks to a bank loan but is unable to sell the additional products due to lack of marketing skills, the net effect will be negative. Therefore it is important to realise the necessity of good BDS when implementing other (financial) services.

V.2.1 Why are BDS important?

As mentioned before, all enterprises need certain services to ensure their business run well. In many developing countries, the market for these services is underdeveloped due to constraints on the supply side and/or the demand side. An example of a supply side constraint is the lack of knowledge and skills in conducting market research by many providers. They therefore do not know what is required and subsequently deliver inappropriate services. An example of a demand side constraint is the lack of critical mass of micro and small enterprises. Consequently they are not considered by larger buyers and have to depend on informal traders (who have their own limitations and are not often reliable buyers) (Posthumus 2006).

V.2.2. What are BDS?

The aim of BDS is to support enterprises in their development (Marr 2004). BDS are broadly defined as: “non financial services that are provided to entrepreneurs to help them overcome certain obstacles so that their business can operate better and eventually grow” (Marr 2004, Posthumus 2006). BDS have virtually no limitations or boundaries in what they may address (infrastructure, regulations, etc) but they can be divided into **strategic support,** such as consultancy, training, capacity building, building links with strategic partners and business plan development, and **operational support** such as transport, advertising, technical assistance and accounting (Bussel 2005, Marr 2004, Posthumus 2006).

Low-cost irrigation systems for horticulture growers in Maharashtra, India

Water has been a major constraint in the development of horticultural activities in Maharashtra, India. Scarce groundwater as well as non-availability of affordable irrigation equipment have been the prime issues for small and marginal farmers. Although drip irrigation was used in the area, most of the systems available in the market were designed to fulfil the needs of affluent farmers. Even after the government subsidised the drip systems, these generally remained beyond the reach of small and marginal farmers. Moreover, the non-availability of government funds as well as the cumbersome procedure added to the misery of farmers.

International Development Enterprises India (IDE-I) is an NGO focusing on rural development through irrigation development. IDE-I promotes drip irrigation and other low cost and low water-use systems. Rather than providing the services themselves, they support local private businesses to play this role. IDEI commenced operations in Maharashtra on 1 October 2001. It adopted this BDS approach with the objective of facilitating market development to address the demand and supply side constraints to improve the socio-economic and environmental conditions of small and marginal farmers. The programme focused on horticulture crops which are widely cultivated in Maharashtra. These are high value fruit crops (banana, sweet lime, orange, pomegranate, etc.) as well as vegetables (egg plant, chilli, tomato, gourd) for which relatively better market links exist in the region.

To address the issue of irrigation for smallholders, IDEI introduced affordable, divisible and simple drip irrigation technologies. The range of products includes Bucket Kit, Drum Kit, Easy Drip and Customised systems. These can cater to the range of irrigation needs from kitchen garden to medium sized horticultural farms of about 1 acre. The simple design enables farmers not only to manufacture/ assemble these systems locally but to easily install and maintain these systems. The drip irrigation system costs between 50 and 150 Euros per 4000 m2.

In its role of facilitator, IDEI explored and identified providers for assembling the systems. The source of components was identified and the assemblers were linked to these manufacturers. These assemblers procure components from various manufacturers/ suppliers, assemble the kit locally as per the needs of the farmers and then sell them to the farmers. IDE-I has worked hard on identifying and capacitating these suppliers. To create demand for the products, IDEI has collaborated with a few watershed NGOs and has leveraged their penetration among the farmers to disseminate information on drip systems. IDEI staff have also initiated demand creation activities in the field. These include various promotional activities such as demonstrations, village meetings, exposure visits, video shows, etc. The acceptance of drip kits can be gauged from the fact that in the very first year the assemblers were able to sell over 5000 systems with no element of subsidy. The numbers have been growing ever since. The increasing demand and interest in drip kits have motivated many local mechanics to join in the project. The increasing number of assemblers has given the farmers a choice of dealers/assemblers. At the same time it has prompted the assemblers to improve their services and product quality. Although IDEI has been promoting the technologies, now the assemblers have themselves started promoting their firms and the products. Some of them even advertise in the local print media.

For more information: Programme officer India

The diversity of BDS is also reflected in the wide range of BDS providers. They can be government agencies, international donors, NGOs, Chambers of Commerce, universities, business associations, private foundations, as well as informal social networks embedded in inter-firm links. Posthumus (2006) focuses on the differences between **BDS and VCD** (Value Chain Development) to prevent the mixing of terminology. He summarises them as follows:

1) BDS focuses on certain actors (in a chain) and BDS providers offer certain (commercially sustainable) services to (only) these actors to enable them to improve their performance.
2) VCD focuses on the entire value chain and promotes joint initiatives by the stakeholders in order to improve the performance of the chain (and chain actors) whereby some of the interventions can be classified as BDS, while other interventions can be classified under different headings (see also Chapter III.4).

Traditionally, BDS to small enterprises have been provided with the support of donor and government subsidies. Such interventions often proved to be unsustainable and have had a limited impact (Posthumus 2006). Since the end of the 1990s there has been a shift whereby the BDS delivery called for the **development of *markets***[17], rather than that of individual institutions alone. This implies a shift in thinking from subsidised supply-led BDS provision to market-determined demand-driven services, where both sides of the market - demand and supply - are helped to develop (Steel *et al* 2000, Gibson, Hitchins and Bear 2001).

Figure 16 presents the core principles of the new approach. The starting point is an emphasis on clearly understanding the *constraints* that prevent suppliers from satisfying the demand for BDS, as well as the *obstacles* that restrain consumers from making their demand explicit. In the diagram, we can see that BDS suppliers may not provide for small enterprises due to, amongst other factors, limited information about their clientele, deficient staff skills, inappropriate products and inefficient organisational structures.

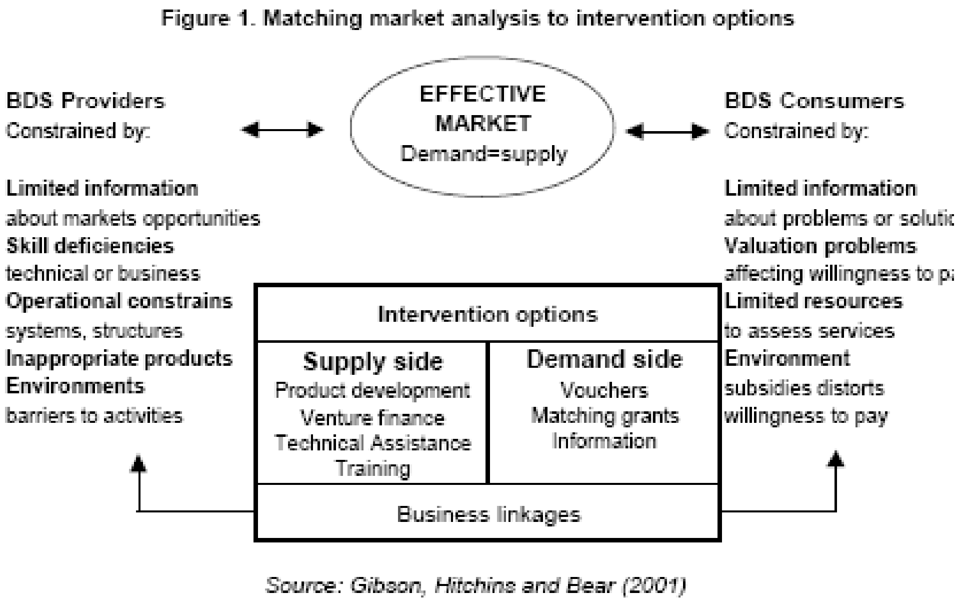

Figure 16: Matching market analysis to intervention options

[17] Some examples of BDS markets are: Communication centres, product transport/ delivery, transport and money transfer, advertising, bookkeeping and accounting, management training, technical training, trade fair, sales on commission, business travel, internet access, info in newspaper/magazine, finance and tax advisory, package and parcel delivery (Miehlbradt 2002)

On the demand side, users may be constrained by limited or distorted understanding about their own needs/problems, limited resources and capabilities to assess market-based services and to determine whether these represent value for money and by business environmental factors, such as the expectation to receive free or heavily subsidised services (Marr 2004).

Following the above mentioned, three different approaches in the delivery of BDS can be identified (Marr 2004): the government driven approach, the partnerships of donors with national institutions approach and the independent approach. These approaches are explained below.

