



Schweizerische Eidgenossenschaft  
Confédération suisse  
Confederazione Svizzera  
Confederaziun svizra

Direktion für Entwicklung und Zusammenarbeit DEZA  
Direction du développement et de la coopération DDC  
Swiss Agency for Development and Cooperation SDC  
Agencia Suiza para el desarrollo y la cooperación COSUDE

# **Comparative Approaches to Private Sector Development – a MMW perspective**

## Working paper

Authors:

Marieke de Ruijter de Wildt, David Elliott, Rob Hitchins  
The Springfield Center

April 2006

**Employment and Income Division**  
Freiburgstrasse 130, CH – 3003 Bern  
Tel. ++41 31 322 10 65, Fax ++41 31 323 08 49  
[e-i@deza.admin.ch](mailto:e-i@deza.admin.ch)  
[www.deza.admin.ch/ei](http://www.deza.admin.ch/ei)

*This paper is a contribution by the Springfield Centre, on behalf of the FAUNO Consortium. The views of the author are not necessarily the views of SDC.*

## 1. INTRODUCTION

This document has been prepared by Fauno and is intended to serve as a focus for SDC Employment and Income (E&I) Division discussions about the relationship between various private sector development (PSD) fields. This note addresses a common challenge in private sector development: how to reconcile apparently diverse concepts such as *value chains, subsectors, clusters and networks, enabling environment* and *local economic development*, and the approaches related to them.

In doing so, the document will try to illustrate that recent thinking on *making markets work for the poor* rather than being a substitute for or in competition with these other concepts and approaches, is complementary to them, providing an overarching framework to aid understanding about their use in efforts to reduce poverty.

This document builds on an initial briefing note prepared by Fauno for E&I “*The enabling environment for business and other fields of private sector development*” and feedback from E&I on that note. This document has three purposes:

- To provide orientation to this topic;
- To frame discussions in the E&I-Fauno workshop of November 2005; and
- To serve as the basis for a more expansive document or range of documents addressing this topic.

This paper has been updated to reflect discussions and findings from the Fauno workshop held in November 2005.

This document comprises four sections in addition to this introduction: an overview of key PSD fields; the relationship between these fields and Making Markets Work (MMW); and implications for development agencies and in particular E&I.

## 2. OVERVIEW OF KEY PRIVATE SECTOR DEVELOPMENT FIELDS

This section discusses the following five key fields of private sector development, providing an overview of their rationale, origins and definition, key aspects of the approach and current developments:

- Value chain analysis
- Subsector analysis
- Clusters and networks
- Enabling environment
- Local economic development

These overviews cannot be comprehensive. Reflecting the diverse nature of development and development organisations in general, these fields are subject to pronounced variations in definition, interpretation and application. Seldom does a standard view exist.

Given this caveat, what follows is an attempt to define the extent to which these various fields represent descriptions of socio-economic phenomena, justify themselves in terms of poverty reduction, establish conceptual foundations, serve as frameworks for understanding and provide guidance for development agency intervention.

### 2.1 Value chain analysis

#### 2.1.1 *Origins, rationale and definitions*

A value chain describes the full range of activities required to bring a product from its conception to its end use and beyond. This includes activities such as design, production, marketing, distribution and support to the final consumer. The activities that comprise a value chain can be contained within a single firm or divided among different firms. Value chain activities can be contained within a single geographical location or spread over wider areas. In sub-sector analysis nomenclature, a value chain is indistinguishable from a *marketing channel*. (See however “Current developments”.)

Value chain analysis (VCA) therefore is the methodology by which the structure and processes of a value chain are understood. Value chain analysis originates from three distinct sources:

- The Francophone *filière* approach emerged in the 1960s.<sup>1</sup> It is seen as a neutral, value-free technique applied to analysing existing marketing chains for agricultural commodities. The *filière* approach made no attempt to develop a unified theoretical approach, but was used purely to delineate the scope of analysis.
- In the 1980s modern value chain analysis emerged from the work of Michael Porter<sup>A</sup> where it was developed as an instrument for identifying the value of each

---

<sup>1</sup> Developed by researchers at the Institute National de la Recherche Agronomique (INRA) and the Centre Internationale en Recherche Agronomique pour le Développement (CIRAD)

step of production. This information could then be used to reconfigure a value chain to improve its competitive advantage.

- The Global Commodity Chain (GCC)<sup>2</sup> approach emerged in the 1990s. Advocates would claim that it emphasises four additional elements to Porter's work: an international dimension; power relations within the chain; coordination as a source of competitive advantage; and organisational learning as the means by which firms improve their position in the chain. In reality the focus on power relations or *governance* is probably the most distinctive contribution of GCC. GCC attempts to develop a unified theoretical framework which can identify key points for *upgrading* firms within particular types of commodity chain in order to change existing power relations within the chain. GCC focuses on *lead firms* which control major resources in the chain and thus determine value chain power and dynamics. Power in value chains may be producer-driven (usually capital/technology intensive industries, such as automotive manufacture) or buyer-driven (usually labour intensive industries, like garment manufacture).<sup>3</sup>

GCC has added a more value-based dimension to VCA. Recent application has focused on globalisation: to understand why many of the potential benefits of globalisation fail to reach the very poor; why particular countries and types of enterprise find it difficult to enter certain sectors; and identify policy implications. Fair trade and trade justice movements have used VCA as a basis for advocacy arguments (around changing global trade rules and market access).

### 2.1.2 Approach

VCA conceptualises enterprises, not as discrete entities, but as part of a system of different but linked production and exchange activities.

At its core, VCA plots the flow of goods and services up and down a chain, and possibly even between different chains. Considered in this way, "*the value chain is a descriptive construct, at most providing a heuristic framework for the generation of further data*".<sup>B</sup>

As noted above, recent advances in VCA have focused on three primary aspects: understanding where value added occurs in a chain; understanding the power dynamics of relationships between actors in a chain; and understanding the nature of power dynamics across the entire chain. The purpose of this analysis is defined in the concept of upgrading. This refers to the acquisition of technological capabilities and market linkages that enable firms to improve their competitiveness and move into higher-value activities. Analyses of upgrading from a value chain perspective pay particular attention to the ways in which value chain linkages facilitate or obstruct upgrading.

### 2.1.3 Main steps in VCA

- Map the chains of interlinked production and exchange activities in particular sectors or subsectors
- Map the geographic spread of linkages over international, national and local
- Identify the governance structures affecting the distribution of value between activities and geographical areas
- Identify the interventions directly

<sup>2</sup> Developed by Gereffi et al within the framework of an analysis of the political economy of development and underdevelopment (linked with world systems theory and dependency theory)

<sup>3</sup> There is also the concept of *World Economic Triangles*, which emphasise international-local linkages, and combine elements of value chain and cluster thinking. This is a more conceptual than analytical framework

<p>areas</p> <ul style="list-style-type: none"> <li>Identify key stakeholders at different levels and locations of the chain, and in relation to different opportunities and constraints</li> <li>Measure the relative value accruing to different levels, locations and stakeholders of the chain</li> </ul>	<p>targeting different levels of the chain</p> <ul style="list-style-type: none"> <li>Clarify the likely direct and indirect impacts at these different levels</li> <li>Explore the different alternative levels of intervention or strategy</li> </ul>
---	---

### 2.1.4 Current developments

From a development practitioner perspective four key issues are emerging:

- At its core VCA is a value-free technique. It says nothing, for example, about poverty and how it can be reduced. However, the context within which VCA is increasingly being utilised is concerned with poverty. As a result, frameworks are emerging that ask specifically where the poor are located within a value chain and seek to identify pro-poor opportunities.
- Whilst VCA presents a systemic view of inter-firm organisation, by concentrating only on vertical linkages this view is only a partial one. Understanding how value chains fit within the wider national economy is increasingly seen as important.
- VCA is increasingly being used for more micro-level interventions rather than inform macro-level policy change. Consequently new techniques are required for gathering information and determining interventions.
- As a guide for intervention VCA sets only the rather loosely defined objective of upgrading. It says nothing about *how* to approach upgrading. This can lead to inappropriate intervention practices.

USAID, particularly under the Office for Microenterprise Development's AMAP, is investing considerable resources in the value chain field. Its emerging *value chain framework* (VCF) places VCA at its centre, but builds on this to address the four emerging issues mentioned above. Moreover, in contrast to earlier thinking, value chains now appear to be regarded as a collection of market channels (as per subsector analysis) rather than as synonymous with a market channel.

