ACDI VOCA
Expanding Opportunities Worldwide

Value Chain Framework

Strengthening Value Chains to Promote Economic Opportunities

Value chains encompass the full range of activities and services required to bring a product or service from its conception to its end use. Value chains include input suppliers, producers, processors and buyers; a range of technical, business and financial service providers; and the final markets into which a product or service is sold, whether local, national, regional or global. Understanding how industries in which MSEs participate can become more competitive requires both systematic and systemic analysis of the factors affecting the performance of the firms in the value chain and the relationships among these firms.

Our work is never finite—we strive to create lasting effects. Fixing on the long-term progress and well-being of our beneficiaries motivates us to achieve true development. And our beneficiaries are our partners, identifying challenges and priorities and working with us to address them.

End Markets

End markets determine the characteristics of the final product or service generated. The demands of the end market drive quality and standards. End buyers are important sources of demand information, learning and benefits that flow down the chain. Analysis of end markets must demonstrate the potential for competitiveness through a combination of three strategies: producing and delivering goods and services more efficiently, differentiating products or services through quality standards and branding, and exploiting new market demand. The value chain approach assesses the opportunities in all possible markets into which products and services flow.

Business Enabling Environment (Local, National and Global)

International trade agreements and standards tremendously affect the constraints to and opportunities for industry growth. They present opportunities for market expansion but can be extremely expensive for firms, especially MSEs, and can easily preclude a developing country from being competitive.

The national policy and regulatory environment is critical to the functioning of markets and enterprises; it should create incentives for private sector growth and involvement in the policy process. Moreover, poor local government operations and poor enforcement of legal and regulatory regimes increase transaction costs and risks, limiting investments in relationships and upgrading. Conversely, conducive local and regional policies can provide opportunities for rapid improvement of the enabling environment.

Inter-firm Cooperation: Vertical Linkages

Cooperation among firms through vertical or horizontal relationships is critical for transferring skills and reducing transaction costs. Vertical linkages are the relationships among firms at different levels of the value chain between input supply and distribution to the final market.

Vertical linkages are critical for moving a product from inception to the market and for transferring benefits, learning and embedded technical, financial and business services from firms up the chain to firms down the chain or vice versa. Mutually beneficial relationships among vertically related firms can improve MSEs' access to new markets, new skills and a wide range of services. They can also reduce market risk by securing future sales and create incentives for the adoption of more value-added functions or activities.

Inter-firm Cooperation: Horizontal Linkages

Horizontal linkages among producers are needed to reduce the transaction costs incurred by exporters or local buyers when working with many small suppliers. Through inter-firm cooperation, such as buying inputs in bulk or meeting large orders, horizontal linkages can help small firms generate economies of scale, which can contribute to their competitiveness and bargaining power.

Horizontal linkages among MSEs can take the form of formal or informal groups, as well as networks that are managed through a third party (e.g., lead firm, broker or trader). Similarly, cooperation among larger firms can be important for creating industry standards, developing marketing campaigns or lobbying.

Supporting Markets

Supporting markets are key to firm-level upgrading and include sector-specific services (e.g., input and equipment providers), financial services, business management services (e.g., auditors and lawyers), and information technology (particularly as it pertains to market information access and dissemination).

Where these services are needed over the long run, they must generally be provided commercially, either by stand-alone service providers or by firms in the value chain. In this latter case, services tend to be embedded as part of an existing market transaction, with the cost of the service included in the mark-up on the transaction. New technologies or technical services can have a substantial effect on the competitiveness of the industry and can even change the dynamics of competition.

Firm-level Upgrading

Firm-level upgrading refers to changes made by firms to improve their competitiveness through product development and improvements in production and marketing techniques or processes. Firm-level upgrading requires access to information, technology and finance. Product development and improvements in production and marketing processes are integral to sustained competitiveness by enabling firms to meet the market's constant demand for innovation.

Power

The wielding of power in relationships between firms in the value chain shapes the incentives that drive behavior and determines which and how much firms benefit from participation in an industry.

Relationships can range from highly dependent, where one party dominates, to balanced, where all parties involved have some power that they can wield. In any given industry, relationships can cover the full range, and these relationships can change depending on shifting market demand.

Learning & Innovation

Learning and innovation are key to creating and sustaining an industry's competitive advantage since upgrading is dependent on knowledge of what the market requires and the potential returns on investments in upgrading. It is essential that learning and innovation flow through the value chain in order to optimize these returns.

The process of acquiring new knowledge or skills is not necessarily straightforward. Learning and innovating in a systemic sense are closely tied to the incentives that encourage or discourage the delivery and absorption of new knowledge or skills, and the types of mechanisms that are in place to affect their transfer.

Benefits

If industries are to maintain their competitiveness, benefits must be sufficient to provide incentives for changes in behavior patterns that entail taking on new risks and adopting innovations.

Benefits are closely related to power relationships and learning. In the context of MSE development, benefits are much broader than just increases in income, although that is an important part of the equation. Benefits can also mean reduced market risk (more stable income) and increased value of assets. Power in value chains typically translates into benefits. The firms able to wield power through branding or access to worldwide suppliers, and those traders in a chain able to control information, can often exact a larger share of benefits from producers and suppliers.