Government driven approach
The government-driven approach is characterised primarily by its aim to achieve national goals, such as higher employment, rapid industrialisation and better export competitiveness in international markets. A *positive* effect is that these government-led BDS programmes reach large numbers of beneficiaries (Marr 2004). One *drawback* of the approach is the distortions it can cause to market prices and the provision of BDS by the private sector. As services are generally delivered in a highly subsidised manner, prices are lower than those determined by market forces. This creates distortions in both the demand for and the supply of BDS. On the demand side, beneficiaries begin to expect free or cheap services even when they have the capacity to pay. On the supply side, subsidised BDS effectively crowd out private sector provision of these services, resulting in overall market inefficiency (Marr 2004).

Partnerships of donors with national institutions approach
The partnerships of donors with national institutions is aimed at delivering services through an existing local institution rather than through the creation of new BDS providers or via direct delivery by international donors. There are three types of organisations that usually become donor partners:

1) Public organisations
2) NGOs
3) Private sector institutions.

Ad. 1. The *advantage* of partnership programmes with public sector organisations is the benefit from the nationwide coverage of these institutions, with the expectation of correspondingly high levels of outreach of BDS delivery. A *disadvantage* or *common risk* is the potentially detrimental control that government agencies may have over the programme (Marr 2004).

Ad. 2. The major aim behind building partnerships with NGOs is to achieve a certain depth of outreach. This means that it is not only important to create high coverage (as with the government agencies) but also to reach the poorer segments of the population in order to alleviate poverty. The advantage of this is that poorer segments of the population are reached. The disadvantage is that these projects are rarely financially sustainable and NGO staff are often not skilled enough, due to high staff turnover.

Ad. 3. The main goal in private sector partnerships is to run BDS programmes with a strong business focus (Marr 2004). The advantages of this is that the BDS programme is influenced by the business-like working culture in which payment for services is more normal than getting services for free. The disadvantage or risk is that these BDS providers tend to serve the upper-end of SMEs and outreach to the target population is decreased.

Training facilities for micro credit clients, La Paz, Bolivia

The Bolivian NGO IDEPRO became known in the region for its successful micro finance programme. In 1991 IDEPRO initiated training activities to strengthen the management and entrepreneurial capacities of its clients. In 1999 it outsourced the micro credit facilities and specialised in business development services. Its services consist of group and customised training programmes. Its target group is micro and small enterprises in urban areas. Initially the training programmes were related to production improvements and trade for SMEs in general. But it soon became clear that it would have to specialise in a number of supply chains to create real added value for its clients. To this end, IDEPRO conducted in-depth studies of a number of chains. Based on this study, it selected 8 supply chains that are most relevant for SMEs in Bolivian urban areas: textile, *castaña* (paranuts), leather, wood, grapes/wine/*singani* (local strong liquor), tourism, quinoa (highland cereal) and *camélidos* (lama/alpaca products).

The development of this activity as a commercial one has not been easy. The main challenge IDEPRO has been confronted with is the limited market it is able to reach and the low segment it represents. Most of its clients are smallholder producers in the informal sector, producing low product quality and limited volumes. Consequently, its clients have problems paying their own contribution. Furthermore, some of these producers feel that these services should be either offered for free or heavily subsidised while external donor organisations are promoting the idea of demanding contributions. IDEPRO also notices that the individual training has become more popular than group training. This is because of its customised nature. As a result, the contributions for individual training programmes are paid more easily than those for group training.

For more information: Programme officer Bolivia

The independent approach

The independent approach is most in line with the shift towards market-oriented BDS. The aim of this approach is to help develop fully independent BDS providers in terms of legal status, financial sustainability and market-oriented provision of services to their clientele.

There are three models (Marr 2004).

1) The first model is to set up **Business Centres** that provide a wide range of non-service and non-sector specific services. It seeks to develop institutions that can provide these services by building linkages with local organisations. In many occasions, start-up subsidies are available from international donors, although only under concrete measures to become self-sufficient.
2) The second model is to **build clusters and linkages**. In this model the services are both sector and place specific. This model is generally applied to businesses of the same sector or same geographical area to cooperate and/or build vertical alliances in order to gain access to BDS. For more information on building clusters, see V.5.
3) The third model of **business incubators** aims at nurturing enterprises in the early stages of their development in order to transform them into profitable businesses that would create jobs in local communities. Businesses are offered a working space and hence become 'tenants' of a Business Incubator; other BDS are also provided. After a period of approximately two years of incubation, businesses 'graduate' and are expected to survive and prosper in competitive local markets.

Ad 1: A major strength of Business Centres is their potential to develop sustainable service providers. A disadvantage is that international NGOs acting as donor cannot become shareholders and therefore their demand for high performance is restricted. Another disadvantage is that pressures on the BDS to attain financial sustainability seem to be at the expense of outreach capacity and the small and poor entrepreneurs are generally affected.

Ad 2: An advantage of clustering is that entrepreneurs can overcome market barriers and gain access to services that would not otherwise have been available to them alone. The major challenge is to overcome the costs of forming clusters and deal appropriately with power imbalances that clusters and linkages can generate.

Ad 3: A major strength of business incubators is their focus on start up and young enterprises. A challenge for business incubators is the macroeconomic environment in which they operate and when to expand.

V.2.3. What are the points of attention when looking at BDS?

The following suggestions are taken from Miehlbradt (2001). It provides a useful overview of some principles to take into account when designing a BDS intervention strategy and also relates to the shift as described under "Aims and Key Elements". It is stressed that these principles are not sacred and may not apply to every situation and every target group. Nevertheless, they are all important to bear in mind and there should be good reasons for neglecting these principles when such is the case. These principles are as follows:

<u>1 Start with a market assessment</u>

To effectively intervene in a market, donors and practitioners must first understand it. What BDS are being offered to targeted small enterprises? Who is supplying them? Are they paying for the service? How else is the service procured? What types of services are in demand by small enterprises? What prices can they pay? Who is providing those services in the market, but perhaps not to small enterprises? What are the weaknesses and opportunities in the market? In order to minimise the market distortion that any subsidy creates in a market, it is helpful to have a good understanding of BDS markets before starting interventions.

2 Facilitate market development rather than providing services

In traditional programmes, donors and governments provide services to small enterprises directly or permanently subsidise services by non-government providers. In the market development approach, donors and governments try to promote transactions between small enterprises and primarily private sector suppliers, facilitating the expansion of markets rather than providing services. Rather than offer financial assistance to suppliers, interventions concentrate on technical assistance and incentives to encourage suppliers to enter new markets, t develop new, low-cost products and expand services to underserved markets.

3   Fit the intervention to the market issue

Because any intervention will change the market, limited and focused interventions are more likely to address a market issue with minimal distortions. Donors and practitioners should target market problems and opportunities identified during market assessment with interventions aimed specifically at addressing those issues. Interventions are designed with specific market development objectives.

4   Use subsidies primarily for pre and post-service delivery activities

Subsidies which directly reduce the cost or price of services are likely to distort markets more than subsidies for pre or post-delivery activities. In the market development approach, subsidies for transactions are avoided or limited to a short duration with specific objectives. Donors use subsidies instead for pre-delivery activities such as the development of service products, test marketing, capacity building and awareness raising or for post-delivery activities such as gathering consumer feedback. Subsidies are also used for monitoring and evaluation.

5   Work towards a sustainable market and have an exit strategy

Like traditional programmes, market development programmes may continue indefinitely unless programme managers have a clear vision for a sustainable BDS market and an exit strategy. In a sustainable market, competing suppliers usually offer a wide range of products and frequently innovate to meet changing demand and capitalise on market opportunities. Development agencies are more likely to end programmes successfully if there is a specific vision for a sustainable market. The challenge is to assess objectively when the market has reached a sustainable level.

6   Separate the roles of provider and facilitator

In many BDS programmes, one organisation performs both the supplier role, offering services directly to small enterprises, and the facilitator role, encouraging other individuals and firms to supply these services. This may present a conflict of interest. Because facilitators usually have a development agenda and suppliers a commercial agenda, mixing the roles often leads to ineffective programmes and inefficient use of funds. If facilitators are publicly funded, they should disappear as the market develops and suppliers or other permanent market actors take over their functions. The exception is if a facilitator can finance its activities by selling services to suppliers, thus becoming a sustainable, permanent market actor.

7   Promote competition and efficiency in the market

Traditional programmes often work with only one supplier, giving that supplier an unfair advantage over others. Instead, facilitators should promote competition among suppliers, usually by working with multiple suppliers. This does not preclude working with one supplier for some activities at some points in a programme, for example testing a new product or in a new or very weak market. However, it means that a facilitator must always be careful to promote rather than stifle competition in the market.