### 2.1.5 Overview of value chain analysis

Poverty rationale / world view	Framework for analysis	Guidance for intervention
<p><b><i>Increasingly defining a poverty rationale</i></b></p> <p>At its core, VCA has no world view on poverty reduction. It is value-neutral. The context within which VCA is used defines values that become associated with VCA. GCC is concerned with understanding the organisation of global value chains and is used to advocate for changes in international trade rules and practices for the benefit of lower income countries. In this sense GCC is defining a more explicit macro poverty focus on VCA.</p>	<p><b><i>Strong, but narrow systemic focus, but improving</i></b></p> <p>Generally, VCA offers a strong framework for analysis. However, (a) by only offering a partially systemic view it is limited, and (b) a world view on poverty reduction would influence what questions are asked under VCA, and how they are asked. Used in isolation of a framework that sets values and defines objectives, VCA offers little.</p> <p>The emerging VCF seeks to address these issues. It</p>	<p><b><i>Strong guidance for analysis, weak for intervention</i></b></p> <p>In addition to lacking an explicit world view on poverty reduction, VCA does not provide common guidelines for good intervention practice. One observer notes that <i>"My concern is simply that the phrase 'assisting firm upgrading' could be misconstrued by governments, donors and firms as an exhortation, for example, to spend public money on modern equipment for particular firms or to restrict competition. It needs to be made clear that this is not</i></p>

<p>Increasingly, VCA is also being used as an approach for understanding more micro aspects of poverty; asking where the poor are located within value chains; how they can do better; and what the role of development agencies is in improving their positioning.</p>	<p>expands the analytical framework to consider (a) inter-related markets (particularly service markets) and (b) wider <i>enabling environment</i> issues.</p> <p>In mapping vertical relationships between firms, VCA is mainly suitable for product and commodity markets. It is less useful for considering service markets, public benefit services, infrastructure and factor markets.</p>	<p><i>the intention.”<sup>C</sup></i></p>
---	---	---

## KEY RESOURCES

### Physical resources:

- Porter, M. “The competitive advantage of nations”
- Gereffi, G. “Commodity chains and global capitalism”
- Kaplinsky R. et al. “A handbook for value chain research”

### Web based resources:

- [www.globalvaluechains.org/](http://www.globalvaluechains.org/)
- [www.cirad.fr](http://www.cirad.fr)
- [www.corse.inra.fr/](http://www.corse.inra.fr/)
- [www.microlinks.org/](http://www.microlinks.org/)
- [www.sdc-valuechains.ch/](http://www.sdc-valuechains.ch/)

## 2.2 Subsector analysis

### 2.2.1 Origins, rational and definition

A *marketing channel* is defined as any traceable path through a production or distribution system of product transformation. As defined, the term marketing channel equates to the term *value chain* (albeit with caveats, see “Value chains”). A sub-sector is the aggregation of alternative marketing channels for one or a group of closely related products.<sup>D</sup> *Subsectors* can be delineated by final product or a key raw material.

Subsector analysis (SSA) therefore is the methodology by which the structure and processes of a subsector are understood. SSA has its roots in pioneering work dating from the mid-1980s, which transferred SSA from its agricultural marketing roots into the world of SME development.<sup>4</sup> The context at the time was one of: (a) growing recognition of the importance of smaller firms in developing economies and consequently the increased prominence of small enterprise development as a public policy objective; and (b) frustration with the limitations of existing small enterprise research approaches.<sup>5</sup> Subsector analysis emerged as a framework to guide the analysis of small enterprise development constraints and opportunities.

A key concept within subsector analysis is *leverage*; that small focused inputs can generate commensurately larger outputs. This recognises that development agencies

<sup>4</sup> Particularly work at Michigan State University funded by USAID under their Small Enterprise Approaches to Employment Cooperative Agreement

<sup>5</sup> These (typically survey methodologies) were deemed expensive and time consuming, limited by using administrative rather than market boundaries, and by concentrating solely on the firm they offered only an incomplete and static analysis

cannot afford to work with small firms on an individual basis and that therefore they must seek to make interventions that can influence large numbers of firms with a single stroke.

Historically, virtually all early subsector analysis focused on agricultural commodities, describing and assessing the economic networks through which individual commodities are transformed and distributed to their ultimate consumers.<sup>6</sup>

Beyond its emphasis on the importance of small firms, SSA is essentially a neutral, value-free technique.

### **2.2.2 Approach**

Subsector analysis represents a *systems* approach to the analysis of economic activity. At its heart is the recognition that small firms operate in systems, and to effectively promote small enterprises one must understand the systems within which they operate. It defines a core market (the subsector) and provides a basis for analysing this. Further, it recognises that this core market operates in a wider environment that is critical to the development of particular marketing channels. This wider environment is seen as comprising “*three important components: (a) the rules [formal and informal], (b) the information flows and (c) the service institutions*”.<sup>E</sup>

SSA offers a modular approach to understanding product and commodity markets. Whilst various manuals have been developed, the basic process contains a number of key steps.

### **2.2.3 Main steps in SSA**

- Sub-sector selection based on a wider economic analysis that gives insight on issues of size, potential and relevance to target group of focus
- Definition of the basic subsector map
- Specify the environment in which the subsector operates
- Identify overlays along dimensions of particular interest (normally interpreted in practice as service market overlays)
- Collect focused qualitative and quantitative information and perform analysis
- Identify recommendations for policy and programme interventions

SSA today is seen as very similar to value chain analysis (indeed the terms are often used interchangeably). However advocates of the GCC school of VCA see SSA as being restricted to activities within national boundaries.

### **2.2.4 Current developments**

The theoretical underpinning of SSA around systems-based thinking is powerful and coherent. Its modular approach to analysis offers clarity to practitioners seeking to use the tool. Consequently SSA has been widely applied within the field of SED. However, the apparent simplicity of the modular approach has arguably led to inconsistency between the use of the tool and its underpinning systemic theory. All too often in practice the system has been defined narrowly as the sub-sector itself. Applying systemic thinking to addressing identified sub-sector constraints – of whatever nature – is often lacking. This typically results in interventions being designed to directly tackle constraints through donor-funded actions, and consequently raises concerns about issues such as sustainability, outreach and replication.

---

<sup>6</sup> Dating back to the 1960's



Further development of SSA has largely stalled, overtaken by substantial learning in the VCA field. Interestingly much of the recent evolution in VCA towards VCF has been about systemic thinking which was there in SSA from the outset in theory but neglected in practice.

SSA provides limited guidance on steps that lead to actual intervention design and practice as a result of subsector mapping.

### 2.2.5 Overview of SSA

Poverty rationale / world view	Framework for analysis	Guidance for intervention
<p><b>No explicit poverty rationale</b></p> <p>SSA in itself is arguably value-neutral. However, one might argue that the theoretical underpinning of SSA does express a world view on economic growth at least. On the one hand SSA is based on a belief that small enterprises are important for growth and employment creation.</p> <p>Further, that supporting small enterprises effectively requires understanding of firm dynamics in a wider systemic context. Firms operate in systems, and one must understand those systems if firms are to be supported effectively.</p> <p>SSA does not take a view on poverty reduction directly.</p>	<p><b>Systemic underpinnings, strong, narrow application</b></p> <p>Generally, SSA offers a strong framework for analysis. However its practical application tends to be narrow, neglecting its underpinning systemic theory, by failing to rigorously analyse overlays for services and institutional factors.</p> <p>A world view on poverty reduction would influence what questions are asked under SSA, and how they are asked. Used in isolation of a framework that sets values and defines objectives, SSA offers little.</p> <p>In mapping vertical relationships between firms, SSA is mainly suitable for product and commodity markets. It is less useful for considering service markets, public benefit services, infrastructure and factor markets.</p>	<p><b>Strong guidance for analysis, weak for intervention</b></p> <p>In addition lacking an explicit world view on poverty reduction, SSA does not provide any guidelines for good development intervention practice. In the absence of guidelines, all too often a typical intervention response is to directly intervene to fix whatever constraints are identified. Whilst this may deliver short term impact, it is criticised for not taking sustainability seriously.</p>

#### KEY RESOURCES

##### Physical resources:

- Boomgard, J. et al Subsector analysis: its nature, conduct and potential contribution to small enterprise development

##### Web based resources:

- [www.msu.edu/](http://www.msu.edu/)
- [www.katalystbd.com/](http://www.katalystbd.com/)
- [www.commark.org](http://www.commark.org)

## 2.3 Clusters and networks

### 2.3.1 Origins, rationale and definition

The concept of clusters – as a “*sectoral and geographical concentration of enterprises*”<sup>F</sup> – has been present in industrial economics literature since the late 19<sup>th</sup> century. The concept is a somewhat nebulous one however, lacking a common

definition. However their essence is about proximity, networking and specialisation, as recognised by Porter:

*“Clusters are geographically close groups of interconnected companies and associated institutions in a particular field, linked by common technologies and skills. They normally exist within a geographic area where ease of communication, logistics and personal interaction is possible. Clusters are normally concentrated in regions and sometimes in a single town”.*

The concept of networks is closely related to that of clusters (and equally difficult to define), but without a fixed spatial dimension. In fact networks are seen as a fundamental element of clusters.

