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Useful principles for adopting a market development approach for enterprise development organizations

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Abstract

Purpose – To provide a practitioner focused discussion for enterprise development organizations (EDOs) who are seeking to incorporate principles of sustainability into their strategies.

Design/methodology/approach – Presents general principles that can be useful to EDOs who are trying to take on a more market development (sustainable) approach to enterprise development.

Findings – The principles can be applied to economic development projects that target small, medium or large enterprises. They apply to programs promoting agricultural, manufacturing, and services – and also have application in other sectors such as health, conservation, and education.

Originality/value – Provides leading insights into EDO strategies.

Keywords Business development, Sustainable development, Value chain

Paper type Viewpoint

Introduction

The following is a presentation of general principles that can be useful to enterprise development organizations (EDOs) who are trying to take on a more market development (sustainable) approach[1] to enterprise development. The principles can be applied to economic development projects that target small, medium or large enterprises. They apply to programs promoting agricultural, manufacturing, and services – and also have application in other sectors such as health, conservation, and education.

Develop a positive attitude towards the private sector

In order for market development programs to be successful, the "facilitators"[2] of these programs need to develop a positive attitude towards the role of the private sector in economic development. They need to recognize that all market actors (producers, traders, processors, input suppliers, etc.) play an important role and they need to become comfortable with the principle that these actors need to make a profit in order for their activity to survive.

It is also important to recognize that the motivation of many market actors (including larger firms and intermediaries) goes beyond just making money. Businesses need to make a profit as described above, but many take personal pride in their work and the impact it has on their local communities and their country's economy. Developing a mindset that respects the role of all market actors is very important in promoting "win-win" relationships[3] in targeted markets. If EDO staff can develop this attitude then their ability to partner with lead firms to bring increased benefits to MSE/poor will improve.

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Along the same lines, EDOs should not see their role in market development programs as "protecting the poor." This reinforces the view held by some that "all private sector businesses are intent on exploiting the poor." While there are examples of monopolistic and exploitative behavior, there are many more examples of close collaboration and positive inter-firm relationships among market actors. In many cases one sees that the most successful lead firms (buyers, processors, input suppliers, etc.) are those that foster positive relationships with the MSEs they buy from or sell to.

In order for EDO staff to identify opportunities to build and strengthen such relationships they need to look at product value chains as a "team effort" that involves all of the market players (including producers who are themselves part of the private sector) – each one playing an important role. EDO programs need to focus on:

- how to increase and improve the participation of MSE/poor in those markets; and
- how to help lead firms[4] understand how better to structure their relationships with producers[5] they source from or sell to (including how to create positive incentives for them).

Once interventions[6] have begun, projects can monitor activities to determine whether or not benefits are actually accruing to MSEs/poor via these relationships.

Impact through indirect interventions

One of the lessons of market approaches is that it is not always necessary to intervene directly with the poor to bring them benefits. Greater impact can sometimes be achieved indirectly by working with other market players. The reasons for this include the high cost of interacting directly with large numbers of small-scale enterprise and the lack of sustainability of this kind of intervention. Examples of activities that can create large-scale and sustainable benefits for the poor without intervening directly with the MSE/poor include:

- assisting an agribusiness firm to structure mutually beneficial contract farming (procurement operations) with small-scale producers;
- working with traders to develop new marketplaces closer to targeted communities – where they can provide market access and market information to producers; and
- addressing policy constraints to create incentives for MSE/poor (such as advocating for correct enforcement of land leasing policy).

In all of these examples, the objective of the project is to impact the poor – it is the indirect method employed that differs from more traditional approaches. The challenge in all these cases is to identify win-win relationships where all parties benefit. In this way, the relationships and corresponding benefits to both parties will continue once the project activities end. It is important, however, to carefully select the private sector companies that the project will work with – to insure that they are capable of creating win-win partnerships with the MSEs.

Avoid market distortions

Market distortions frequently occur when development programs intervene directly in markets without building upon or taking account of the existing market players.

There are examples of EDOs that have used donor funds to take a direct commercial role in industries such as crafts and poultry. These programs frequently sell inputs and/or purchase and market final products. Their interventions are frequently justified by stories of unfair intermediaries, etc. While well intentioned, they oftentimes have a negative effect on private entrepreneurs who are trying to fulfill these functions in a commercially viable manner. These entrepreneurs find it difficult to compete with NGOs or others who are subsidized by donors and who don't need to fully rely on commercial sources of revenue.

Such programs can push existing entrepreneurs out of business and create problems for the MSE/poor if their subsidy of market operations ceases at some point due to lack of donor funds. As they do not need to depend as much on market forces to survive, these NGOs also tend to be less "demand driven." Their products and services frequently reflect more of what the NGO managers think is appropriate versus what the market demands.