8 Develop a transactional relationship with suppliers

Facilitators should have a transactional relationship with suppliers, i.e. the suppliers should be paid according to the services they provide rather than receive institutional funding (which is unrelated to real output). Programmes working with commercial suppliers have found that it is helpful if suppliers invest their own resources in programme promoted initiatives. If suppliers choose to work with the programme in the same way that they make other investment decisions, weighing costs and benefits, they are more likely to feel some ownership of the initiatives and use programme resources wisely.

9 Tread lightly in markets

Large government and donor programmes have often suppressed private BDS markets or crowded out private suppliers. Even what donors consider moderate financial inflows can damage a promising market. Particularly when poverty alleviation is the goal, donors face pressure to disburse funds. Visible donor involvement in MSE support programmes tends to distort markets, as small enterprises and providers expect subsidies. Donors and practitioners should exercise discipline, matching interventions to the level of the market, emphasising technical assistance over financial inflows and maintaining a low profile. This is difficult but important in markets with weak demand, a common characteristic of low-income consumers.

10 Make programmes flexible and responsive to the market

In traditional programmes, managers specify the steps leading to the achievement of programme outputs at the outset and then, for the most part, follow them. Market development programmes show that a more flexible, entrepreneurial approach is needed. Markets can change rapidly and often react to facilitators' efforts in unexpected ways. Experience has shown that facilitators must be free to respond to the market, taking advantage of opportunities and changing strategies as appropriate.

11 Coordinate donor efforts

It is very difficult and not very effective for a donor to pursue a market development approach if others continue to subsidise transactions and offer publicly funded services in the same market. Free services reduce the willingness of small enterprises to pay. Even if all donors are pursuing a market development approach, coordination is important. In markets with relatively few suppliers, these suppliers can be overloaded or lose their commercial focus if they receive significant financial resources from several donors.

- In addition to the suggestions of Miehlbradt, other points of attention to consider are: the importance of evaluating the performance of BDS programmes. It has been observed that evaluation and impact studies are often a weak point of BDS programmes. Key elements on which performance could be measured are**:**
  - Outreach, meaning both the number of enterprises (scale) and the effort to provide services to people not served by existing markets (access);
  - Cost-effectiveness of programme activities;
  - Impact on MSEs and the wider economic/social environment;
  - Sustainability of business service delivery and supplier institutions.
- A good evaluation is important to make adjustments to the BDS programme. However in the past the targets to evaluate were often difficult to determine. There is also a debate on who should pay for these evaluations: the players or facilitators of the BDS programme (see also SNV site http://www.snvworld.org/cds/rgBDS/introduction.htm).
- The development of BDS can be distorted by external factors. For example, in the case of the ICCO initiative in Gujarat, sales of the IDE-I KB system fell dramatically after the Government of Gujarat introduced a subsidy scheme for regular irrigation systems. Even though the subsidised systems were still more expensive than the IED-I KB system, they became more popular because of a loan component and the

(perceived) higher durability of the traditional irrigation system. In general larger farmers would qualify for the subsidy, while poor farmers were left out.

- In September 2006 a group of Sharepeople participants studied the Gujarat BDS case and produced some interesting recommendations, including:
    - make the KB product more visible in the field through membership club, more frequent after sales contacts etc.;
    - further strengthen knowledge of farmers on farming and irrigation;
    - create demonstration plots;
    - develop a 10 year package deal, whereby farmers can spread payments over 10 years (lease-buy) and systems are maintained (this would need IED-I to link up with rural banks to finance this);
    - improve income from farming by organising reversed auction (the "clock" going down or 'afslag";
    - develop capacity of dealer in marketing.

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V.3 Public-Private Partnerships

Why is public private partnerships a useful intervention strategy for ICCO employee?

PPPs enable ICCO to obtain insight into the workings of markets, access additional resources, develop new models for resource allocation and gain greater credibility and leverage with respect to their own donors. As a result, partnerships for sustainable commodity chain development can help ICCO be more effective at their own core business through a better understanding of the business case side of chain development.

The improvement of market access often has to do with solving constraints in the enabling environment. In some cases this has to do with legislation, procedures, or other barriers that are created and can be removed by public entities. PPPs can be an intervention strategies to define common actions to improve the enabling environment between public and private entities.

V.3.1. Why are Public-Private-Partnerships important

Public–private Partnerships (PPPs) have become increasingly popular in development policy and practice as a means of addressing issues as diverse as health, education, environment, finance, governance and agriculture. They have also become popular as a way to foster the development of innovations through collaborative R&D. As a tool in poverty reduction, PPPs currently form an important tool in the programmes of International Cooperation by the Dutch Government (Hartwich e.a., 2005).

The literature on partnerships shows that PPPs can be beneficial for a number of reasons. They allow organisations with distinct competences to exchange knowhow and facilitate 'cross-fertilisation'. Companies can gain more insight into their effectiveness in addressing societal problems while at the same time obtaining reputational benefits from increased social responsiveness. In the case of partnering for sustainable commodity chain development, partnerships can help companies reduce risk by spreading costs and through e.g. enhanced transparency (Muller e.a., 2006b). More specifically, one can learn from the cases studied by Muller e.a. (2006a) that partnership strategies make a clear contribution to development. Partnerships help improve agricultural output and productivity, employment, value adding, exports and diversification, market access and increase human capital.

Another general assumption behind public-private partnerships is that PPPs present advantages to both public (research) organisations and private sector entities and can generate social benefits[18]. Hartwich (2005) adds that many PPP-approaches seek to outsource public services to private companies. They recommend that, when entering in PPPs, public agents ensure that these partnerships comply with public needs and generate social benefits.

[18] For references to literature, see Hartwich e.a., 2005, page 6.

Public-private partnership for organic sector development in Peru.

In 1989 the Organic Agriculture Network RAE was established in Peru. The main objective of this network is to stimulate NGO cooperation in the promotion of organic agriculture. Due to the growing demand for products and the need for transparency in the production schemes applied, RAE started stimulating the implementation of formal certification schemes. In the early 1990s, this service was provided by foreign entities from the European Union and the USA. In those days, hiring a foreign certifying body cost approximately US$700 per day. This was too expensive for organic farmers in Peru, for which 4 NGOs united forces to create INKA Cert, a local certifying body. In 1998 this entity became part of Biolatina, a regional network of nationally accredited commercial certifying entities. Violating enables local farmers to get certified with international standards.

The growing number of organic farmers also created the need to develop an organisation which could defend their interests and rights. For this the Asociación Nacional de Productores Ecológicos (ANPE) was created in 1996.Currently ANPE has 10.000 members and 16 regional offices and represents half of the Peruvian organic farmers.

By the end of the 1990s, the volume and quality of organic products had increased so much that the sector had to obtain access to new market segments. A private sector entity was therefore created, Grupo EcoLógica, which was responsible for the marketing and sales of organic agricultural products to individual consumers and the retail sector. Grupo EcoLógica was an initiative developed by RAE and ANPE.

At the same time, governmental interest increased to define a clear position with regard to the significance of organic production for the Peruvian agricultural sector in general. For this, the Ministry of Agriculture defined the Law on Organic Production in 1998. Also the National Commission for Organic Production (CONAPO) was created. In this commission, representatives of RAE, ANPE, Biolatina, and Grupo Orgánica are seated. Together they have developed local regulations for organic production. Currently, this multi-stakeholder commission is responsible for the development of the national service for agricultural health (SENASA) and the promotion of organic agriculture in Peru.

For more information: Program officer Peru

V.3.2 What is a Public-Private partnership?

The Dutch Ministry of Foreign Affairs (memorandum 1, 2005) defines PPPs as follows, in accordance with definitions by the UNDP, World Bank and World Resources Institute:

"A partnership is a voluntary cooperation arrangement between actors from government and non-government sectors (NGOs, the business community), that agree to work together to achieve a common objective or carry out a specific task, by sharing the risks, responsibilities, resources, competencies and benefits."

A partnership[19] is a form of agreement in which autonomous organisations proceed to make sustainable agreements and thus coordinate parts of their work. It leads to a diversity of collaborations that have a sustainable intention, but are finite in character. Partnerships are collaborations between organisations, not within organisations or between teams or on a project basis.

A partnership is a *process* focused on specific goals; there must be commitment by people to invest energy in the process. It requires dedication of resources and must have significance and value. Organisations will make joint decisions and will therefore have to cede "bits" of autonomy with the expectation that it will lead to benefits/advantages. There is no direct control; mutual influencing, communication, negotiations and trust in each other's intentions are the main characteristics. It can be at odds with the (in-company) need for control and reduction of uncertainties.