*“Networks are formal and informal [arrangements] that facilitate the exchange of information and technology and foster various kinds of co-ordination and collaboration in a cluster.”<sup>G</sup>*

The basic rationale behind focusing on clusters and networks is that inter-firm cooperation can collectively improve the efficiency of participating enterprises beyond the level which could be expected without cooperation. Clustering and networking is particularly pursued in response to competitiveness constraints arising from small firm size, yielding benefits such as:

- Improved access to inputs and services
- More effective advocacy and buyer/supplier negotiation
- Cost sharing and participating for more effective innovation and R&D
- More efficient marketing and market access
- Opening possibilities for increased specialisation

Just as there is a diversity of definitions, there is equally a diversity of approaches to cluster analysis and development. Clustering and networking development is mainly concerned with upgrading the competitiveness of existing enterprises. It tends not to focus on providing physical inputs for the creation of new clusters.

Typically cluster and network development has focused on urban areas and has strong links to the local economic development field. In focusing on cooperation between firms at the same level in the value chain (horizontal) and cooperation along value chains (vertical) cluster and network development has links to VCA (as a tool for analysis) and World Economic Triangle (see “Value chains”).

Key proponents of cluster and network development have been UNIDO, the EU and its member states and the OECD. Clusters have also become popular with many developing country governments, most notably India and Indonesia.

### **2.3.2 Approach**

As noted above, there is no single approach to cluster and network analysis or development. However the approaches are the subject of numerous practitioner manuals (such as Humphrey and Schmitz). Broadly, most approaches follow a modular process, based on some key steps.

### **2.3.3 Main steps in cluster and network development**

#### **General preparation process**

- Cluster identification
- Cluster analysis

#### **General implementation process**

- Formation of cluster engagement group (companies that will participate in the

- Cluster selection and initial engagements
- Identification and recruitment of cluster manager or network broker
- process)
- Presenting analysis, facilitating discussions, identification of common challenges, and formation of initial engagement plans
- Implementation and monitoring of engagement plans
- Exit strategy

The conventional approach is based on a cluster manager or network broker facilitating business and cooperation relationships between member firms. Having established a basis for cooperation, demonstrated benefits, and built a momentum, the idea is that the cluster manager / network broker can withdraw leaving the system fully functioning and able to move forward without further support.

### 2.3.4 Current developments

As described in the above approach, typically the cluster manager / broker function is considered a finite and temporary role. However, increasingly these roles are being recognised as integral functions, needed to ensure that the cluster or network continues to collaborate and upgrade. Sustainability is therefore a key challenge: how to incorporate the cluster / broker function within the local institutional system.

The purpose of promoting clusters is also being debated. Many fields of economic development have focused on clusters. Programmes to promote innovation and competitiveness have often been based on clusters or networks. In agri-business development, clusters of producers are often referred to and are central to sector promotion strategies (normally for delivery of business services). Local economic development is another field where clusters have been a prime focus.

Finally, as development interventions are increasingly being required to be transparent about how they contribute to poverty reduction, cluster and network initiatives are re-thinking how they can fit in to poverty reduction strategies. This demands that they think beyond general growth arguments to consider how the poor can benefit from cluster and network initiatives. This might entail trade-offs between promoting high technology clusters in urban centres, typically demanding proportionally higher skills or assets than possessed by the poor and promoting low technology clusters in peripheral areas, that might be more inclusive of the poor, but whose growth trajectory is likely to be lower.

### 2.3.5 Overview of clusters and networks

<b>Poverty rationale / world view</b>	<b>Framework for analysis</b>	<b>Guidance for intervention</b>
<p><b>No explicit poverty rationale</b></p> <p>At its core, cluster and network thinking has no explicit world view on poverty reduction.</p> <p>However, cluster and network thinking is based on a belief that small enterprises are important for growth and employment creation. The underlying concept of clusters and networks is based on one of increasing efficiency through encouraging</p>	<p><b>Narrow systemic focus</b></p> <p>Clustering and network approaches offer a framework for identification of existing clusters, and some basic analysis of cluster dynamics (often drawing on other methodologies, like VCA). The process of analysis for intervention design tends to be generated through the intervention process itself.</p>	<p><b>Strong emphasis on operational aspects</b></p> <p>The main thrust of cluster and network initiatives lies in a framework for intervention. Many manuals and guides exist focusing on methodologies for recruiting and running clusters and networks.</p> <p>The emphasis of guidance tends to be operational rather than strategic (eg it does deal with issues like sustainability.)</p>

cooperation; that in turn fosters competitiveness which drives economic growth.	Generally, clusters and networks only offer a limited framework for analysis.	
---	---	--

## KEY RESOURCES

### Physical resources:

- Humphrey J. et al "Principles for promoting clusters & networks of SMEs"
- Porter, M. "The competitive advantage of nations"

### Web based resources:

- [www.unido.org](http://www.unido.org)
- [www.worldbank.org](http://www.worldbank.org)

## 2.4 Enabling environment

### 2.4.1 Origins, rationale and definition

The *enabling environment* is a broad concept, widely applied in and beyond economics and development; as such the term can mean many things to many people and remains without a clear definition. In the private sector development field its widest definition can comprise "*all factors external to firms, including the policy, legal and regulatory framework; external trade policy; governance and institutions; physical security; the social and cultural context of business; macroeconomic policies; access of firms to financial and business services; and the availability of physical and social infrastructure services.*"<sup>H</sup>

More commonly, the enabling environment is thought of in rather narrower terms as "*the extent to which government policies, laws and regulations set the rules of the game for business and influence, positively or negatively, the performance of markets, the incentives to invest, and the cost of business operations.*"<sup>I</sup> Terms such as *investment climate, business climate, business environment* and *framework conditions* are seen as synonymous with the term enabling environment.

In the field of economics and development, the term first gained prominence in the context of the wave of market-oriented reforms advocated in the 1980s. During this time there was recognition that policy orientation was an important determinant of economic growth performance. So-called *market-friendly* policies were seen to correlate with strong growth performance. The term enabling environment therefore emerged as a reference to define the extent to which a country's policies were deemed market-friendly.

More specifically the term emerged in the SED field in relation to the idea of a *level playing field*, as a response to perceived policy, regulatory and public service access biases in favour of large-scale formal sector. These biases were seen to exclude or impact unfairly on the significant but largely invisible rump of small enterprises and informal activities which comprise the bulk of most developing economies. In this respect enabling environment referred to objectives to make policy, regulatory and public service orientation more conducive to small-scale and informal economic activities.

The emerging focus on enabling environment is based on a construct linking enabling environment to economic growth and poverty reduction. The logic of this construct is based on the links between poverty reduction and growth, growth and private sector development, and recognition of the importance of factors external to firms, but which strongly affect their investment decision-making and overall

performance (factors that increase risks and costs in starting, running or closing a business).

The importance of an enabling environment as a driver of growth performance is explored in detail in a 2003 World Bank research paper by Beck et al<sup>J</sup>, which came to three main conclusions:

- Whilst a large SME sector is a characteristic of successful economies, there is no evidence that small firms are necessarily a driver of growth (viz larger firms).
- The overall business environment facing both large and small firms – as measured by the ease of firm entry and exit, sound property rights, and contract enforcement – is a driver of economic growth.
- However, whilst a sound business environment tends to help the poor by accelerating aggregate growth, the results do not suggest that the business environment influences poverty beyond its influence on the overall economy.

For most development agencies, the enabling environment is in effect an objective, rather than a technical approach or methodology for intervention. The rationale for focusing on enabling environment issues is that it is more systemic. Focusing on the framework conditions beyond individual firms offers agencies greater potential to achieve leverage and impact than more direct measures.

### 2.4.2 Approach

Given that enabling environment is an all-encompassing term, it is not surprising that there is not a common approach for enabling environment interventions. As noted above, it is not really an approach per se. A review of donor practice<sup>K</sup> indicates four main areas of donor enabling environment focus: macro-economic stability; governance<sup>7</sup>; policy, law and regulation; and institutional framework and capacity.

Specialised approaches often exist for each of these areas. In general terms however there are some typical assessment and intervention approaches.

