

Value Chain design for MSMEs

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ABSTRACT : *The approach presented in this paper combines the strengths of value chain analysis with the promotion of sustainable, market-based solutions (MBSs) that respond to the recurrent needs of micro, small, and medium scale enterprise (MSMEs). Value chain analysis is important in understanding markets, inter-firm relationships, and critical constraints that limit MSME growth and industry competitiveness. Collaboration among private sector market actors to address value chain constraints can result in MBSs that are sustainable in the long run and that do not distort local markets. The approach presented in this paper can help ensure that solutions for MSMEs will continue once the program is over and that impact will be sustained. It also helps establish links between program facilitation activities and impact on MSMEs. From this approach efforts have been made to provide practical tools to link value chain analysis with the development of market based solutions (MBS) by addressing needs of MSMEs, identifying and promoting embedded solutions often found in relationships between actors in specific value chains and focusing on market based sustainable solutions in growth value chains that will result in increased MSME incomes.*

KEY WORDS: *Value chain, MBS, Sustainability, MSMEs, industry competitiveness.*

I. INTRODUCTION

The dominant paradigm for the analysis of firm-level competitive advantage in the strategy literature from quarter a century ago has been the value chain model developed by Michael Porter (1985). The basic idea is that competitive advantage cannot be understood or managed by looking at the firm as a whole. It is necessary to consider the myriad of activities that the firm does in the process of creating value for its customers. The value chain is here a simple activity template that can be used to identify, represent and analyze value activities. The paper is targeted at both donors and practitioners from enterprise development organizations, and is organized into three main sections. This first section explains the rationale of the approach, in the context of current thinking on private sector/enterprise development programs. The second section describes the approach and provides guidelines for implementation. The third section presents general principles for the design and implementation of value chain and market development programs

II. RATIONALE

There is general recognition in the development community that traditional approaches to enterprise development have been lacking in impact and sustainability. This has led the field to look for more sustainable solutions. The promotion of "market-based" or "commercially viable" solutions has emerged as an alternative - and focuses on developing sustainable solutions that: 1) contribute to both firm and industry level competitiveness; 2) have positive impact and scale, and; 3) avoid distorting private sector markets. Experience among many practitioners has shown that value chain analysis is a useful tool that can help identify constraints to MSME growth and competitiveness in a given value chain. When combined with an orientation towards MBSs an approach emerges that can result in programs with significant impact on MSME's as well as improved competitiveness of the targeted sectors as a whole. This approach combines the strengths of value chain analysis with methods for promoting sustainable MBSs that result in MSME and industry competitiveness. It allows practitioners to understand market dynamics, identify major constraints and opportunities, and promote sustainable economic solutions to identified constraints. Many donors, practitioners, and projects are already using a value chain approach for their enterprise development programs. These include programs targeting specific agricultural products, manufacturing activities, and professional associations. The approach presented in this paper can help ensure that solutions for MSMEs will continue once the program is over and that impact will be sustained.

DESCRIPTION OF APPROACH : The approach to program design presented in this paper is comprised of six steps (see Figure 1 below).