Partnerships are built on the basis of *sustainable agreement.* Partnerships are based on explicit and implicit agreements which may take all kinds of forms. There may be informal or oral agreements, formalised in complex legal contracts, new organisational structures (joint ventures), etc. *Partnerships are finite in character*: A one time transaction is not sustainable, nor is the acquisition of one organisation by the other, as the acquired organisation gives up its autonomy (See Figure 1).

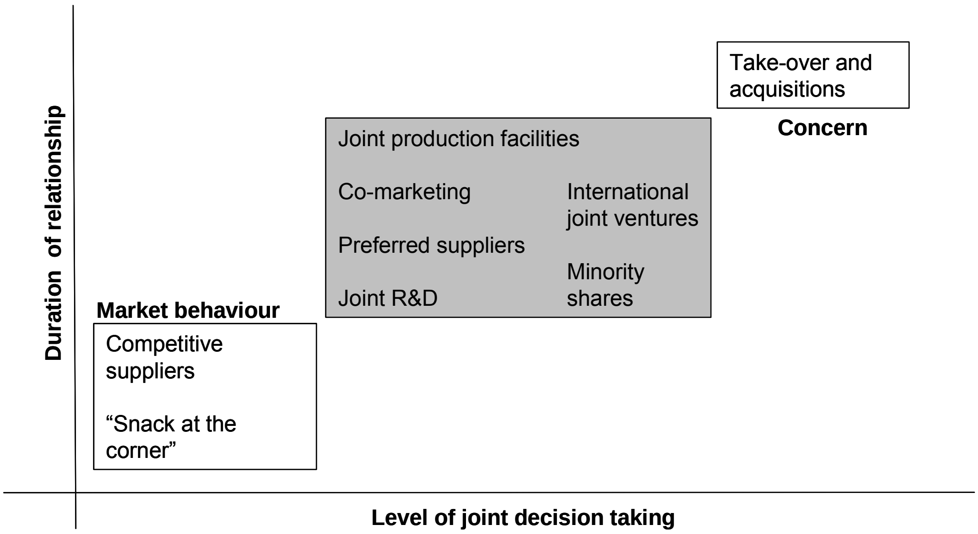

Figure 17: The positioning of partnerships (Kaats e.a., 2005)

In a public-private partnership (PPP), actors (organisations, associations, firms etc.) from public and private sector form a strategic alliance with a determined objective.

[19] This paragraph is adapted from Edwin Kaats e.a. "Organiseren tussen organisaties", 2005, pages 29-31.

In the evaluation of four case studies of PPPs for market chain development, Muller e.a. (2006a) state that the term ‘Public-Private Partnerships’ can be confusing in cases when only NGOs are involved. In such cases, it may be more appropriate to classify the partnerships as Private–Community Partnerships or Civil Society – Private Partnerships. In some cases partnerships seem more exclusively centred on NGOs (Civil Society Partnerships).

Kaats e.a. (2005) distinguish three key levels in partnerships:

1. ***Network level***
   Partnerships can take place within different type of networks. This depends on the ambition and strategies of individual organisations (partners) to take part in groups (networks) as a starting position to developing partnerships. The choice of position of an organisation (in the periphery, centre or free space) will determine the choice of specific partnerships. Partnerships are certain agreements between different institutions; this is in contrast with clusters which are geographically grouped institutions linked by complementarities, but necessarily having partnerships with each other.
   Main questions: What are my ambitions? What are my capabilities to form part of a network? What can I offer the network? What can the network offer me?

2. ***Relationships between organisations***
   Four basic forms of partnerships are distinguished, based on the extremes of two axes (see Figure 18):
   a. Intention of the partnership: improving versus innovating
   Main questions: what is the main objective of the partnership: to do things in a smarter, better way (improvement)? Or do I want to develop new possibilities to do things (innovation)?
   b. Character of the partnership: sharing versus exchanging
   Main questions: does the partnership focus on integrating organisation processes or is it limited to a sustainable form of exchange (services, products, information, knowledge).

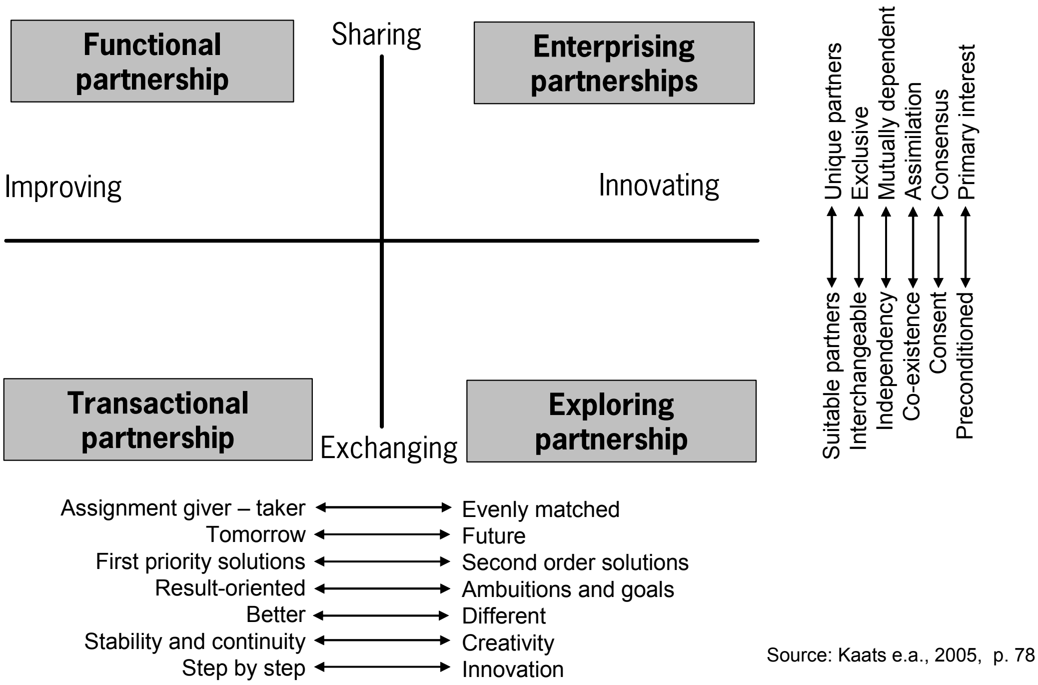

Figure 18: Basic forms of partnerships
Source: Kaats e.a., 2005

3. ***Competences of the organisations to enter into and maintain partnerships.***
   a. *Alignment:* Align the internal organisation to the activities that are carried out in partnership;
   b. *Relationship fit:* Judge whether the partnership fits not only in terms of strategic opportunities but also in terms of organisation culture, management style and operating style;
   c. Build up a *strong working relationship* during negotiations;
   d. Develop *common work and ground rules*;
   e. *Dedicated alliance managers:* Have managers feel responsible for the partnership;
   f. Compose teams with sufficient *collaboration skills*;
   g. *Collaborative corporate mindset*: Think and work with partnership relationships as primary focus;
   h. *Manage multiple relationships*;
   i. *Auditing alliance relationships:* Audit (monitor) relationships with partners
   j. *Manage changes* during partnerships

In line with the three levels, Muller e.a. (2006b) also refer to the need for organisations (NGOs) to assess their ('external') positioning towards companies, other NGOs and society; towards partnerships as strategic decisions to achieve core objectives (ambitions); and the ('internal') capabilities of partnering. The question of whether or not a strategic fit exists between the organisation's capabilities and the possibilities offered by partnering can be addressed through a SWOT[20] analysis.

Other important elements for achieving win-win situations in partnerships are related to the demonstration of commitment, open communication lines, a clear division of responsibilities and partners behaving towards each other with integrity.

V.3.3. What are the points of attention when looking at PPP?

- ✓ For the development of sustainable commodity chains through PPPs, the need for stability and shared vision in partnerships in the turbulent and ever-changing context of global commodity chains requires more attention on understanding the dynamics of partnerships. Contingency or scenario planning may offer ways to manage uncertainty. Therefore partnership must be based on an explicit vision of chain development.

- ✓ Some pitfalls during PPP refer to the multiplicity of roles played by multiple actors at various stages which does not contribute to transparency in the partnership and confuses partners if not communicated clearly. Different stakes and divergent interests associated with different roles may lead to tensions in the partnership.