### 2.4.3 Typical approaches used in EE interventions

Assessment	Intervention
<p>A number of methodologies are used.</p> <p>Typically tools offer a common basis for cross country/region comparison, including:</p> <ul style="list-style-type: none"> <li>• Business climate assessments</li> <li>• Investment climate assessments</li> <li>• Investor roadmaps</li> <li>• Doing business surveys</li> <li>• SME country mapping</li> <li>• Global entrepreneurship monitor</li> </ul> <p>Other assessment tools are more specific eg regulatory impact assessment or organisational assessment methodologies.</p>	<p>Interventions typically focus on support for:</p> <ul style="list-style-type: none"> <li>• Privatisation and parastatal reform</li> <li>• Investment, competition and commercial justice reform</li> <li>• Reform relating to general enabling environment and pro-poor growth promotion</li> <li>• Regulatory reform</li> </ul> <p>Types of support would include:</p> <ul style="list-style-type: none"> <li>• Budgetary support</li> <li>• Capacity building and technical assistance</li> <li>• Policy research</li> <li>• Promotion of dialogue between public and private sectors</li> </ul>

<sup>7</sup> This is a broad term that refers to the ways in which governments administer and manage society and the economy. It includes issues such as the rule of law, government administration, corruption, security, accountability, etc. Note that the term is also used in relation to power relations in recent thinking on value chains

There is seldom much direct connection between assessment tools and intervention design and planning, although assessment processes and the information that they generate can be used as a means for engaging with key stakeholders. One problem is that many assessment tools tend to identify symptoms of problems rather than the root cause of problems (eg the fact that it takes 270 days to process formally register a business, rather than the policy, regulatory or administrative reasons for such a lengthy process), providing little insight therefore into the required nature of intervention.

#### 2.4.4 Current developments

There are many debates and developments occurring within the variety of technical areas consumed within the all-encompassing term of enabling environment. From a SED perspective, five issues stand out.

First, debates around finding a common definition and framework for enabling environment. The Donor Committee for Small Enterprise Development is leading the work in this area, but it is at a very early stage.

Second, there is a concern that simply “*getting policies and regulations right*” is unlikely to be sufficient to stimulate the desired supply and demand side responses that will lead to pro-poor growth. Allied to this is concern about the extent to which interventions bring about sustainable institutional change as the foundations for an enabling environment in the long term (eg through building improved local governance and advocacy structures), rather than – as is more common – seeking to change rules and regulations directly.

Third, there is increasing awareness of the *cross-cutting* nature of the enabling environment and therefore a need to consider it more systemically, for example, in the way in which it relates to key sectors like infrastructure or agriculture, rather than only in generic terms.

Fourth, there is concern about measuring the impact attribution of enabling environment initiatives on poverty. On one hand the rationale for enabling environment initiatives is that they potentially offer opportunities for greater leverage and impact. On the other hand, attribution of impact to programme interventions is fraught with methodological challenges. There is a general lack of systematic evaluation in this field.

Fifth, there are practical issues which have yet to find resolution in the midst of high-level conceptual discussions. These include: defining entry points for intervention, engaging appropriately with partners, moving from research to intervention design; and defining the role of development agencies.

#### 2.4.5 Overview of enabling environment

Poverty rationale / world view	Framework for analysis	Guidance for intervention
<b>Limited poverty rationale</b>	<b>Narrow systemic focus</b>	<b>Weak</b>
As a catch-all term, enabling environment does not have a cohesive world view on poverty reduction.  However, the essence of the term does represent a belief that growth is good for poverty	No common framework for understanding the enabling environment.  Enabling environment thinking is systemic in some respects, but tends to have a narrow focus on policy, legal and regulatory	Whilst some principles of good practice exist, there is little “how to” guidance for practitioners.  Interventions tend to either get directly involved in bringing about change (with resultant sustainability problems) or

<p>reduction and that an enabling environment for private sector development is good for growth.</p> <p>In this sense enabling environment is as much as anything an objective or an aspiration.</p>	<p>reform.</p> <p>Tools used for specific elements of enabling environment have narrow application (eg RIA) or often fail to identify the root causes of problems (eg institutional factors).</p> <p>However these problems are starting to be recognised and addressed.</p>	<p>alternatively are very hands-off, eg research/studies.</p>
--	--	---

## KEY RESOURCES

### Physical resources:

- White, S. et al "Review of DFID activities in the enabling environment"
- Beck, T. et al "Small and medium enterprises, growth and poverty: cross country evidence"

### Web based resources:

- [www.worldbank.org](http://www.worldbank.org)
- [www.dfid.org](http://www.dfid.org)

## 2.5 Local economic development

### 2.5.1 Origins, rationale and definitions

No commonly accepted definition of local economic development (LED) exists, although most practitioners would generally agree with the statement that "*the purpose of LED is to build up the economic capacity of a local area to improve its economic future and the quality of life for all. It is a process by which public, business, and non-governmental sector partners work collectively to create better conditions for economic growth and employment creation*".<sup>L</sup>

LED therefore encompasses both objective and process: it is about *building local economic capacity* in *defined areas* by establishing the local development agenda amongst *key stakeholders*, such as local governments, business and civil society groups.

Distinctive features of LED include:

- An explicit geographic dimension (usually sub-national)
- A focus on local economic capacity development
- Processes based on multi-stakeholder participation

However, as Meyer-Stamer<sup>M</sup> observes, LED lacks a conceptual framework, particularly to describe what constitutes the *local economy*. It faces a similar problem to the *enabling environment* concept in terms of how broad and inclusive its scope should be.

The roots of LED lie in urban and physical planning, but it is a multi-disciplinary field drawing on economics, geography, sociology, business and competitiveness fields. It emerged in the context of regional economic decline and marginalisation in industrialised countries in the 1960s and 1970s. It began to appear in the developing world in the 1980s and 1990s. Three main stages are usually recognised in the evolution of LED:

- 1960s to 1980s: predominantly public sector-driven, focusing on FDI and investment in large infrastructural projects.
- 1980s to mid-1990s: public sector-driven, investment-oriented, but more targeted towards certain sectors and including *soft* as well as *hard infrastructure*.
- Late 1990s to date: continues to be public sector-led, but increased focus on public-private partnership, leveraging private investment and initiative and a growing focus on promoting an enabling environment and soft infrastructure (eg clusters).

LED focuses on the sub-national level, mainly in urban or peri-urban areas. It tends to be concerned with three main strata of *geo-political organisation* and *public administration*: (a) the *national level* (in terms of how it determines the legal basis, structures and resource allocation to sub-national levels); (b) the *regional level* (usually as an intermediate strata between central government and local government); and (c) the *local or municipal level*. It has achieved particular prominence in relation to decentralisation and regional autonomy trends.

A key rationale for LED has been employment creation in economically disadvantaged areas, and latterly, the promotion of growth in order to achieve this. LED is motivated by the recognition that such efforts (and the role of government in particular) need to be more coordinated: as Porter has wryly observed, it has been common for government to create a multitude of regulatory and bureaucratic obstacles for business “*while at the same time running many programmes to train people for non-existent jobs in industries with no projected growth*”<sup>N</sup>.

Key players in LED have been GTZ and the EU. The Club du Sahel and the OECD are promoting an LED methodology called ECOLOC. This is being rolled out in several African countries, with some support from SDC governance division.

### **2.5.2 Approach**

Reflecting the diversity of its roots and objectives, there is not a common approach to LED. It has been developed by practitioners who need to work with governments and other stakeholders, has combined different combinations of economic, political, social and environmental thinking and practices, and has evolved in different directions around the world. However LED processes generally emphasise *stakeholder dialogue*, *local empowerment and ownership* and more *transparent and accountable local institutions*.

LED approaches therefore overlap with (a) public sector and governance reform and – increasingly – (b) the private sector development field, including enabling environment, clusters and value-chains and business and financial services promotion. LED activities might focus on a broad range of areas: business and investment climate, infrastructure, local business development and growth, inward investment, sector and cluster development, regeneration, skills and employment for specific disadvantaged target groups.

Though defined differently in different organisations, a LED approach usually involves several key steps (see below). In practice, preliminary activities revolve around organising local efforts and the establishment of a (usually aid-funded) LED team, ideally within a local government and which involves public, private and civil society stakeholders. Some form of diagnosis is then conducted based on qualitative and quantitative data. An LED strategy is then developed, which typically includes a local economic vision, goals, objectives and a plan of action over a three to eight year time frame. The main difference between approaches usually concerns the



level of emphasis put on participation and whether it is before or after diagnosis is conducted.

### **2.5.3 Main steps in LED processes**

- Mobilising and organising local effort
- Conducting local economy assessment
- Developing a local economic strategy
- Implementing the local economic strategy
- Reviewing the local economic strategy

### **2.5.4 Current developments**

LED objectives and processes have been widely adopted by numerous agencies over recent years, and there is some dissatisfaction with the outcomes of interventions to date<sup>O</sup>. Whilst there is no clear overall direction emerging for the field, a number of challenges and trends which are pertinent to E&I stand out:

First, the field has been hampered by unclear theoretical and conceptual underpinnings. For instance, this lack of clarity has led to confusion between community development and LED. The latter tends to have a stronger social dimension, whilst in practice LED increasingly appears to be moving in a more private-sector driven and economically-oriented direction.