A market development approach will always take a look at the larger "market systems"[7] to understand who the existing market players are and what function they play in the value chain. They then try to work with these existing players (or encourage the emergence of new players if there are no existing ones) to address the "systemic constraints"[8] facing the targeted market and participating MSE/poor. Expressed in another way, they try to identify existing market players that can provide sustainable market-based solutions[9] to the constraints that are holding back industry competitiveness and increased benefits to MSEs.

Revisit the role of middlemen

One of the commonly held views around the world is that middlemen (or women) are the source of low prices, inefficient value chains, and exploitative behavior towards the MSE/poor. The automatic reaction of many projects therefore is to try and "eliminate the middlemen." Middlemen or "intermediaries" play an important role in product markets. They provide links to markets, help to consolidate production, provide transportation, and sometimes provide inputs, technical assistance, finance or other services to the MSEs they source from. They also take risks in buying products, stocking them, and finding buyers who will accept the product. These are usually tasks that individual MSEs cannot, or do not want to undertake on their own. They can also be complicated tasks that go beyond the ability of groups or cooperatives to successfully manage.

It is frequently stated that the price paid by intermediaries to MSEs is very low compared to the price they receive when they sell. This is, therefore, interpreted as exploitative behavior. Before making assumptions, however, that margins are unduly high or unfair, it is important to investigate the costs of intermediation. These costs include transportation, storage, pre-financing, and personnel, not to mention a salary for the intermediary himself/herself. Intermediaries are also taking risks – they may enjoy a good margin one day and make a loss another. Once all of these factors are taken into consideration it is frequently the case that the cause of high margins and low prices is more due to market inefficiencies such as poor roads, long distances between farms and markets, lack of adequate storage and transportation facilities, fees paid to officials, etc. – and not so much the intermediaries themselves. Such an investigation also uncovers the challenges that intermediaries face themselves – and could result in a new found respect for the role that they play. To conclude, instead of trying to eliminate middlemen a more effective approach in market development programs can be to explore how to work with both intermediaries and producers to reduce the inefficiencies that are causing low prices.

Promote smart subsidies

One of the principles of market development programs is the use of "smart subsidies" to promote sustainable solutions that will continue to accrue benefit to targeted sectors and MSE/poor after the development program is complete. Under a market development approach such subsidies are used to fund the activities of "facilitators" (such as EDO staff who are implementing the programs). The activities of facilitators include such things as:

- developing the capacity of private sector "providers"[10] to offer improved products and services to MSEs in a sustainable manner;
- promoting awareness of these products and services among MSEs; and
- contributing to an improved enabling environment.

These activities, or project interventions, do not need to be sustainable themselves. Once they are complete however, they should leave behind sustainable market relationships and improved services and products for MSEs. Instead of funding direct and unsustainable support to the MSE/poor, smart subsidies are used strategically to build the capacity of market players to interact more productively among themselves.

Poverty alleviation through small/medium firms

Poverty alleviation can be affected in different ways. One way is to promote individual economic activities among the very poor. Another is to help foster employment opportunities for the very poor. This latter point can be achieved by targeting more established MSEs as vehicles for employment generation. These MSEs (which might still be considered as "poor") are frequently in a better position to participate in growing value chains than others who are landless, disenfranchised, etc. If they can grow their activities (agricultural production for example) they will need to hire labor. This can then result in employment opportunities for the "very poor." In some cases, impact on poverty can be greater by following this strategy, rather than by insisting that the very poor have their own economic activities, or that they engage in group economic activities (which can be problematic).

Tread lightly in market relationships

In order to ensure sustainability of impact to targeted MSE/poor it is important for projects to avoid being overly prescriptive or heavy handed in determining what the structure of market relationships should be, what activities to engage in, etc. Some EDO programs try to prescribe what the relationships between market actors should look like without conferring with the market actors themselves. This usually does not work as market actors alone understand what is possible and not possible from their own perspectives. It is always preferable therefore to engage the targeted market players (producers, traders, wholesalers, transporters, etc.) in the design of program interventions. They will be the ones responsible for carrying out the market operations and many of them have significant experience which would enable them to quickly determine what might, or might not be, feasible. Engaging the market players in this way also helps encourage ownership and buy-in which is critical to ensuring sustainability.

In general, the MSE/poor and other market players that the EDO engages with should ultimately make their own market decisions. When looking at hypothetical market scenarios EDO staff should always ask private sector actors "why isn't this happening now?" The answers provide a reality check and help ensure that project interventions result in practical solutions that are based on market realities. This approach also builds on existing knowledge, practice and market players in the targeted sectors.