- ✓ Another pitfall is specifically NGO-related and refers to the desire to ensure success which makes NGOs vulnerable to manipulation and lose focus on the best interests of overall chain development. NGOs furthermore have a tendency to (over)emphasise non-commercial actors in a project, which relates to limited trust in the (demonstrated) motivations of the companies involved. Nevertheless, companies demonstrate a business development role and explicit CSR-based motives for being engaged in addition to their own interest of sourcing high quality products to further their own business. In addition to the 'push' implemented by NGOs, they fulfil a clear 'pull' function to make chains work.

[20] SWOT stands for 'Strengths, Weaknesses, Opportunities and Threats' and is a tool that relates the organisation-internal side (strengths and weaknesses) to the organisation's external environment (opportunities and threats).

- ✓ On the other hand, Muller e.a. (2006a) signal the risk of cooptation for NGOs participating in partnerships, particularly where a clear imbalance of power exists between the company and the NGO. Particularly in the start-up phase, business and NGO cultures may clash, for example when visions of sustainability diverge from visions of profitability.
  - o Thus, points to address:
    - The identification of risks associated with weak actors in the chain (such as organisational weaknesses and lack of commercial experience);
    - Partners must be able to address differences in vision explicitly and have an exit strategy;
    - The development of commitment and trust is very important, including a business development role played by the company;
    - Bring all key actors under one umbrella (formalised if possible);
    - Maintain a 'helicopter view';
    - Develop tools for comprehensive assessments of the strengths and weaknesses of the roles each actor can potentially play;
    - Assess how those strengths and weaknesses can affect the outcome;
    - Monitor the dynamics of (changing relationships within) partnerships – organisations come and go, or adapt their mandate;
    - Dynamics should be linked to explicate exit strategies and this should be based on a shared vision.

- ✓ Several evaluation studies of PPPs (Hartwich, 2005, Muller, 2006a) point out that most partnerships have not developed evaluation mechanisms to measure the benefits or success of PPPs or their contributions to development. Moreover, in the evaluation of cases of PPPs involving agricultural research, the public partners were found not to have a clear picture about the overall public goals or their organisation's strategy to attain them (Hartwich, 2005). Synergistic rewards in partnerships are often sought and referenced but rarely fully articulated and measured (Dobbs, 1999 in Brinkerhoff, 2002). Muller e.a (2006b) indicate that explicit *assessment tools* could be useful for identifying and evaluating the interests, capabilities, weaknesses, potential for mutual trust and potential roles of various actors on a more structural basis.

- ✓ In time, partnerships for the development of market chains will have to give way to market mechanisms if the chain is to be sustainable. In other words, the facilitating role played by the partnership structure in providing 'public goods' and reducing uncertainty and risk in the chain should eventually give way to market mechanisms, substituting the partnership's function as a tool for reducing uncertainty and risk.

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V.4 Clusters and strategic alliances for local economic development

Why is clusters and strategic alliance development a useful intervention strategy for ICCO employee?

A business cluster is a geographic concentration of interconnected businesses, suppliers and associated institutions in a particular field. Clusters are considered to increase the productivity with which companies can compete, nationally and globally.

Many cluster development initiatives originate from or are being promoted by multilateral and bilateral agencies. Despite the large number of cluster developments, there is little evidence of explicit attempts to use cluster development to promote a poverty alleviation agenda, beyond the desire of employment growth (Nadvi and Barrientos, 2004). For ICCO programme coordinators it is important to consider this critical gap within the policy framework on cluster development and to articulate it more clearly in the poverty agenda. There are several options to do this:

1. Poverty targeting: identifying clusters with a high incidence of poor house-holds.
2. Clustering advantages: promoting activities that raise local external economies which have a direct effect on poverty considerations.
3. Poverty strategic support: distinguishing between the kinds of support needed for poorer workers and entrepreneurs and for those in the cluster that are better off.
4. Training: make it a critical aspect of raising productivity, skills and enhancing competitive abilities of clusters.
5. Recognising cluster differences: clusters produce winners and losers. It is important to ensure that marginal groups are not weakened through this process.
6. Cluster impact assessment: using cluster actors to identify their own notions of poverty in terms of capabilities and well-being, but also to use locally ongoing poverty monitoring and evaluation within clusters.
7. Pro poor partnerships: using cluster mapping to identify key stakeholders that can be more effective in supporting pro-poor policy interventions.

V.4.1. Why are cluster development and strategic alliances for local economic development important

Industrial clusters lend themselves to poverty concerns both directly, through employment, incomes and well-being generated for the working poor, and indirectly, through their wider impacts on the local economy.

There are numerous examples of clusters at early stages of industrialisation, engaged in labour intensive sectors and operating within, or on the boundaries of the urban informal economy. In addition to labour intensive urban clusters dominated by small, often informal, enterprises, there is also evidence of rural clusters providing employment for the rural poor. Indonesian rural “cottage industry” clusters produce a range of products, from woven bamboo, food products to furniture and garments. Some of these clusters even export. Nevertheless, these examples do not always lead to the desired objective of improving the economic development of the poor. To analyse how clustering helps small producers and poor workers improve their economic positions, reduce their vulnerability to exogenous shocks and enhance their capabilities, it is important to focus on the processes associated with clustering.

Within the growth and competitiveness focus, cluster policy initiatives centre on:
- promoting joint action within clusters that help firms compete more effectively,
- support the provision of business development services to clustered producers,

- help clustered firms make links with external traders and wider global markets, and
- assist clusters to upgrade their technical capacities by improving their products, their processes and organisation of production, and widening the range of functions that clustered firms undertake.

Thus, many of the policy initiatives concentrate on managerial, institutional and knowledge-based activities within clusters, on cluster innovators and on business development services. These address the need for intervention by external actors, particularly the state, in addressing collective failures and promoting the positive gains that often go undeveloped within clusters.

V.4.2 What are clusters and strategic alliances for local economic development?

An industrial cluster can be defined as a geographical group of inter-connected companies and associated institutions in a particular field, linked by commonalities and complementarities (Porter, 2000). Industrial clusters or geographical concentration of firms and supplementary units engaged in the same sector can generate various advantages for small firms. Schmitz (1995) captures these clustering advantages in the concept of collective efficiency, distinguishing between passively acquired benefits that arise from specialised agglomerations (skills, inputs and knowledge) and actively generated gains that accrue from the joint action of clustered actors. The gains of clustering include localised external economies, particularly economies of scale and scope as small firms specialise and engage in a division of labour. Geographical proximity also creates possibilities for local cooperation, between firms and through local institutions.

Many perceive there to be four methods by which a Cluster can be identified:

1) The Geographical Cluster
2) Sectoral Clusters (a cluster of businesses operating together from within the same commercial sector)
3) Horizontal Cluster (interconnections between businesses at a sharing of resources level e.g. knowledge management)
4) Vertical Cluster (i.e. a supply chain cluster)

The cluster model emphasises ***internal and external linkages***. In the case of internal linkages, the cluster gains are furthered by local business cooperation, local institutions and local social capital. The growing evidence on small firm clusters in developing countries competing in local and global markets has driven much of the policy enthusiasm on promoting clusters. External linkages matter, since global buyers can help local clusters access distant markets, acquire new forms of knowledge and upgrade. The nature of governance in the relationship that local clustered firms have with buyers in global value chains is critical to this, determining the autonomy and power of local actors.

External economies:

A key element of the benefits of clustering is external gains, since this attracts traders and lowers costs. In some cases, clustering results in reduced transaction costs of purchasing inputs and marketing outputs, eases information flows and facilitates order-sharing. However, it can be observed that certain sectors, such as textiles, garments, roof tiles and wood products, have stronger tendencies to cluster and more significant agglomeration gains for clustered producers. These differences are largely determined by technological factors, for example where it concerns the possibility to sub divide the production process, allowing specialisation and subcontracting, as well as by markets.

In more mature clusters, the presence of specialist labour and inputs lower search costs for producers. Subcontracting can be extensive and generate critical scale economies, while the rapid flow of information reduces transaction costs, minimises uncertainties and supports technological development.

Joint action
Agglomeration economies are only one aspect of the benefits that potentially emerge from clustering. Clusters create a potential for local joint action between individual enterprises and at a cluster-wide level through local institutions. Local collaboration is not an obvious outcome of clustering. It requires active intent on the part of the local actors. The evidence that emerges from cluster studies suggests that joint action is less common in incipient clusters than in more mature clusters (Nadvi and Barrientos, 2004). Joint action is important for poverty alleviation programmes, since it can be focused on local institutions and limits the vulnerability of clustered firms and workers regarding external threats. However, there are limited cases in which such joint action has taken place.