Second, LED's roots in urban and physical planning have resulted in an overemphasis on strategy and planning emphasis, rather than action, which has proved frustrating for some stakeholders. Some practitioners are now adopting more action-oriented approaches eg Mesopartner's Participatory Appraisal of Competitive Advantage (PACA) methodology.

Third, although LED places a heavy emphasis on participatory processes, the field has little in the way of guidance on good practice when it comes to how development agencies should intervene, particularly with respect to support for local initiatives identified as a result of participatory planning processes.

Fourth, the shift towards public-private partnership recognises that the private sector is a key source of economic growth and jobs, and has begun to address LED's historic imbalance towards the public sector. However this shift presents LED with a number of new challenges:

- LED's participatory approaches tend to have been geared to the structures and practices of the public sector, which are not suited to the more dynamic private sector. Typically, the private sector is not keen on being involved in elongated multi-stakeholder discussion and planning process. Furthermore LED processes require formal representative organisations with which to engage; in many locations these are often lacking in a nascent private sector.
- LED is a geographic approach; it struggles to deal with a world which is increasingly non-geographically delineated, for example in terms of the way in which the private sector organises itself (eg value chains) or the economic effects of globalisation.
- Participation alone is not a sufficient basis for developing understanding and guiding effective intervention. It is recognised that better tools for analysis are needed.<sup>P</sup>

Fifth, there are some debates about the future of LED. Typically there have been two main forms of LED. At one extreme there has been generic location policy and intervention, aimed at creating favourable conditions for business in general, without targeting specific companies or sectors. At the other extreme there has been strategic spatial policy and intervention, aimed at upgrading and innovation in specific businesses or industries (eg clusters). Some observers suggest that the future of LED lies in a middle way, reflexive spatial policy and intervention, which aims at enabling local institutions to deal more effectively with dynamic uncertainty, based on collective reflection, rather than joint strategies and action (which are perhaps better pursued by individual stakeholders according to their interests and competencies).

## 2.5.5 Overview of LED

Poverty rationale / world view	Framework for analysis	Guidance for intervention
<p><b>Limited poverty rationale</b></p> <p>At its core, LED has no world view on poverty reduction. However, LED is premised on objectives for growth and employment creation in disadvantaged areas.</p> <p>LED increasingly recognises the need for policy and intervention coherence in relation to a wider systemic context. However ultimately, LED does not ask where the poor are located within this system; how they can do better; and what the role of development agencies is in improving their positioning.</p>	<p><b>Incorporating more systemic focus</b></p> <p>Lacking theoretical and conceptual underpinnings, LED does not have an overarching framework for analysis. LED does have geo-political mapping / stakeholder tools.</p> <p>Typically LED draws on analytical tools from other fields (eg VCA). The risk is that these tools are employed in isolation, outside an common framework for analysis and action.</p> <p>However there are some efforts to develop a conceptual framework for LED (eg Mesopartner's 6 Triangles)</p>	<p><b>Strong on participation, weak on intervention</b></p> <p>There are such a multitude of LED approaches, it is hard to discern what is a typical intervention.</p> <p>LED's distinctive contribution is its emphasis on engagement with local stakeholders and participatory processes.</p> <p>It is recognised to lack guiding "how to" principles for intervention, with the risk that agencies are frequently drawn into funding long "shopping lists" that emerge from participatory processes.</p>

### KEY RESOURCES

#### Physical resources:

- Porter, M. "The competitive advantage of nations"

#### Web based resources:

- [www.worldbank.org](http://www.worldbank.org)
- [www.mesopartner.com/](http://www.mesopartner.com/)
- [www.qtz.org](http://www.qtz.org)
- [www.microlinks.org/](http://www.microlinks.org/)

## 2.6 Summary

It is clear that none of these individual fields taken in isolation represent a complete framework for private sector development practitioners (see summary table overleaf). In general terms we find that:

- Their rationale often fails to make an explicit link to poverty reduction
- As frameworks for understanding they provide a partial view of the market system for private sector development, typically focusing on specific elements of the system. In some cases they tend to be descriptive or identify symptoms of problems rather than the root causes of problems.
- Although some may offer technical tools to practitioners, few provide clear guidance about the role of development agency intervention in private sector development.

It is in relation to these three gaps that emerging thinking and practice on making markets work for the poor can contribute.

## Summary of main private sector development fields

	World view / poverty rationale	Framework for understanding system	Guidance for intervention
Value chain analysis	<p><b>Increasingly defining a poverty rationale</b></p> <ul style="list-style-type: none"> <li>• Small firms are part of value chains; scope for growth depends on their position within chain</li> <li>• Understanding organisation and dynamics of value chains is key to upgrade firms and foster growth</li> <li>• Limited view on how value chain development leads to poverty reduction</li> <li>• But, more explicit macro poverty focus is emerging and increasingly used to understand micro aspects of poverty</li> </ul>	<p><b>Strong, but narrow systemic focus, but improving</b></p> <ul style="list-style-type: none"> <li>• Strong framework to analyse VC but partially systemic</li> <li>• Emerging VCF expands analytical framework with inter-related (service) markets and wider enabling environment</li> <li>• Application most suited to product and commodity markets. Reduced applications for service or factor markets or public services</li> </ul>	<p><b>Strong guidance for analysis, weak for intervention</b></p> <ul style="list-style-type: none"> <li>• No guidelines for good development intervention practice</li> <li>• The concept of firm upgrading does not say how it should be brought about in practice</li> <li>• Interventions tend to fix constraints directly; short term impact, but sustainability is a concern</li> </ul>
Subsector analysis	<p><b>No explicit poverty rationale</b></p> <ul style="list-style-type: none"> <li>• Small firms are important for growth and employment</li> <li>• Understanding wider systemic context improves effectiveness of interventions, that leads to growth</li> <li>• No explicit view on how subsector development leads to poverty reduction</li> </ul>	<p><b>Systemic underpinnings, strong, narrow application</b></p> <ul style="list-style-type: none"> <li>• Strong framework to analyse sectors</li> <li>• Practical application tends to be narrow, neglecting underpinning systemic theory, excluding influences from services and institutional factors</li> <li>• Application most suited to product and commodity markets, rather than service or factor markets or public services</li> </ul>	<p><b>Strong guidance for analysis, weak for intervention</b></p> <ul style="list-style-type: none"> <li>• No common guidelines for good intervention practice</li> <li>• Interventions tend to fix constraints directly; short term impact, but sustainability is a concern</li> </ul>
Clusters and networks	<p><b>No explicit poverty rationale</b></p> <ul style="list-style-type: none"> <li>• Small firms are important for growth and employment</li> <li>• Cooperation increases efficiency, which leads to competitiveness and contributes to growth</li> <li>• No explicit view on how cluster growth leads to poverty reduction</li> </ul>	<p><b>Narrow systemic focus</b></p> <ul style="list-style-type: none"> <li>• Strong framework to identify existing clusters and basic dynamics</li> <li>• Analysis tends to be generated through intervention process itself</li> <li>• Often draws on other methodologies like VCA</li> <li>• Tendency to describe clusters, and symptoms of problems rather than root causes</li> <li>• Mainly applied in manufacturing industries</li> </ul>	<p><b>Strong on operational aspects, weak otherwise</b></p> <ul style="list-style-type: none"> <li>• Emphasis of guidance tends to be operational, with many manuals on cluster management, rather</li> <li>• Sustainability concerns</li> </ul>
Enabling environment	<p><b>Limited poverty rationale</b></p> <ul style="list-style-type: none"> <li>• Firms need enabling environment for growth</li> <li>• Belief that growth is good for poverty reduction</li> <li>• But as a catch-all concept cannot does not have a cohesive world view on poverty reduction</li> </ul>	<p><b>Narrow systemic focus</b></p> <ul style="list-style-type: none"> <li>• No common framework for understanding</li> <li>• Partly systemic, but narrow focus on policy, legal and regulatory reforms</li> </ul>	<p><b>Weak guidance for intervention</b></p> <ul style="list-style-type: none"> <li>• Some principles of good practice exist but no "how to" guidance for practitioners</li> <li>• Interventions tend to either get directly involved in bringing about change (with resultant sustainability problems) or alternatively are very hands-off, eg research/studies</li> </ul>
Local economic development	<p><b>Limited poverty rationale</b></p> <ul style="list-style-type: none"> <li>• Disadvantaged areas need firm growth and employment</li> <li>• Increasingly systemic in its recognition of need for policy and intervention coherence in relation to wider systemic context</li> <li>• No explicit view on how local economic growth contributes to poverty reduction</li> </ul>	<p><b>Incorporating more systemic focus</b></p> <ul style="list-style-type: none"> <li>• Narrow, geo-political mapping / stakeholder tools</li> <li>• Draws often on other methodologies like VCA</li> <li>• Overall framework for understanding is lacking</li> <li>• But, recent efforts aim to develop a conceptual framework for LED</li> </ul>	<p><b>Strong guidance for participative processes, weak for intervention</b></p> <ul style="list-style-type: none"> <li>• Multitude of approaches, most tend to be strong on engagement with stakeholders and participatory processes</li> <li>• Lack of "how to" guidance for actual intervention</li> <li>• Process often result in "shopping" list of local interests which agencies struggle to deal with</li> </ul>

### 3. WHERE DOES MAKING MARKETS WORK FOR THE POOR FIT IN?

#### 3.1 What is making markets work for the poor?

The terms *making markets work for the poor* (MMW4P, M4P, or MMW) and *market development* have emerged over the past six years. The origins of MMW are diverse, but essentially emerge from the real world experiences of numerous development agencies. This experience has been characterised by recognition that many interventions have not succeeded in producing sustainable outcomes which have incorporated the poor within the economic mainstream, instead often perpetuating their exclusion, vulnerability and dependency. They have failed to make markets work for the poor.