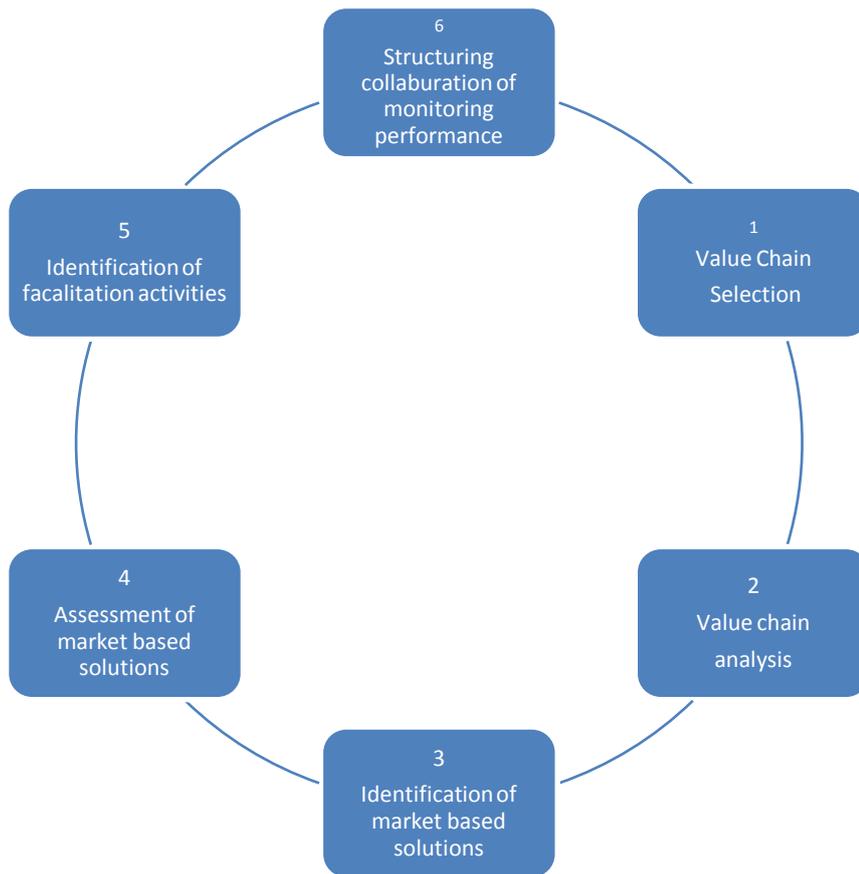


Fig 1. Steps in Value Chain Program Design

III. VALUE CHAIN SELECTION

Selection criteria such as unmet market demand, number of MSME’s in the value chain, and the presence of market actors with incentives to invest in their relationships with MSMEs are used to select value chains for more detailed analysis and targeting. Determining criteria for value chain selection requires strategic thinking about overall program objectives and how to maximize impact and it should reflect the goals of the donor/implementing agency as well as the capacity, experience, and expertise of the facilitating organization(s).

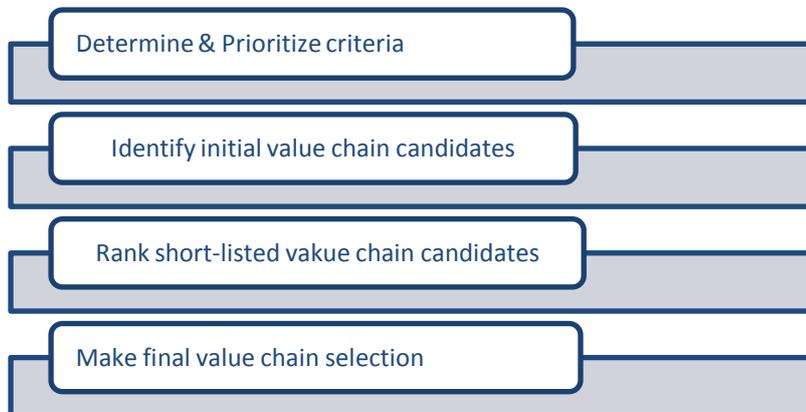


Fig 2. Stages in Value Chain Selection:

Once selection criteria have been established, short-listing of initial value chain candidates is carried out. Figure 2 below depicts the two principle selection criteria, "unmet market demand" and "potential number of MSMEs (including employees)". The short-listing process should be as objective as possible and based on actual quantitative data, where available. The relative importance of one criterion versus the other should also be factored into the selection process to choose between equally attractive value.

Potential Number of MSMEs
(incl. employees)

HIGH		Attractive
MEDIUM		
LOW	Not Attractive	

Fig 3. SHORT-LISTING MATRIX

Having narrowed down the choice of value chains, it is important to rank and prioritize the final short-list. Information to establish the score for each criteria can be gathered from individual interviews of key informants, during focus group discussions, or internally based on available primary and secondary data of the value chains. Having ranked a short-list of value chains, the final step is to decide which ones to select for further analysis. In determining how many value chains to analyze it is important to consider the amount of time and resources available for value chain analysis as well as subsequent implementation activities.