Taking a market instead of group focus

Many EDO initiatives are very "group focused." They target groups, conduct capacity building activities for them (such as how to structure the group, conduct meetings, keep records, etc.), and then look for opportunities to assist them to increase income. These activities sometimes lead to joint marketing or procurement activities that provide economies of scale and modest increases in savings/income to the participants. There are questions, however, as to whether the project costs required to generate these benefits can be justified. In order to find greater, more cost effective opportunities it is important to take a look at markets from a broader perspective. It is important to identify growing product (or service) markets and then to identify all the players in those markets. In many product markets, there are key players or "lead firms" that play a critical role as buyers, input suppliers, etc. Project activities can often partner with such players to bring sustainable benefits to the rural poor. For example, if the poultry sector is growing there might be a lead firms that are providing day-old chicks, feed, even market access to farmers. In another case, there might be a fruit or vegetable processing plant that is looking for suppliers of product. By identifying these market players from the onset, EDOs can introduce them to rural farmers and help the farmers respond to the opportunities they offer. In this case, the project activities are using growth markets and key actors in those markets as a starting point, rather than small farmer groups.

In cases where growth markets can be identified, there are greater opportunities of "expanding the pie"[11] among all market actors, rather than promoting better "sharing of the existing pie." The joint marketing and procurement activities cited earlier are usually an example of "sharing the pie" whereby a group is able to take on some of the functions that were previously provided by other market actors (traders, input suppliers, etc.). By doing this the group members can gain modest benefits, though the cost of taking on the additional functions also needs to be factored in. In the case of a growing market, all market actors can increase their earnings.

Depending on the opportunities at hand, a formal group may or may not be needed to respond to market opportunities. In some cases, farmers may only need to come together to an agreed upon collection point periodically in order to meet with buyers. Or they may only need to come together a few times per year to coordinate bulk purchases of inputs. While these activities may require coordination, they may not require a formalized group with bylaws, officers, etc. It is, therefore, important not to look at group development or group empowerment as an end in itself – but rather as an means to an end in certain (but not all) circumstances.

It is also important to examine the level of coordination or management required of a group in order to respond to different economic opportunities. In general, the less "group management" that is required the greater the chances of success. An example can be seen with "group marketing" activities. In some of these cases, the management requirements of group is minimal. They only need to bring their production to a common collection point at a particular date once price negotiations with traders had been completed by a group representative. The trader then purchases from each group member on an individual basis – conducting grading and then paying the individual. This strategy has been successful because it does not rely on extensive management by the group (which is frequently the downfall of group activities).

Notes

1. Market development approaches refers to strategies that promote market-based and sustainable solutions to the constraints and opportunities facing small enterprises and the value chains they participate in.
2. "Facilitator" refers to enterprise development organizations and their staff who design and implement programs.
3. Refers to situations where both large and small firms (who are engaged in commercial transactions with one another) benefit from their relationship.
4. A "lead firm" in an industry or value chain refers to a company that has extensive forward or backward linkages with other businesses. Examples include large buyers (such as exporters or processing factories) and input supply companies.
5. "Producers" here refers to MSEs who produce goods and sell to others in a value chain. Small-scale farmers are considered as both producers and MSEs.
6. "Interventions" refers to the wide range of activities that development programs undertake to promote economic development.
7. "Market systems" refers to the wide array of businesses in a given industry that buy, sell, or provide services to one another.
8. "Systemic constraints" refer to constraints that are holding back the development of many market actors. An example might be the lack of wood drying facilities that affects the entire wood furniture sector or a government policy that is negatively affecting many businesses.
9. "Sustainable market-based solutions" refers to the provision of training, technical assistance, inputs, finance, etc. from one market actor to another in a commercially viable and sustainable manner.
10. "Providers" here refers to businesses that provide inputs, finance, technical assistance, etc. to MSEs either in a fee-based manner, or as part of their commercial relationships with the MSEs (example of an input supplier that trains MSE producers in the use of the product they are selling them).
11. "Expanding the pie" refers to scenarios where overall economic growth in an area takes place – benefiting all market players. Improving the "sharing of the existing pie" refers to assisting one group of market actors to take on functions currently conducted by another in an attempt to capture more revenue.

About the author

Frank Lusby is a skilled enterprise development professional with 26 years experience in subsector/value chain analysis, program design/implementation and monitoring. Lusby has conducted both long- and short-term assignments throughout Africa, the Caribbean, and Asia.

Since 1992, he has served as Executive Director of Action for Enterprise (AFE). In that capacity, he has helped the organization become a leading authority in value chain-based enterprise development, has provided direct technical support to field activities, and has overseen administrative, market development, and strategic management issues. Prior to AFE, he served as chief of party for a USAID-funded project in West Africa where developed cost effective methodologies for value chain-based interventions in five different industries. Lusby is a frequent speaker/participant in enterprise development forums, working groups, and conferences worldwide. He conducts training workshops and is the author of several publications. He holds an MBA in International Business, a bachelor's degree in Finance, and is fluent in French. Frank Lusby can be contacted at: flusby@actionforenterprise.org