Social capital
Social capital is often cited as a key feature of small firm clusters. It can assist local trust ties but can also contribute to the provision of local social protection, providing an informal basis to cover risk and insurance as well as support for weaker members of the local community. However, evidence of such social capital in practice leads to different results, depending on the region. For example in the African region, the symbols of social networking are less clearly seen than in many of the newly developing clusters in Latin America. Although potential community ties (the use of family labour and migration into clusters) exist, there are few signs that social networks emerge which foster ties between small enterprises (Nadvi and Barrientos, 2004).

United for sustainable economic development in Arequipa, Peru.

In the South of Peru, Arequipa city and its surrounding area are famous for their Alpaca garment industry, tourist destinations and good food. The supply chains of these sectors could be improved in order to generate more employment and income for smallholder farmers, and small and medium-sized enterprises.

With the support of ICCO, a a strategic partnership for local economic development was created among the local government, universities and the Chamber of Commerce. The initiative is called CID-AQP (Competitividad, Inovacion y Desarrollo Arequipa). This partnership stimulates cluster development within the alpaca sector, tourist sector and software sector, aimed at improving job opportunities and income of smallholders and SMEs.

Since 2002, CID AQP has defined strategic development plans for each cluster, identified the main opportunities and constraints and defined action plans to work on these for a 5 to 10 year period. As an example, the alpaca garment sector requires coordinated action between universities, the bigger companies in the region and local farmers to create training centres in the field. In these centres, farmers will be trained in the good practices of alpaca breeding to diminish the mixing of species which reduces the quality of the wool. At the same time, bigger companies must increase their payments to the farmers to enable them to comply with higher quality requirements. From the lower quality wool, SMEs can produce carpets and garments for lower market segments.

The key for the success of these clusters is the added value cooperation offers for all the actors above the advantages of working independently. ICCO supports a local team of technical advisors who facilitate the process of planning and implementation of the strategic plans and act as brokers between the participants in the cluster.

For more information: Programme officer Peru

V.4.3 What are points of attention when looking at cluster development?

- ✓ General observations from studies of newly developing clusters suggest that beyond a division of labour within the cluster and some backward and forward vertical linkages, horizontal collaboration between enterprises and at the cluster level is rare (Nadvi and Barrientos, 2004). Low barriers to entry, limited skill bases, extensive local competition, low trust within clusters despite the often strong presence of common social identities, can result in poor contract enforcement.
- ✓ The evidence of joint action in mature clusters is much stronger. Liberalisation, new competition, demands from global buyers to meet global standards (on environment, labour and quality issues for example) and new technologies can force cooperation as clusters seek collective paths to enhancing collective capabilities.
- ✓ Often where cooperation occurs, it is strengthened by local social capital, common ties of community and identity that can foster cooperation and generate trust.
- ✓ Fostering trust, even with strong community ties can be difficult especially when enterprises are in direct competition with each other, where barriers to entry are low and where conditions of poverty are high.
- ✓ Cluster development programmes tend to concentrate on the growth and competitiveness of firms. As a poverty reduction strategy, it requires stronger attention to people within clusters, namely entrepreneurs and workers, their households and the wider community.

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V.5. Corporate social responsibility

Why is corporate social responsibility a useful intervention strategy for ICCO employee?

It is becoming increasingly accepted that partnerships between NGOs and companies can be a powerful tool for stimulating sustainable development. Momentum is being created to explore structural cooperation between different kinds of stakeholders. The call for improved corporate social responsibility (CSR) is inducing businesses to seek a balance between their profit generating activities and their potentially broader role in society, while the increased significance of market forces is driving civil society organisations like ICCO to reconsider their attitudes towards the market.

Since NGOs can be seen as the representatives of civil society (Tulder and Zwart 2005), this also suggests that NGOs have significant power and therewith a responsibility within the development of CSR. Some experience this as a development towards global democracy; others experience the international NGOs as the formation of a new counter elite with more or less the same needs and interests as multinational enterprises (Tulder and Zwart 2005).

Over the years, business and development communities have traditionally spoken different languages and used different strategies when working in developing countries. It is necessary (and increasingly happening) to bring these two together. CSR is now seen as a development intervention alongside aid, investment, capacity development and other more traditional strategies for donor countries to support the development process. What is now taking place is a greater involvement of those with more direct experience of aid interventions working with and forming partnerships with business'. These partnerships offer the opportunity of creating mutual learning and innovation.

V.5.1. Why is CSR important?

While many businesses have always behaved in a responsible manner, the debate about CSR has been said to have started in the early 20th century, amid growing concerns about large corporations and their power. Corporate Social Responsibility (CSR) is a concept which encourages private sector actors to consider the interests of society by taking responsibility for the impact of the organisation's activities on customers, employees, shareholders, communities and the environment in all aspects of its operations. This obligation is seen to extend beyond the statutory obligation to comply with legislation and sees organisations voluntarily taking further steps to improve the quality of life for employees and their families as well as for the local community and society at large.

Like other things, business and the way entrepreneurs operate are affected by public opinion and globalisation. The 'Global civil society' are expressing themselves clearly in what they do and do not accept and is sometimes even referred to as the 'second superpower' (Tulder and Zwart 2005). This suggests that (global) civil society is considered to have great influence and power. Now, partnerships are receiving new attention on the interface of business and civil society (profit and non-profit), precipitated by the growing complexity of increasingly internationally defined issues, changing stakeholder dynamics and recognition of convergent interests (see also V.3.).

CSR is clearly affecting small holder producers and small and medium sized enterprises (SMEs) in developing countries through direct supply chain relationships as well as the development of legislation and international standardisation and certification. CSR represents not just a change to the commercial environment in which individual SMEs operate but also needs to be considered in terms of its *net effect* on society.

Without the incorporation of smallholder producers and SMEs into the global 'social' value chain, the aim of CSR to contribute to International Development Targets will not be met. They play an important role in the economic development of developing countries. SMEs make up over 90 per cent of businesses worldwide and account for between 50 and 60 per cent of employment. Thus the interaction between CSR and smallholder producers and SMEs in developing countries is an important issue, not only for the smallholder producer, SMEs and those supporting their development, but also for all the actors driving CSR forward: TNCs, civil society organisations (CSOs), governments and multilateral bodies like the EU and UN, which have incorporated CSR within their strategies.

Natural sugar plant stevia creates new market opportunities

Stevia is a plant native to America which replaces, with great benefits, sugar cane as far as its sweetening properties is concerned (it is 200 – 450 times sweeter than sugar). In addition, it is a healthy product, recommended for people who suffer from diabetes or who do not want a fattening product in their diet. It is highly praised in international markets but it is not well known among the small farmers of tropical countries. The cultivation of stevia is highly profitable compared to other tropical products. A hectare of stevia might produce up to 3,000 kg of dried leaves which, at an average price of US$ 4 per kg would mean as much as US$ 12,000. At current market prices, stevia is one of the most profitable crops for the tropics.

The Bolivian NGO Semilla has started to stimulate the cultivation of Stevia with smallholder farmers in the subtropical region of La Paz. Stevia cultivation could become a complementary crop to food security crops, creating sufficient permanent income for farmers growing if it is cultivated in plots ranging from 500 to 2,000 square meters. Besides selling stevia to the conventional local markets, Semilla signed a letter of interest with the Bolivian pharmaceutical company La Far. La Far is interested in developing health products for the export market produced out of local traditional ingredients. La Far was interested in getting involved in this initiatives for two reasons. First, it would help to obtain the required ingredients for their new medicine. Secondly, they would contribute to the improved income of smallholder farmers. For the project to become a success, La Far offered to investigate in technology for more refined processing of the stevia, develop the packaging material, and take care of the marketing activities in the export markets.

With the support of ICCO, Semilla managed to promote the production of stevia among farmers of the tropical zones and help in its commercialisation, among others through an alliance with commercial industry La Far. However, SEMILLA also faced some challenges. First, they encountered a bottle neck in the production, since seeds had to be imported from Paraguay. Then a dramatic change of climatic conditions in the selected area (an extreme drought) caused the loss of more than 60% of the plantations and delayed the growth of the remaining plants in the first year. For this, the development of the alliance with La Far was slower than expected. Besides that, some other development agencies initiated stevia projects in the region, for which the prices in the local market dropped.

For more information: Programme officer Bolivia

V.5.2 What is Corporate Social Responsibility?

Corporate Social Responsibility (CSR) has been defined in many different ways. In general, it refers to companies integrating "social and environmental concerns in their business operations and in their interaction with stakeholders on a voluntary basis (…) not only fulfilling legal expectations, but also going beyond compliance" (EC 2001, Luetkenhorst 2004).