Value Chain Analysis

The basic objectives of this analysis are to:

- Identify primary actors in value chain, their roles, and interrelationships (market systems)
- Identify sales markets, unmet demand, and international competitors
- Identify supply channels and trends within value chain
- Identify constraints and opportunities that inhibit value chain growth and competitiveness

Using structured interview guides, value chain constraints can be identified during interviews with value chain participants. Various constraints are used in the interview guide to systematically look at all areas that typically affect the success of a business. the constraints might need to be addressed concurrently in order to have the desired impact on small-scale producers.

Identification of Market-Based Solution(s)

The identification of market based solutions (MBSs) is directly linked to the value chain constraints identified during value chain analysis. Once constraints are identified one can think of (potential) MBSs that could address them. The true feasibility of the proposed MBS will be assessed in the next step. MBSs are commercially viable solutions which address business constraints in a sustainable manner and strengthen existing transactions between target MSMEs and other market actors. These types of MBSs can include provision of training, access to inputs, provision of design services, access to international markets, etc.

ILLUSTRATIVE CASE: - Identification of Value Chain Constraints and (Potential) MBSs(a typical Agri-firm)

Constraints	Market-Based Solution (Potential)	Existing Providers of the MBS
High cost of inputs	Provision of, and access to, affordable fertilizers, chemicals and quality seeds	Stockists Exporters Producer Organizations
Lack of knowledge and skills in crop husbandry	Training and provision of extension services	Exporters Input Supply Companies Government ; NGOs
Expensive irrigation equipment	Provision of affordable irrigation equipment to small-scale growers.	Irrigation equipment suppliers
Lack of access to affordable credit	Access to growers of affordable credit	Micro-lending institutions Exporters
Produce not suitable for export going to waste.	Access to alternative uses of produce not suitable for export to minimize loss to growers	Exporters Research Institutions
Lack of respect for contracts between growers and exporters.	Access to mediation for breach of contract between growers and exporters	Government agency

MBSs identified earlier are short-listed and prioritized to identify those that will be subjected to more in-depth assessment. MBSs that fall within a pre-determined “attractive” range are given highest priority.

Assessment of Market-Based Solutions

Once the MBSs are selected, they undergo a more rigorous assessment. This assessment helps determine whether or not the MBS can be commercially viable. Information and data on each targeted MBS are compiled and analyzed including:

- Existing providers
- Number of potential and actual users (beneficiaries)
- Challenges to provision and use of the solution
- Awareness of the MBS among potential users
- Proposed provider (s) to target for facilitation activities
- Commercial viability of the MBS

It is at this step that potential private sector MBS providers are identified, as well as incentives and challenges to provision. Later into the program design process, program facilitation activities will be based on helping private sector providers address the challenges identified during MBS assessments. The inputs have to undergo through a filtration process as:

Identifying MBS Providers (Lead Firms)

Existing or potential MBS providers, also known as “Lead Firms” (LFs), are identified during the MBS assessment. LFs include: a) small, medium, and large firms that have forward/ backward commercial linkages with targeted MSMEs; b) dynamic market actors that can promote greater integration of MSMEs into value chains, and: c) companies which provide important goods and services to MSMEs. Examples include input suppliers, buyers of MSME products, brokers/ traders, exporters, consultants/ service providers, and training organizations.

Assessing the Feasibility of Market-Based Solutions

Part of the MBS assessment involves determining how the cost of the MBS will be covered by the targeted LFs. Two ways that the costs of providing MBSs to MSMEs can be sustained in the market are: 1) charging fees, and 2) "embedding" the MBS as part of a transaction.

Presentation of MBS assessments

Market assessment information is presented to participants during a one-day focus group discussion with value chain representatives. This enables them to validate the information and then propose interventions to address constraints to the proposed MBSs.

