

Agro-based Enterprise Development – Clustering Approach

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Promoting Agro-Enterprise and Agro-Food Systems Development in Developing Countries

- **Agro-Enterprise activity – also referred to as Agribusiness is a powerful source of economic growth, diversification and rural poverty alleviation.**
- **Agro-Food Systems– as a by-product of globalization, food supply systems are driven by consumer preferences. Becoming more "Demand-Pull" than traditional "Supply Push".**
- **Transition from subsistence farming to cash-cropping (and commercial livestock production) and demand-pull marketing systems require the coordination activity of input providers, producers and downstream agents.**



The Building Blocks of the Off-Farm Part of the Agro-Food System

- 1. Agro-Enterprises – provide value adding goods and services within the agro-food system;**
- 2. Markets and vertically structured Supply Chains;**
- 3. Rules and Regulations – Institutional Economics;**
- 4. Collective and other meso organizations such as farmer organizations, trusts/foundations, commodity, locational or professional associations.**



The Building Blocks and Competitiveness of Agro-Food System

- **The ways in which these building blocks are organized and their effectiveness with which they operate together as “Systems” effects their competitiveness.**
- **Competitiveness benchmarking analyses, normative trade facilitation assessments, and market assess surveys or case studies of institutional re-engineering are useful tools for assessment of the competitiveness of the building blocks of agro-food system.**



Agro-Food Systems, Economic Growth and Poverty Alleviation

- **Both on the demand and supply sides of agro-food systems, the poor are major stakeholders: -**
 - Demand side – the efficiency of post-harvest and agricultural marketing operations is a major determinant of the prices paid by the poor (important factor in household food security).
 - Supply side – several direct and indirect relationships between poverty alleviation and agribusiness.
 - Agro-enterprise activity employs the poor, either through self- or wage-employment.



Agro-Food Systems, Economic Growth and Poverty Reduction

- **One World Bank estimate, household income field surveys – 25% of total rural incomes come from non-farm, agribusiness activities.**
 - The poor are employed in farm machinery repairs, farm product processing, food product trade and other agribusiness functions;
 - Such spin-off employment rises as developing economies move from low income to middle income status;
 - For a cross-section sample of developing countries, agro-processing accounts for 20-35% of wage employment in the manufacturing sector.



Agro-Food Systems, Economic Growth and Poverty Reduction

- **Increased level of rural employment is expected to be involved in:**
 - Handling, packaging, processing and transporting food products compared with producing crops or raising animals on the farm.
- **Improving agro-enterprise efficiency can lower operating and transaction costs which benefit a broader group of farmers.**



Implications for Developing Economies

- **In sum, agro-enterprise and agro-food system developments and improvements in competitiveness provides catalytic force to poverty reduction especially in developing and transition economies.**
- **Agribusiness investment and activity remain an important determinant of overall economic growth in low and middle income countries.**
- **Empirical analysis of economic structure points to a general pattern:-**
 - **The value-added in agribusiness accounts for some 15-25% of GDP (formal sectors) of low income countries;**
 - **This share and size of agribusiness in national GDP increases to 30-40% for middle income countries.**



Implications for Developing Economies

- **The modernization of agribusiness systems stimulates broader economic development.**
 - Rising demand, esp. fruits and vegetables, live stock products and other goods with relatively high income elasticity stimulates product and process innovations;
 - Induces backward and forward linkages within the agro-food system.
- **Recent experiences teaches that:-**
 - Effective reorganization of the institutional building blocks is necessary to make an effective transition to a competitive system integrated with global food markets;
 - Supply chains and agro-enterprise clusters development requires determined and focused tactical efforts at the national level.



Concluding Observations

- **Globalization, changing consumer demands, application of powerful ICT are the driving forces in the worldwide agro-food industries.**
- **Supply chains are institutional arrangements linking producers, processors, markets and distributors, retailers and consumers.**
- **Country experiences show that new markets, products and services can best be developed through partnerships integrating suppliers, input providers, markets and consumers within the agro-food systems chain.**



Development of Clusters and Networks of SMES

- **SMEs, including agro-based enterprises, play a key role in economic growth and equitable development in developing countries**
- **SMEs become more competitive by fostering inter-enterprise linkages as well as collaborative relations with local support institutions – Individual SMEs experience difficulties in achieving economies of scale.**
- **Within groups or ‘clusters’, enterprises’ joint initiatives are stronger with critical mass, more cost effectiveness and proximity fostering mutual knowledge, innovation and cooperative competition.**