The main causes of these problems were seen to be (a) a failure to understand market systems and where the poor fit in to them and (b) inappropriate interventions, which actually distorted and displaced indigenous market mechanisms and institutions, rather than promoting local incentives and ownership and hence sustainability. In parallel with this experience many agencies are increasingly aware of the limits of donor funds and are exploring partnerships with the corporate sector. Moreover, observations beyond the world of development demonstrate significant impacts on poverty through changes in market systems that are appropriate for the poor.

MMW has therefore emerged from hard-won experience, but it is not a precise science or rigid methodology. Its key features include:

- A starting point which recognises that the poor exist within wider market systems and that the objective of development interventions is to stimulate those market systems to work more equitably for disadvantaged groups.
- A sound understanding of market systems as the basis for all interventions; why they don't currently work for the poor and how they might work more effectively in the future. *Market systems* is understood as a more realistic and nuanced picture of markets than that of classical economics' emphasis on spot transactions between private actors.
- An explicit commitment to sustainability, which focuses on stimulating and aligning the incentives and capacity of local institutions so that they play more effective roles in market systems.
- An explicitly temporary, finite role for development agencies, where they do not perform market roles directly, but try to facilitate indigenous market actors to play more effective roles in market systems.
- Intervention approaches which are sensitive to local market conditions and appropriate for objectives of sustainability.

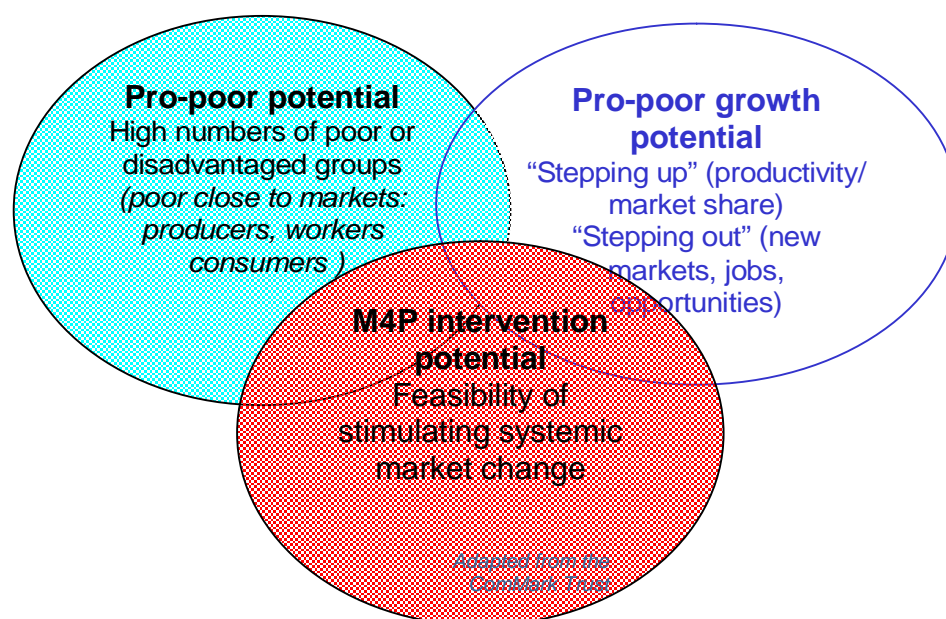
In simple terms MMW can be seen as comprising three elements which can add value to the private sector concepts and approaches discussed above:

- A world view or rationale for thinking about poverty reduction.
- A framework for understanding the market systems in which the poor exist.
- Guidance for intervention practices.

It is important to recognise that MMW is not a substitute for these concepts and approaches; indeed it has grown out of some of their experiences. The three elements of MMW are overarching; they help us position different concepts and approaches into a bigger picture; they help use different concepts and approaches to better understand the poor in market systems; and they help us determine our role as development agencies.

### 3.2 MMW as a world view or rationale for poverty reduction

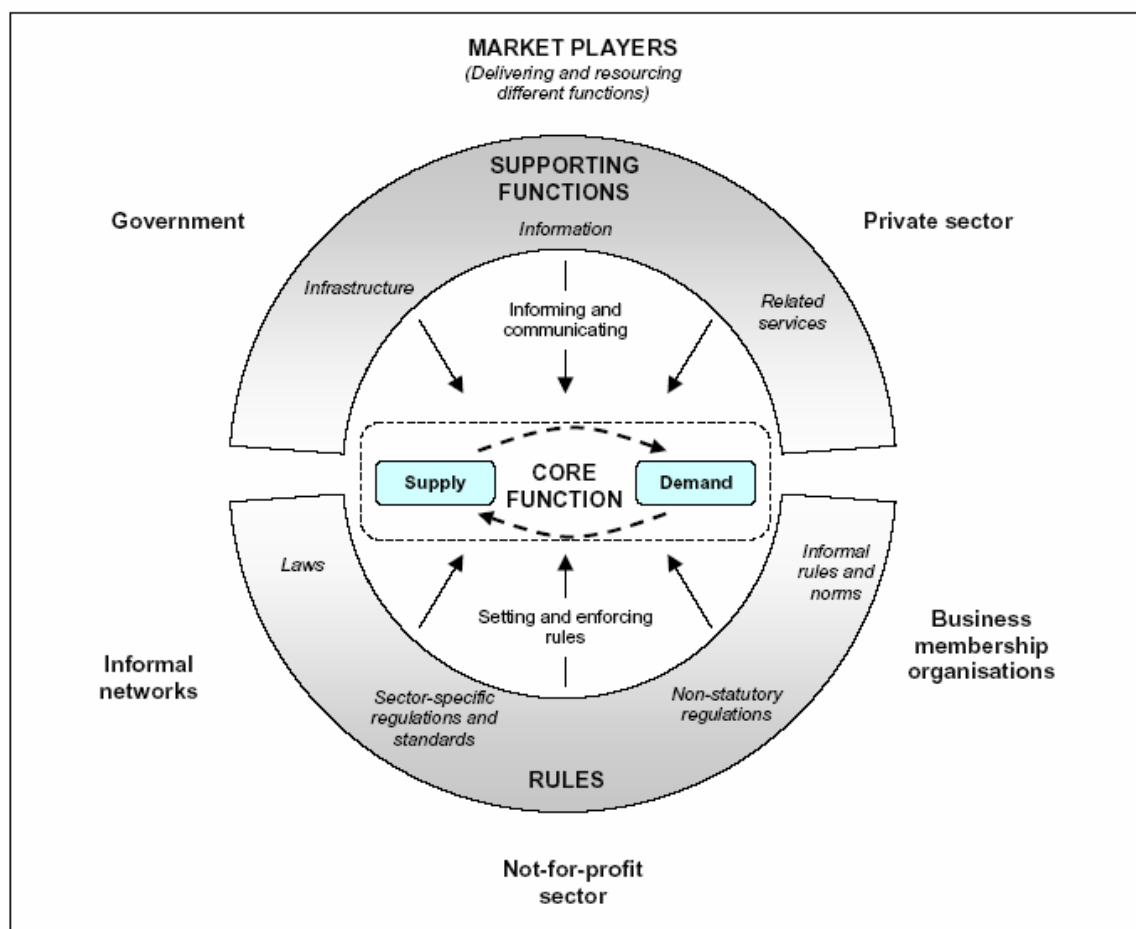
The starting point for MMW interventions is poverty reduction. In simple terms this is defined by three questions: where are there significant numbers of disadvantaged groups (be that as producers, workers or consumers)?; are there untapped opportunities for those groups which could see them incorporated more equitably in the economic mainstream?; and is it feasible to stimulate systemic change that will bring about this incorporation on a sustainable basis?