Identification of Facilitation Activities

During this step, the Lead Firms identified in Step 4 are invited to propose initiatives that will help them overcome the challenges they face in providing targeted MBSs in a sustainable manner. This is done through “invitations for applications”, focus groups, strategic planning sessions, question guides, and in-depth discussions. Interventions proposed by these Inclusive Businesses that meet program requirements can then be supported with both technical and financial assistance.

Technical support

Development program’s technical support include assisting LFs to:

- develop business and marketing plans for new initiatives
- develop strategies for outgrowing operations
- organize training of trainers for company staff
- prepare for trade shows and exposure visits
- access technical specialists with specialized knowledge and skills
- identify and adopt information communication technologies
- conform with industry standards and buyer requirements

Financial Support

In addition to technical support, collaboration between development programs and LFs often includes financial support (cost share) where the development program helps to offset some of the costs and mitigate the risks that the LF faces in making new investments (investments that will benefit producers they buy from or sell to). It will also be a basis to provide incentives for the LF to move forward with an initiative that otherwise they might not be willing or able to do in the near term.

Structuring Collaboration and Monitoring Performance

Carefully structuring collaboration with LFs is done through Memorandums of Understanding (MOUs) and Addendums to the MOUs that specific how the DO will support specific LF initiatives/ interventions. Once activities are underway, special care is made to closely monitor both implementation and impact of the LF interventions. Three systems are used to ensure that this is accomplished:

- [1] Monitoring Checklists for specific LF interventions
- [2] Monitoring and evaluation systems for the development project
- [3] Technical and financial reporting from LFs

Performance measurement systems are then developed based on a causal model that connects project facilitation activities to intermediate and final results. These systems are based on a series of cause-and-effect relationships starting with project activities and proceeding to outputs, outcomes, and ending with intended impacts. Formal agreements are also established with the participating market actors.

IV. GENERAL PRINCIPLES

The following principles can be helpful in program implementation and in promoting donor coordination.

- [1] Providers of market-based solutions must cover their costs through transactions with enterprises - The implication of this principle is that donors would not subsidize the direct provision of training, inputs, or other products/services to MSMEs.
- [2] Local organizations need to determine if they are facilitators or direct providers of MBSs. If they are facilitators then their objective is not to sustain themselves through commercial provision – but rather to use donor funds to promote sustainable solutions among market actors. Donors should not fund organizations that claim to be both direct providers and facilitators of solutions.
- [3] Facilitators should have a clear exit strategy from the beginning with benchmarks for pulling out of temporary provision or ending facilitation activities.

Additional principles for facilitation of value chain and market development programs include:

Professionalism

- manage collaboration with LFs in businesslike fashion; deliver what is promised
- ensure LF information is kept confidential; be clear that sensitive LF business information will not be shared with others.

Understand Private Sector and Business Principles

demonstrate understanding of private sector competitive and operating environment
recognize LFs as innovators, economic drivers, etc.
understand and appreciate LF risks

V. CONCLUSION

The approach to enterprise development program design presented in this paper provides practical tools to link value chain analysis with the development of market-based solutions. Bridging these two aspects of MSME development can result in private sector programs that address value chain constraints and opportunities in a sustainable fashion, thereby providing long-term benefit to MSMEs. Many donors, practitioners, and projects are already using a value chain approach for their enterprise development programs. These include programs targeting specific agricultural products, manufacturing activities, and professional associations. There are both advantages and risks in this approach. One of the main advantages is that it addresses the specific needs of MSMEs operating in different industries, which tend to vary greatly. One of the risks of the approach is its dependence on the continued viability of the targeted value chain. If that market fails for some reason, program facilitation activities will not have their desired impact. This risk can be mitigated, however, by focusing on several value chains at the same time. It can also be mitigated by targeting multiple markets within a given value chain, for example both domestic and export markets. Another challenge is finding or developing the requisite expertise to implement the approach - which generally requires a multidisciplinary person or team skilled in economic analysis, business needs assessment, facilitation, and enterprise development.

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