SMEs Clusters

- **SME Clusters – important and dynamic players within the international market**
 - Responding to global competition challenges by capitalizing on local opportunities and collective competitive advantage.
- **Well documented successful cases of many SME clusters have been operated in Italy in sectors as diverse as textiles, leather, jewelry, optical frames, among others.**
- **Another representative case of SME clusters in India – Tirupan in the State of Termil Nadu hosts an agglomeration of more than 7000 SMEs exported US\$ 650 million of cotton hoisery to world export markets**



Some Principles of Development of Effective Clusters

- **Participatory approach to vision building.**
 - The initial task is to building trust among cluster stakeholders – enterprises and local institutions.
- **Capacity-building based on shared targets – including the networking of existing institutions and bridging the gap between supply and demand.**
- **Sustainability of the cluster development process – tapping technical assistance programmes related to the process.**



Further Principles for Promoting SME Clusters and Networking

- **It is argued that clusters of SMEs have the advantage of flexibility and responsiveness – They can be more competitive than larger firms**
- **Policies for SME clustering can be particularly effective when:**
 - They are driven to meet the demands of the customers (i.e., demand-driven);
 - It is directed at groups of enterprises – collective approach entails lower transaction costs and improve efficiency;
 - There is established condition leading to the cumulative capacity to upgrade and become less dependent on support from outside.



Drawing SME Clustering Lessons from Europe

- **The international interest in clustering was fueled by the experience of 'Third Italy' in 1970s and 1980s.**
- **Its rapid growth was associated with the rapid growth of SME-based industries, with the concentration of firms in particular sectors and localities.**
- **Groups of firms clustered together in specific regions seemed to be able to grow rapidly, develop niche export markets and offer new employment opportunities.**



Drawing Lessons from Europe

- **The Italian experience used the concept of industrial districts to capture the success of agglomeration of small firms.**
- **Such clusters enabled SMEs to establish a strong position in world markets in traditional products – shoes, leather handbags, knitwear, furniture, tiles, and food processing, to name a few, and also industries which supply machinery to these sectors.**
- **The main attributes of effective clustering/industrial districts – geographical proximity, sectoral specialization, predominance of SMEs/firms, close inter-firm collaboration and competition based on innovation, socio-cultural identity, and supportive regional and municipal government.**



Clustering, Networking and Competitive Advantage

- **There are gains in clustering is old hat in industrial economics – Such gains are known as ‘external economies’ relevant to small firms:**
 - Competitive advantage derived from collective efficiency and joint action;
 - Static gains such as easy availability; Dynamic gains such as the rapid spread of new ideas of how to innovate;
 - Rivalry among clustering producers may be severe but they join forces to overcome common bottlenecks in infrastructure, input supply or access to distant markets.
 - Combination of competition and cooperation drives the search for improvement among clustered SMEs.



Clustering Lessons from Developing Countries

- **Public policies are instrumental in promoting clustering and networking of SMEs in developed and developing economies.**
- **Some clusters in Asia have acquired great depth in concentration of specialized suppliers and support bodies.**
 - For example, the metalworking and textile industries of Ludhiana in the Indian Punjab, the engineering and electronics cluster of Bangalore, the Korean textile clusters in Daegu, and electrical fans in Gujarat in Pakistan.
- **Clustering can also be a feature of rural industrialization as in Indonesia – Specialization of entire villages, for example, in manufacturing of roof tiles or rattan furniture in Java.**