### 3.3 MMW as a framework for understanding pro-poor market systems

MMW goes beyond the views of conventional economics of markets as spot transactions between many buyers and sellers. It recognises in the real world that it is a more complex range of structures and institutional arrangements that make markets work. These are not only private but public in nature; therefore assessments of sustainability should also apply to public actors as well as private actors. MMW is distinctive in that it explicitly distinguishes between function financed by indigenous governments and the public financing of international aid.

MMW recognises that the composition and structure of specific market system will vary enormously from context to context; different exogenous influences, different distributions of players and roles, different markets and different collections of individuals and interests. Understanding these dynamics – the structure of the market system – is critical for guiding effective intervention and positive change. MMW provides a framework for just such analysis and intervention action. This framework is shown below.



**The core:** Businesses operate in a market system for inputs and outputs (land, labour, raw materials, capital, services etc). Conventionally, markets are seen as having one **core** function, delivery and consumption of a good or service, the structure or organisation of which is usually described in terms of a specific *value chain*, *sub-sector* or *cluster*. However markets do not function solely as a result of supply and demand of goods and services; they are governed by formal and informal **rules** and underpinned by a range of **supporting functions** which determine behaviour and practices, shape relationships, generate and provide information, knowledge and incentives. Within this environment a diverse range of public and private, formal and informal **players** may be active.

**Rules:** formal or informal rules act to shape market outcomes and govern or control the entry, exit, operations and behaviour of business. Rules typically provide the foundations for other more direct interfaces with business. For example with respect to the *enabling environment* field a specific *policy, law or regulation* may initiate and determine the nature of specific public service delivery or other public action. Rules include informal rules or norms, formal rules or laws and other standards and codes of practice.

**Supporting functions:** a range of other functions, together with rules, determine and support the way in which a specific market system works. Supporting functions, as their name implies, support the core functions of a market, and also the ways in which rules are formulated, applied, interpreted and enforced. Supporting functions might be seen to include: policy analysis, consultation and formulation processes; infrastructure; research and development (R&D); information; development and maintenance of factor quality and broad-based access to factors; representation and

mediation; co-ordination; and other specialised functions and services. These functions correspond to the focus of *enabling environment*, *local economic development* and *clusters*, in particular.

MMW recognises that rules and supporting functions overlap and are inextricably linked. For example, if value-added tax is to be introduced or a specific regulation revised, this will be only successful if processes for analysis and consultation, formulation and implementation are effective. Appropriate information that signals changes and the resultant business implications need to be disseminated through relevant channels to the target population. Mechanisms and services need to be in place to enable businesses to interpret changes in circumstances, comply with new requirements or seek mediation or redress in the event of difficulties.

**Players:** In addition to the core supply and demand-side players who provide and consume a specific good or service, there are clearly many other players involved in markets. Any market system consists of a diverse range of public and private players: government, the commercial private sector, non-profit organisations such as universities and think tanks, business representation organisations, not to mention a range of other informal networks and alliances. Understanding the presence, capacity and roles of different market player is vital to any intervention in the business environment. A geo-political dimension (as per *LED*) further complicates this diversity. Government in particular, (but not exclusively, chambers of commerce, for example), usually organises itself along geographic or political lines, at national, regional and district levels. Therefore understanding the structure and spatial arrangement of key players is also important in enabling environment work.

Clearly, one implication of using this framework is that to effectively consider a specific market system it is imperative to consider the inter-relation of a range of different elements.

It is this multi-dimensional, multiple player system that we must consider when we refer to the market system and necessities a broad understanding of a diversity of different functions and players and the roles that they play, in a specific context.

This is the essence of MMW: a good systemic understanding of a specific market system, which not only identifies problems but the sources and potential solutions to those problems and which shapes the nature of subsequent agency intervention.

### 3.4 MMW as guidance for intervention

Development interventions are always about some form of subsidy, in the sense that they are publicly financed. Internationally-funded development interventions receive public finance of some form or other, on a temporary basis, to bring about developmental outcomes in a recipient country. MMW interventions are no different. The key questions MMW poses are: what are the objectives of subsidies?; where are they directed?; and how are they applied?

MMW advocates considerable caution in the application of financial resources directly into local market systems, be that for the financing of public or private roles. In practice MMW interventions utilises more sensitive and indirect approaches, aimed at influencing and leveraging market actors. This is the essence of so-called facilitation.

An MMW intervention will appraise intervention activities in the context of its understanding of the market system in question:



- Do intervention activities relate to a potential market function in the future?
- If so, are there appropriate local actors who might have an interest in performing this function in the future?
- If so, what kind of relationship do we need to have with them to ensure that they are encouraged to focus on the performance of the function?
- What kind of support is needed to be consistent with that relationship and the future performance of that function?
- Is our intervention leaving the door open for *crowding in* of other actors, or are we conferring an unfair advantage to specific actors?

### 3.5 How does MMW help us think about other fields of private sector development?

The three elements of the MMW can help us position the various private sector development fields in relation to their orientation towards poverty reduction; how they contribute to building up our understanding of where the poor fit – or could fit – into the wider economic system; and the guidance they provide for intervention.

#### 3.5.1 Poverty rationale

As noted above, the starting point for MMW is poverty reduction: how market systems can work better for poor people. This need not be direct – it may relate to the poor as producers, labourers, consumers or citizens – but it needs to be explicit.

The table below looks at the various fields in relation to a poverty rationale; the conventional perspective and what an MMW interpretation would be.

PSD field	Conventional	MMW
<i>Value chain analysis</i>	Increasingly defining a poverty rationale	Selects VC in terms of their relevance to the poor. Some influence on VC thinking (and vice versa)
<i>Subsector analysis</i>	No explicit poverty rationale	As above. MMW partly responsible for revival of SSA
<i>Clusters and networking</i>	No explicit poverty rationale	As above. Inter-connected markets central to MMW approach
<i>Enabling environment</i>	Limited poverty rationale	EE constraints in terms of barriers to poor's participation in specific market systems. MMW sees EE as part of market system
<i>Local economic development</i>	Limited poverty rationale	Selects areas in terms of distribution of pro-poor potential and seeks to address barriers at appropriate level

#### 3.5.2 Framework for analysis and understanding

MMW places great emphasis on understanding the system in which the poor are located, the root cause of constraints that they face (rather than the symptoms of the problem) and ways in which the system might be changed to benefit them.

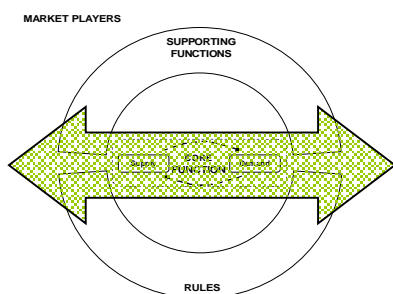
The table below looks at the various fields in relation to their level of systemic understanding; again in terms of a conventional perspective and what an MMW interpretation would be. Below the table, the market system diagram has been

adapted to illustrate, in general terms, where the various fields provide insight or focus in relation to the market system as a whole.

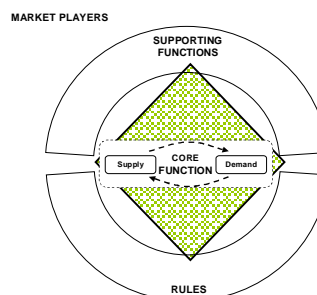
PSD field	Conventional	MMW
<b>Value chain analysis</b>	Strong, but narrow systemic focus, but improving	VC is at core of market system and can include other functions close to core market.. Broader MMW elements now incorporated in emerging VCF. <b><u>See figure A below.</u></b>
<b>Subsector analysis</b>	Systemic underpinnings, strong, narrow application	SS at core of market system. MMW is close to original SSA underpinning theory. Similar to VC. <b><u>See figure A below.</u></b>
<b>Clusters and networking</b>	Narrow systemic focus	Clusters correlate to MMW's relationship between core and supporting functions, and inter-connected markets but less comprehensive. <b><u>See figure B below.</u></b>
<b>Enabling environment</b>	Narrow systemic focus	Correlates to MMW rules and perhaps some supporting functions. MMW is increasingly appearing in EE literature as emerging approach to analysis and intervention design for institutional framework and capacity initiatives. <b><u>See figure C below.</u></b>
<b>Local economic development</b>	Incorporating more systemic focus	Correlates to MMW rules and support services though specific to core function in geographical setting, not wider market system. MMW analysis framework being adopted by LED practitioners. <b><u>See figure D below.</u></b>

**Graphic representation of where PSD Fields fit within the MMW Framework**

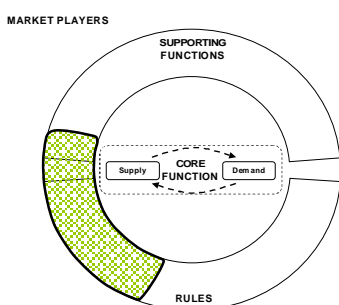
**A: Value chains and Sub-sectors**



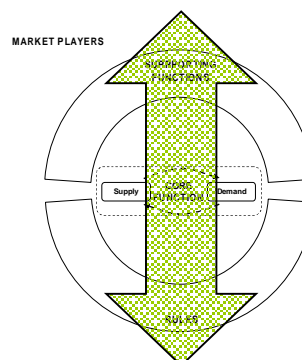
**B: Clusters and Networks**



**C: Enabling environment**



**D: Local economic development**



### 3.5.3 Guidance for intervention

MMW recognises that how agencies intervene is critical to bringing about sustainable pro-poor market outcomes in a market system. The table below assesses the extent to which the various fields provide guidance for intervention, again presenting a conventional view and a market development interpretation.

