Shaping Value Chains for Development – Experience in Development Assistance

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Abstract

This article reviews the use of the value chain concept in development practice, both as an analytical tool and a guideline for development assistance. The value chain approach delimits a specific area of action and provides a powerful conceptual framework. However, given the range of issue involved in chain upgrading, intervention strategies rely on various fields of development expertise. What they have in common is the systemic perspective on sectoral economic structures and a concern for the tasks of organizing collective action and facilitating linkages.

Introduction

“Pro-poor growth” has become the leitmotif running through much of the recent development debate. In agriculture, pro-poor growth is increasingly associated with the diversification and development of those markets for high-value food and natural products that generate employment and allow a broad-based participation of farmers and small enterprises. Promoting these markets development policy increasingly refers to the value chain concept (KOHLMEYER, 2005, in this volume). In the following, value chains are defined as

- the sequence of productive processes from the provision of specific inputs for a particular product to primary production, transformation, marketing and up to final consumption
- the organisational arrangements linking and coordinating the producers, processors, merchants, and distributors who perform these functions.

This definition is more generic than the narrower “supply chain” concept employed by private companies to optimize their sourcing and marketing functions. Here, the “value chain” defines a whole market or subsector as a unit of analysis and as field for development cooperation. (cf. Stamm, 2003).

This article explores the application of the concept in development practice. Contrary to the academic study of value chains, development agencies use the value chain concept for pragmatic purposes, i.e. to analyze development constraints, and to identify areas of public investment and action. The text boxes present examples of GTZ experience promoting value chains.

The Value Chain Concept as Analytical Tool

Within the international development community there is widespread agreement that poverty alleviation will not be achieved without effectively functioning markets. The value chain concept
is an instrument to analyze market relationships and issues of common concern for farmers and enterprises operating in a specific market.

Two typical problem situations may be distinguished: First, in many countries, especially in Africa, domestic food markets are often poorly organized. Problems may be found all along the chain: At the upper end smallholder producers have difficulties accessing services, inputs and market information. Further downstream, trade is often underfunded and risky, and therefore largely personalized. Weak infrastructure, high taxes and corruptive practices keep transaction costs high. At the final sales point, product and quality differentiation is weak – and consumer prices high. Overall, domestic food chains are frequently characterized by low efficiency and a highly asymmetric distribution of information and market power between buyers and sellers (DFID, 2005). As a consequence, market incentives are stifled preventing smallholder intensification and quality improvement. Hardly any growth of value added can be expected. The value chain concept can be used to systematize such constraints and identify points of intervention.

Box 1

Analyzing the potato chain in Kenya

The potato subsector is potentially of great importance for pro-poor growth in Kenya, because it employs around 500,000 farmers – and potatoes are the second most important staple food in Kenya. Initiating its activities in support of potato production for domestic consumption, the PSDA programme conducted a value chain study. The analysis reveals serious disincentives to the product and process upgrading. The main bottlenecks are in the trade system: Traders use variable bag sizes ranging from 100 to 220 kg/bag that inducing considerable uncertainty over prices, a problem aggravated by the absence of grades and quality standards. While local and market authorities charge high cesses and are prone to corruption, trader cartels take advantage of the market coordination failure. As farmers are forced to sell at low prices, there are little possibilities to invest in better inputs and improved on-farm storage.

Source: PSDA programme (GTZ Kenya, Nairobi)

An opposite scenario can be found in high-value export production sensitive to logistics, e.g. horticulture. In highly competitive global horticultural markets the coordination of production and marketing processes gets ever more important. Global value chains function as systems with their own rules, often controlled by the main buyers. Contrary to traditional food markets, the partners in global value chains collaborate intensively. From a pro-poor growth perspective the challenge is to link smallholders to these markets and to keep most of the value added in the country of origin. The value chain concept helps to understand the competitive position of producers, the conditions of market entry, and the distribution of gains between small-scale suppliers and buyers. An example is the market for organic products (see GUENTHER and BULEY, 2005, in this volume).

Both description point to the issue of chain governance. In the first case, a failing market coordination needs to be corrected, in the latter interventions are required making a “quasi-hierarchical” form of governance (HUMPHREY and SCHMITZ, 2001) as pro-poor as possible.

Value Chain Promotion in Agricultural Development

As an approach to development assistance, the value chain concept not only constitutes a framework for analysis, it also delimits a field of interventions – according to a development potential. Consumer markets amenable to smallholder participation and offering the most promising growth potential are selected for promotion. Subsectors typically chosen for promotion by development agencies include e.g. horticultural products, coffee and cocoa, freshwater fish, dairy, honey, spices and different niche products.
The objective of value chain promotion is to facilitate the upgrading of products and processes increasing the value added. This is achieved by linking farmers, service providers, industry and buyers, investing in efficient market institutions, and correcting market failures that impede growth and discriminate against rural producers. In order to identify the appropriate interventions, three lead questions are useful:

- What are the reasons for a value chain to stagnate?
- Which gaps exist between the requirements on a value chain derived from market demand and its current structure and performance?
- Which constraints reduce the competitiveness of the target group and prevent their integration into a value chain?