Over the last 20 years, there have been many different developments and many different responses by entrepreneurs to CSR (Raynard and Forstate 2002). To somehow frame the great variety of approaches and models suggested in literature, the four approaches or business models to CSR of Tulder and Zwart (2005) is helpful. The approaches they distinguish are: corporate self responsibility, corporate social responsiveness, corporate social responsibility and corporate societal responsibility (See Table 5). None of them are mutually exclusive or present a best practice model. Table 5 presents the approaches in a compact way. A short description follows. For further details please refer to Tulder and Zwart 2006, Chapter 8.

Table 5: Four CSR approaches

IN-ACTIVE	**RE-ACTIVE**	**ACTIVE**	**PRO/INTER-ACTIVE**
"Corporate *Self* Responsibility"	"Corporate Social *Responsiveness"*	"Corporate Social *Responsibility*"	"Corporate *Societal* Responsibility"
Inside-in	Outside-in	Inside-out	In/outside-in/out
'Doing things right'	*'Don't do things wrong'*	*'Doing the right things'*	*'Doing the right things right'*
"Doing well"	*"Doing well and doing good"*	*"Doing good"*	*"Doing well by doing good"*
'Just do it'	*'Just don't do it'*	*'Do it just'*	*'Just do it just'*
Efficiency	**Equity/Ethics**		**Effectiveness**
Utilitarian motive: Profit maximisation	Negative duty approach: Quarterly profits and market capitalisation	'Positive duty' or 'virtue based': Values (long-term profitability)	Interactive duty approach: medium-term profitability and sustainability
Indifference	Compliance	Integrity	Discourse ethics
Business and Society Management		Business in Society Management	Business-Society Management
'Trust me'		'Proof it to me'	'Involve/ Engage me'; 'Join me'
Economic Responsibility [Wealth oriented]	←	→	Social Responsibility [welfare oriented]
Narrow (internal) CSR			Broad (external) CSR

Source: Van Tulder with Van der Zwart (2006)

The suggested approaches can be characterised by distinctive procedural attributes:

a. in-active,
b. re-active,
c. active and
d. proactive.

Research has shown that the different approaches emerge in society at different stages over time.

► ***The inactive approach*** "reflects the classical notion of Friedman that the only responsibility companies (can) have is to generate profits. This is a fundamentally inward-looking (inside-in) business perspective, aimed at efficiency and competitiveness in the immediate market environment. Entrepreneurs are particularly concerned with 'doing things right'; no fundamental or ethical questions are raised about what they are doing. The focus is largely on products and/or services provided:

fast production, clever marketing, innovation in time and patenting or not. Good business from this perspective equals operational excellence. CSR thus amounts to 'Corporate Self Responsibility'. The slogan of sportswear manufacturer Nike, 'Just Do It!' is in line with this type of reasoning. The motivation for CSR is primarily utilitarian (Swanson, 1995), derived from so-called 'consequential ethics' where the focus is on the end result rather than the means by which it is achieved. In this goal-oriented approach, CSR is aimed at profit and sales maximisation, return on investment and sales."

- ***The re-active approach*** is "[a] slight variation on the inactive attitude [and] shares the focus on efficiency but with particular attention to not making any mistakes. This requires an outside-in orientation where entrepreneurs monitor their environment and manage their primary stakeholders so as to keep mounting issues in check without otherwise allowing it to give rise to fundamental changes in the business philosophy and primary production processes. Entrepreneurs are socially responsive and respond specifically to actions of external actors that could damage their reputation. Corporate philanthropy is the modern expression of the charity principle and a practical manifestation of social responsiveness (Post et al, 2002: 89). During their protests campaigns against Nike for using suppliers in South East Asia whose factories allegedly resembled 'sweatshops', NGOs and activists rephrased the Nike slogan as: 'Just Don't Do It!' to get their message across (The Economist, 14 December 2002). In this approach the motivation for CSR is primarily grounded in 'negative duties' where firms are compelled to conform to stakeholder-defined norms of appropriate behaviour (Maignan, Ralston, 2002). The concept of 'conditional morality' (Cf. Basu, 2001), in the sense that managers only 're-act' when competitors do the same, is also consistent with this approach.

Both inactive and reactive approaches focus largely on output indicators such as (short term) returns and productivity and are strongly means and wealth oriented. Relationships with societal and community stakeholders are relatively involuntary and room for managerial discretion is limited. Most entrepreneurs have a (neo-classical) perspective on CSR and will probably conflict with organisations on a regular basis. Moreover, such efficiency thinking harbours the risk that an entrepreneur may indeed be doing something really well but that they are following the wrong course or pursuing the wrong objective".

- ***An active approach*** "to CSR represents the most "ethical" entrepreneurial orientation. Entrepreneurs who pursue this approach are explicitly inspired by ethical values and virtues (or 'positive duties') on the basis of which company objectives are formulated. These objectives are subsequently realised in a socially responsible manner regardless of actual or potential social pressures by stakeholders. Such entrepreneurs are strongly outward-oriented (inside-out) and they display a certain 'missionary urge' which makes them heroes to NGOs but an annoyance to 'true' entrepreneurs. (...) Entrepreneurs who adopt an active CSR approach share a strong orientation towards justice that is motivated by a healthy and clean environment, social equity, social progress and so forth. They are set on doing 'the right thing'. While these entrepreneurs may have terrific relationships with NGOs, they do run the risk of neglecting business efficiency and jeopardising the continuity of the company. In a society that is structured around the principles of business production methods, this can also be regarded as socially irresponsible."

Chain development: Organic Exchange

Organic Exchange is an international organisation that promotes the production and use of biological cotton worldwide. Organic Exchange brings all the players and chains together, from the cultivators and spinners to the clothing manufacturers and retailers. Members such as C&A, H&M, Levis and Nike produce a part of their collection from biological cotton, in this way helping cotton farmers to move to more environmentally friendly methods of agriculture and at a better price. ICCO supports Organic Exchange financially, and ensures the connection between the cotton farmers and the network of companies belonging to Organic Exchange.

For more information: International Market Expert for Cotton and Expert Cooperation with Private Sector

According to Van Tulder (2006: 145), "[a]ll three perspectives on CSR have their managerial shortcomings: purely ethical business practice can result in managers doing the 'right things' wrong, while competitive market oriented business practice can lead managers to doing the 'wrong things' right. Societal issues are almost always complex and involve a range of interests (Schumacher, 1979), with the result that a variety of 'right' answers are possible. A [more dialectical] perspective is consequently required where the field of tension between ethics and efficiency is engaged in a socially responsible manner. This requires a synthesis of (or a trade-off between) the two approaches and the term proactive CSR can be employed to describe this orientation."

► ***The pro/interactive approach***: "One can speak of a pro-active approach if an entrepreneur undertakes activities aimed at external stakeholders right at the beginning of an issue's life cycle (...).In a bargaining society, effective CSR is characterised not only by proactive business practices, but also by *interactive* business practices, where an 'inside-out' and an 'outside-in' orientation complement each other. In moral philosophy, this approach is also referred to as 'discourse ethics'. In discourse ethics, as developed by Habermas (1990), actors regularly meet in order to negotiate/discuss a number of norms to which everyone could agree. The motivation for managers to engage in CSR is based on what we might call 'interactive' duties and 'situational 'and 'relativistic' ethics apply. The field of tension between ethics and efficiency is only resolved when entrepreneurs are willing to focus on the 'profitability of values' (SER, 2000a) and think of efficiency as 'doing the right things right' (effectiveness). This implies medium-term profitability and longer-term sustainability, not only for themselves but for the whole sector and sometimes even for the whole economy (adding a welfare orientation to a company's aims). Both active and pro-active approaches to CSR share a considerable degree of voluntary action and managerial discretion."

Corporate Social Responsibility in Latin America: Ethos

Ethos is the national organisation for Corporate Social Responsibility in Brazil. Large Dutch companies established in Brazil, such as ABN AMRO and Philips, are members of Ethos. Together with trade unions, universities and development organisations, Ethos stimulates companies to conduct their business and production process in such a way that they contribute to alleviating poverty. For example, by buying products from small co-operatives, creating new jobs, or involving local people in working for the support services. ICCO supports the activities of Ethos, and thinks along with them which strategies can put the desired approach into practice.

For more information: Programme officer Brazil and Expert Cooperation with Private Sector

Van Tulder (2006) observes three ways in which organisations can evolve from inactive and reactive to a more proactive approach to dealing with societal concerns, represented by the arrows A, B, and C in figure 19.