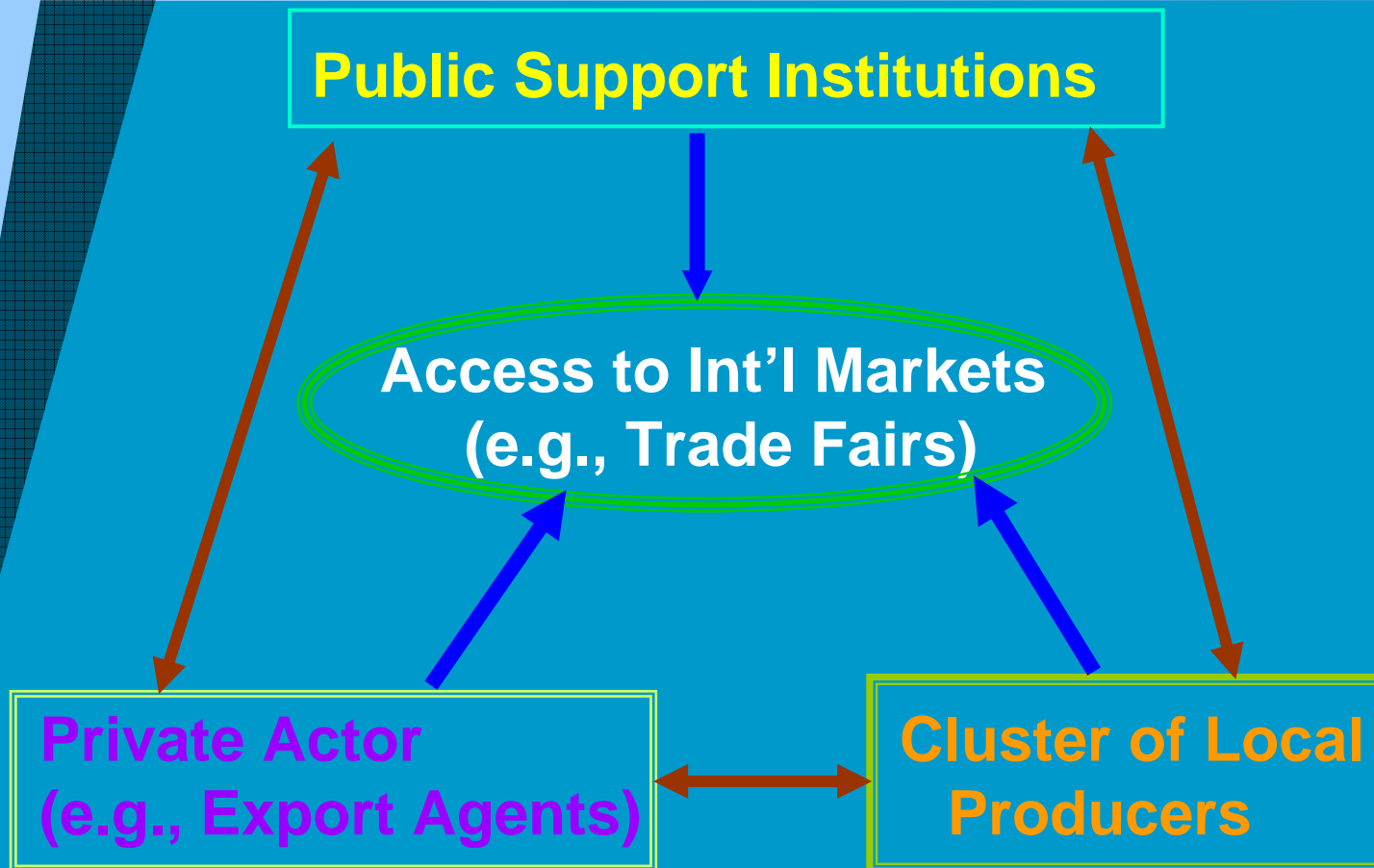


Towards a Demand Focused Approach

- **Clustering is of significance to the industrial organization of small-scale manufacturing in developing countries.**
- **Some clusters are more dynamic than others – One key seems to be forward linkages and customer orientation/demand driven.**
 - **Examples: Cotton knitwear cluster of Tiruppur in India; Surgical instrument cluster of Sialkot in Pakistan - being major actors in their respective national and international markets.**
- **Successful international market entrant- Production is organized by buyer-driven commodity/production systems chain.**



Transforming Agents in the Cluster Development



Conclusions and Clustering Policy Implications for Developing Countries

- **A large body of research literature on policies for SMEs clustering and small-scale industry in developing economies finds that:**
 - ✓ Research on clustering in developing countries has been inspired by the competitiveness of industrial districts in advanced economies – The European success stories of the 1970 and 1980s exemplify the power of collective efficiency focused on demand driven approach;
 - ✓ Assisting groups of enterprises is more cost effective than individual enterprises – The collective approach has lower transaction costs and facilitates mutual learning.
 - ✓ Public support for SMEs in developing countries tends to be overly supply oriented (e.g., training, credit, raw materials, technology) and not sufficiently focused on demand (successful customer-oriented programmes).



Conclusions and Clustering Policy Implications for Developing Countries

- ✓ In sum, intervention is most effective when it is based on three 'C's: Customer-oriented, Collective and Cumulative – SME clustering support approach guided by customer orientation and targets the collective enterprises is more likely to achieve cumulative improvement in competitiveness.
- ✓ The promotion of SME clusters may also benefit the rural economy by creating new sources of economic growth – Agribusiness investments linked to processing and marketing activities are crucial for increasing the value of agricultural production.
- ✓ Some of the most interesting insights for policy are emerging from experiments in developing countries themselves – For policy lessons, South-South Channels seem to be as important as North-South channels for mutual learning and possible replication in practice.



THANK YOU