Value chain promotion means addressing the constraints and working to improve the coordination of enterprises and public agencies along the value chain. The focus is on economic structure, the “systemic competitiveness” (ESSER et al., 1994) of the chain as a whole and not just the individual producers. Therefore, a promotion strategy needs to coordinate interventions. By adopting a holistic perspective on the subsector and combining interventions at different stages, the value chain approach goes beyond the traditional field of agricultural market development.

An important principle of value chain promotion is to foster a self-sustaining development process. Public and private services should be paid for with the income generated in the value chain. Any public support is limited to strengthening framework conditions and facilitating the own initiatives of farmers and enterprises.

**Intervention areas**

There is a great choice of potential actions supporting value chain upgrading. While the main issues are given by an initial value chain analysis, the intensity of the effort will depend on the size of the subsector and the initiatives of private enterprises.

A basic distinction can be made between actions at different levels of the economy. A promotion strategy may assist enterprises at the micro level, strengthen business associations and specialized agencies at meso level and/or cooperate with government institutions at the macro level. A micro-level strategy typically operates through public-private partnerships (PPP), supports service providers, facilitates vertical integration (contract farming, outgrower schemes, sales contracts), assists farmer organizations and helps producers comply with the rules imposed by lead firms.

**Promoting high-value aromatic cocoa in Ecuador**

Ecuador produces high quality cocoa that receives a premium price on the world market. However, this special competitive position is at risk. The project brought together the economic actors in the cocoa business, at the national level and within the two major production regions (Esmeraldas and Amazonía). They decided to coordinate quality management and get access to the markets for specialty cocoa (aromatic, organic and with certificates of origin). Major project interventions include the organization of round table meetings on technological and research issues, production and marketing, and the development of producer associations. The first national cocoa forum initiated a competitiveness strategy for the Ecuadorian cocoa sector. This strategy includes actions to improve production technology, form a national federation of cocoa producers, position Ecuadorian cocoa on the world market and promote exports. National quality norms and the a standard for organic cocoa have been established. In addition, the project invested in the development of a website and production of information material. The strategy benefits most of the 16,000 Ecuadorian smallholders engaged in cocoa production.

*Source: Proyecto GTZ-PAC (NAMARES programme, GTZ Ecuador, Quito)*
Actions at meso and macro levels address collective problems of all actors in the value chain. Important topics are the introduction of grades and standards and other interventions improving the regulatory framework (licensing, taxation, customs clearance etc.). Development programmes may also advocate policy change and infrastructure investment or assist with trade negotiations.

The range of options makes it clear that value chain promotion is not a unified development approach. Each strategy is a combination of measures at different stages of the value chain and at different levels of aggregation. Support strategies have to utilize and adapt know-how from various fields of development expertise. The connecting theme is the intermediation between farmers, input suppliers, traders, companies and rural banks.

**Box 3**

**Promoting spices in Sri Lanka**

Spices are a traditional export product of Sri Lanka providing income to a large number of smallholders. The project conducted a participatory study of the pepper and cloves value chains bringing together actors from the different stages. A “value chain core group” was formed to address the issues that have been identified, viz. quality improvement, training, improvement of export regulations, and export promotion through export incentives, branding and the establishment of joint ventures with European partners. Partners include the national spice council, important processing and export companies, representatives of growers, the Ministry of Agriculture and various NGOs. It is also envisaged to create national spice fora.

*Source: Capacity building for Competitiveness programme (Integration Consult/GTZ Sri Lanka)*

**Assessment of the Experience: Prospects for Impact**

In general, chain upgrading is the result of private investment and the contributions of several public agencies engaged in promotion. Individual projects can seldom claim the ongoing structural change as their impact. The key issue is to select those markets for promotion providing opportunities for pro-poor growth. The growth-poverty reduction linkages can refer to the market integration of smallholders or to the creation of new jobs at the processing and marketing stages. In order to be effective, interventions of chain promotion projects need to provide answers to current value chain constraints.

However, the tradeoff between growth and poverty alleviation remains, as more efficient markets drive out less competitive producers. So far, no conclusion can be drawn as to what extent the rural poor will eventually benefit: Value chain development is a necessary condition, but by itself not sufficient to respond to the problem of economic exclusion.

**References**


Guenther, D. und M. Buley (2005): this volume (please complement the title)

Kohlmeyer, Chr. (2005): this volume (please complement the title)