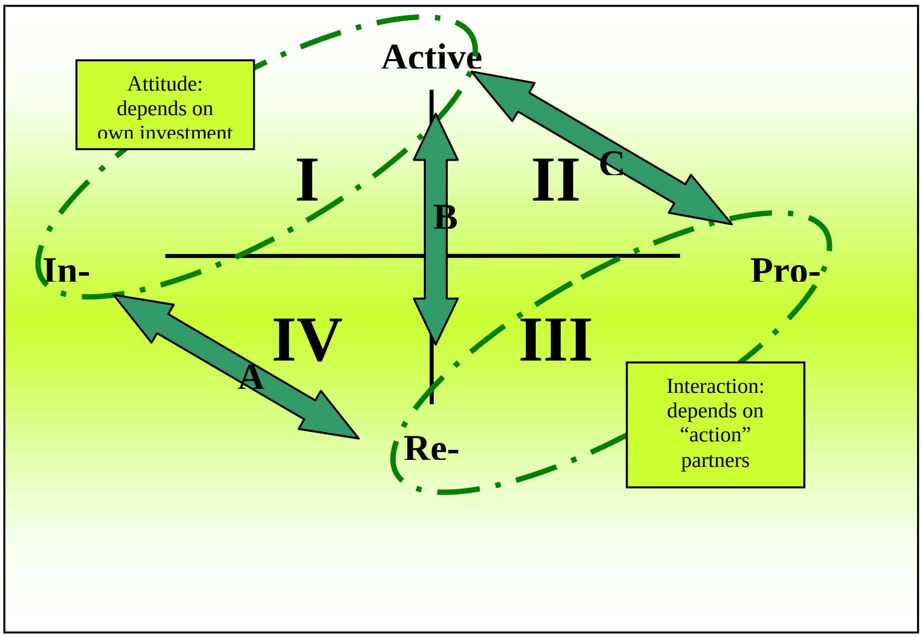

Figure 19: Dynamics in CSR approaches
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The issue here is how to *credibly* evolve from one approach to responding to societal concerns to another. Claims regarding social responsibility and statements regarding the intention to interact with stakeholders are not neutral; organisations will be held accountable for delivering on their promises and their actual contribution to solve societal issues for which they are (partly) responsible. Not delivering on promises will only increase societal distrust, will lead to a widening of expectational gaps and may ultimately result in a damaged reputation.

Moving directly from a reactive to a proactive mode of communicating with stakeholders may be an implicit desire of organisations that have been confronted with the influence and power of pressure groups. In practice, however, this move appears almost impossible. Interacting with stakeholders is meaningless and could even be harmful when the organisation has little to offer in terms of corporate citizenship or (societal) problem solving capabilities. In such cases, the perception of 'window dressing' may well turn against the organisation.

Before making the move towards interacting with external parties, an organisation will need to build some form of creditworthiness, based on sincere intentions. This requires the organisation to focus first and foremost on what is needed *within* the organisation and on *internal commitment* in terms of an explicit intention to organise the business more responsibly and sustainably. This implies a development from *inactive* to *active* (see area I in figure 2.5), requiring that the organisation (i) develops a vision on the principles and values it wants to stand for with regard to its position in society; (ii) intends to imbed these principles and values in the organisational structure, culture and management layers; (iii) integrates these business principles and corporate values in the strategy of the organisation and in the business objectives; (iv) incorporates the principles and values in all relevant business activities and processes; and (v) is willing to be held accountable about how principles and values are integrated within all activities.

In general, organisations that can be classified as 'inactive' are unlikely to spontaneously move towards a more active approach. In these cases, an external *trigger* will usually instigate such a move. Often, organisations need a 'wake-up call' before a *sense of urgency* is experienced.[21] Consequently, the development trajectory from inactive towards active usually tends to be travelled via the arrows A and B (figure 19): an inactive approach toward societal concerns can only result in reactive – and therefore defensive – communication with external stakeholders. Because the reactive approach is also the approach that often leads to unwanted public attention and reputational damage, organisations may feel the need to move towards a more active approach. It goes without saying that this development process does not happen overnight.

The more an organisation is evolving towards a more active approach to societal concerns (arrow B in figure 19), the more it becomes prepared to constructively interact with stakeholders. Depending on how effective such interaction processes proceed and depending on the attitude and approach of external parties, the organisation may also develop more sensitivity and understanding about those changes needed to prepare the organisation for the challenges and developments of tomorrow.

To demonstrate good business citizenship, firms can report compliance with a number of CSR standards (for more information on standards, see V.6), including:

- AccountAbility's AA1000 standard, based on John Elkington's triple bottom line reporting
- Global Reporting Initiative's Sustainability Reporting Guidelines
- Verite's Monitoring Guidelines
- Social Accountability International's SA8000 standard
- The ISO 14000 environmental management standard

Some nations require CSR reporting, although agreement on meaningful measurements of social and environmental performance is difficult. Many companies now produce externally audited annual reports that cover Sustainable Development and CSR issues, but the reports vary widely in format, style and evaluation methodology (even within the same industry). Critics dismiss these reports as lip service.

Drinking water for the poor: Vitens

The water company Vitens has been working on the rehabilitation of existing drinking-water systems. Vitens is also working on providing alternatives for water pipes in the slums and the smaller cities in Ghana. It is relatively expensive to provide, and increases the problem of waste water. Vitens is working with ICCO and other partners of the Dutch Water Partnership to develop affordable alternatives in these areas, such as collective/communal tap points or tank trucks. Together with Ghanian partners, government institutions and companies, they are seeking out which models of management are most appropriate to provide this target group with sufficient water of a high standard.

For more information: Programme officer Ghana and Expert Cooperation with Private Sector

V.5.3 What are the points of attention when looking at CSR?

- ✓ Some critics believe that CSR introduces social and environmental clauses resulting in protectionism by the back door. CSR could also impose inappropriate cultural standards or unreasonably bureaucratic monitoring demands on small

[21] A well-known illustration is what the Brent Spar and Nigeria affairs have meant for Shell.

businesses. The net effect on the communities concerned will be a reduction in welfare. On the other hand, CSR offers opportunities for greater market access, cost savings, productivity and innovation to SMEs, as well as broader social benefits such as education and community development.

- ✓ Pressure for greater CSR whether focusing on environmental, consumer or human rights issues often shares the common underlying concern that corporate influence is too great. Many critics accuse the corporate sector of unaccountable power and influence, cultural imperialism, bleeding local economies dry and using the mobility of capital to force an international 'race to the bottom'. Data identifying half of the world's largest economies as corporations support the belief that TNCs cannot be regulated by national governments. The range of negotiated voluntary guidelines, partnerships and the emerging 'civil regulation' frameworks are a pragmatic response to this. However the paradox is that it is easier for larger companies to respond and make commercial gain from their actions than it is for smaller companies, thereby tipping the scales further in favour of TNCs. This works on a number of levels:
  - It is easier for large companies with their developed systems and economies of scale to deal with the demands for formal monitoring and standards. SMEs do not have the financial and human resources to invest heavily in CSR activities unless they bring immediate tangible benefits.
  - Large companies can afford to spend time and effort developing relationships and partnerships with NGOs, governments and UN agencies.
  - Global brands can outsource production and pass the costs of necessary improvements down the supply chain to their suppliers while gaining the reputational benefits for these improvements.
  - Global brands and market leaders are then in the best position to make commercial gain from their CSR stance. Southern SMEs generally have a less direct relationship with Northern consumers and are therefore unable to reap the reputational benefits.
  - Large companies have more complex networks of relationships, which CSR can help strengthen, manage and understand. In SMEs these relationships are more often invested in the personal interaction of the entrepreneur.
  - CSR is the 'human face of globalisation' and as such eases the entry of global companies into the home markets, high streets and sectors where SMEs have dominated.

- ✓ Clearly SMEs will have to join the CSR fold, if the small business sector is not to become the loophole in which polluting, exploitative industries flourish. However, many of the concerns underlying calls for more CSR by TNCs do not apply to SMEs, which lack the power to influence governments, dictate standards or move between countries in search of lighter regulation. On the other hand, SMEs generally have a greater understanding of local cultural and political contexts, more links with local civil society and a greater commitment to operating in a specific area.

- ✓ It is critical that SMEs in the South are able to go beyond a compliance-based reactive mode to CSR to engage in the ongoing development of what effective, appropriate CSR means at all levels. CSR approaches are increasingly being seen alongside other development interventions, in which donor countries can assist in the development process.

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