<b>PSD field</b>	<b>Conventional</b>	<b>MMW</b>
<b><i>Value chain analysis</i></b>	Strong guidance for analysis, weak for intervention	Facilitative approaches eg for stimulating supporting functions can help overcome upgrading sustainability problems
<b><i>Subsector analysis</i></b>	Strong guidance for analysis, weak for intervention	
<b><i>Clusters and networking</i></b>	Strong on operational aspects, weak otherwise	Sensitive approaches to incentive and institutions can help ensure sustainability of cluster manager /network broker
<b><i>Enabling environment</i></b>	Weak guidance for intervention	MMW is increasingly appearing in enabling environment literature as an emerging approach to analysis and intervention design for institutional framework and capacity initiatives
<b><i>Local economic development</i></b>	Strong guidance for participative processes, weak for intervention	MMW approaches to private sector engagement address current gaps in LED approaches

## 4. IMPLICATIONS FOR SDC / E&I

As a driver of growth, the critical contribution of the private sector to poverty reduction is increasingly being recognised. Private sector development therefore is becoming more central to poverty reduction strategies. As its importance increases, development agencies are increasingly reviewing the extent to which their approaches to private sector development are consistent with achieving strategic and systemic impact on poverty reduction.

This paper has considered five established approaches to private sector development. Each approach represents an important instrument for SDC programming. E&I's concern, as a thematic division of SDC, is that the developmental utility derived from working with any of these approaches is maximised. In support of this end, this paper attempts to clarify what these approaches are, what they offer, and where their limitations lie – either in theory or in practical application.

This paper is neither definitive nor exhaustive in its examination. It acknowledges wide deviations in how approaches are defined, perceived and in particular how they are applied. However, it is precisely because of these wide deviations in definition, understanding and application that “benchmarking” of different approaches, such as attempted in this paper, is so important if clarity and consistency are to be ensured.

This paper benchmarks the various approaches to private sector development against a market development framework. It does this for two principal reasons. Firstly, a common framework was required, and the market development framework is gaining increasing relevance with development agencies. Secondly, it is important to establish the relationship between MMW and common approaches to private sector development.

A number of implications arise from this benchmarking of approaches to private sector development. All of these implications are relevant to E&I. Some of these implications have wider relevance to development agencies in general.

### 4.1 Objectives first, approach second

As with other development agencies, SDC is concerned to ensure that its work contributes to achieving the Millennium Development Goals (MDGs). This demands that interventions are guided by a clear and coherent poverty reduction rationale. As shown in this paper all of the approaches are essentially value free. A defining poverty reduction rationale that guides the use of any of the approaches is not explicit. Value chains and sub-sector approaches talk of upgrading for improved competitiveness and growth. But, they do not demand any analysis of how the poor are to participate in any upgrading. Enabling environment reform talks of removing obstacles to “doing” business. However, it often neglects to demonstrate clear links to the performance of poor entrepreneurs.

Poverty reduction as an objective is at the heart of MMW. As such, an MMW framework can ensure the consistency of various approaches to the objective of poverty reduction. MMW can therefore add value to private sector development approaches through ensuring that poverty reduction objectives are set at the heart of any approach.

For example, it can support transparent decision-making when choosing which value chain, or sub-sector an intervention might choose. It would ask which sectors are important for large numbers of poor people, that have economic potential, and where intervention is feasible. Furthermore, applying MMW thinking would set the objectives for upgrading within value chains or sub-sectors in terms of improved participation of the poor.

Establishing such explicit poverty-focused objectives might not effect which approach is chosen, but it will certainly strongly influence the way in which any approach is implemented.

## **4.2 No single approach is comprehensive**

This paper has examined the various approaches in terms of what they offer in respect of:

- A poverty rationale;
- A framework for understanding; and
- Guidance on intervention actions.

These three factors are at the heart of ensuring good development practice. They must be linked and they must be coherent. A clear poverty rationale defines what any intervention should try to understand, and ensures that intervention practice is consistent with both analysis and objectives.

This paper shows the relative strengths and weaknesses of each approach in terms of these three factors. Whilst each has their own strengths and weaknesses, no approach is comprehensive. Applying any approach within a market development framework can help to fill the gaps, thereby ensuring greater coherence, consistency in application and therefore overall effectiveness of the approach.

## **4.3 Approaches are not mutually exclusive**

Applying a market development framework can ensure that approaches are deployed against clearly identified objectives and analysis. Furthermore through understanding what each approach can deliver, and what it cannot, applying an MMW approach in practice can ensure the right approach or combination of approaches are used for the right reason at the right time. One singular approach might be dominant, but need not be exclusive.

For example, a local economic development approach might well be a strong model for multi-stakeholder partnerships and joint actions. However, it might also benefit from the type of information provided through a value chain or sub-sector analysis – that understands market dynamics beyond administrative boundaries.

Similarly, as a vehicle for promoting thematic coherence, MMW can support the application of approaches considered in this paper to enhance work in the fields of financial sector development and skills development. For example, the application of value chain analysis within an MMW framework might shed light on specific sectoral constraints to financial access and skills development by the poor and thereby lead to more focused engagement in these respective fields. Certainly an MMW framework will provide guidance on intervention principles to all fields related to private sector development.

Understanding what each approach can achieve, and what it cannot achieve is critically important in managing expectations and improving practice. There is currently little consensus in development circles, with different agencies often promoting its approach of choice as dominant over others. Replacing this rather adversarial competition with a commitment to clarity and openness is vital for learning and progress.

#### **4.4 Direct implications for E&I**

In light of the above general implications, a number of specific areas of attention emerge for E&I:

##### Improving practice in SDC programmes, through:

- Promoting learning using benchmarking exercises, as conducted in the Balkans;
- Preparing case studies and papers that show clearly how MMW can add value to approaches (such as the Katalyst vegetable sector case study);
- Engaging in community of practice (COP) discussions to crystallise the uses and limitations of approaches, and how MMW-style thinking can enhance their application. As in the recent value chain COP, MMW can provide a useful framework for the conduct of these discussions;
- Showing more tangibly how MMW is a way of adding value to established private sector development approaches, rather than a competing approach.

##### Improving practice of development agencies more widely, through

- Influencing wider development thinking and practices by channelling experience and learning that has been generated into wider development fora, for example, via the value chains working group of the Donor Committee.

---

## REFERENCES

- A Porter, M. (1990); *The Competitive Advantage of Nations*, Free Press, New York
- B Kaplinsky, R and M Morris (2001); *A Handbook for Value Chain Research*, prepared for the IDRC
- C Wood, A. (2001) *Value chains – An Economist’s Perspective*, in IDS Bulletin, Vol. 32, No. 3
- D Boomgard, J. et al. (1986); *Subsector analysis: its nature, conduct and potential contribution to small enterprise development*, MSU International Working Paper No 26
- E *Ibid.* p.9
- F Humphrey, J. and H. Schmitz (1995); *Principles for promoting clusters & networks of SMEs*, Small and Medium Enterprise Branch, UNIDO
- G European Commission (2003); *Final report on the expert group on enterprise clusters and networks*, p16.
- H White, S. and P. Fortune (2005); *Review of DFID activities in the enabling environment*, DFID
- I *Ibid.*
- J Beck, T. et al. (2003); *Small and medium enterprises, growth and poverty: cross-country evidence*, World Bank
- K White, S. and J. Chacaltana (2002); *Donor experiences in supporting reforms in the business environment*, Donor Committee for Small Enterprise Development
- L World Bank (2003); *Local Economic Development: a quick reference*. Urban Development Unit of the World Bank
- M Meyer-Stamer, J. (2003); *The Hexagon of Local Economic Development and LED in South Africa*, Mesopartner
- N Porter, M. (1995); *The competitive advantage of the inner city*, Harvard Business Review. Vol. 73, No. 3, pp 55-71
- O Meyer-Stamer, J. (2003); *Why is Local Economic Development so difficult, and what can we do to make it more effective?*, Mesopartner
- P Meyer-Stamer, J. (2005); *How do “Enabling Environment” and “Making Markets Work for the Poor” relate to LED and PACA?*, Editorial, PACA News, No. 9, December