Multi-Year Expert Meeting on

Enterprise Development Policies
and Capacity-building in Science, Technology and Innovation (STI)
(Fourth session)

Geneva, 16-18 January 2012

The importance of linkages for pro-poor SME development

by

Leora Rajak
Founder, Enterpriseroom

This view expressed are those of the author and do not necessarily reflect the views of UNCTAD.
The importance of linkages for pro-poor SME development

Prepared and Presented by
Leora Rajak of Enterpriseroom

UNCTAD Multi-year Expert Meeting
16-18 January 2012
This presentation focuses on using supply chain opportunities and linkages to enable the emergence and growth of successful pro-poor SMEs

- **What constitutes “pro-poor” opportunities?**
  - Development of poor enterprises and entrepreneurs, i.e. SMEs
  - Development of products and services that serve the poor
  - Development of distribution / vendor networks of the poor

- **What kinds of linkages matter?**
  - Public-private sector partnerships (PPPs)
  - Business linkages between procurers (TNCs, MNCs, local corporates, government) and SMEs
  - Partnerships between government and SMEs with enablers and support-providers

- **What effect will creating multi-stakeholder pro-poor networks & linkages have?**
  - New business and employment creation
  - Pro-poor product and service innovation and development
  - Strengthening of local value chains
  - Increased FDI
  - Reduced cost to poor consumers, and improved prices to poor producers
Pro-Poor Development

Stakeholder and Required Linkage Framework

- Government
- Corporate
- Enablers and Support Providers
- SME

Policy and Platform development partnerships
Platform creation & Procurement
Product and Service provision partnerships
BDS & other support
PPP

Policy and Platform development partnerships
Platform creation & Procurement
Product and Service provision partnerships
BDS & other support
PPP
**Stakeholders’ R&R**

Governments must develop and utilise the pro-poor platform

<table>
<thead>
<tr>
<th>Drivers</th>
<th>Key Linkage Requirements from Government in relation to...</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Hopes</strong></td>
<td></td>
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</tbody>
</table>
| + Sustainable SME growth | **PPP creation and support:** Develop and support Public-Private-Partnerships (PPPs) aimed at creating an enabling environment  
  ➢ Develop shared platforms, systems and tools (e.g. Business registration, )  
  ➢ Develop and support corporate/SME linkages, e.g. through shared databases of SMEs, facilitation of linkage programs, etc.  
  ➢ Develop incentive programs (e.g. South Africa’s BEE program, tax breaks, etc.) |
| + Increased FDI |  |
| + Broad-based SME development |  |
| + Poverty relief |  |
| + Commercial funding for SMEs |  |
| + Effective allocation of own skills and funds |  |
| **Fears** |  |
| – SME complexity |  |
| – Lack of commercial viability of SMEs |  |
| – Lack of investor confidence |  |
| – Lack of local value-addition |  |
| – Non-local sourcing |  |
| **SMEs** |  |
| ➢ **Policy development:** Policy frameworks for pro-poor product & service provision & to encourage use of SMEs |  |
| ➢ **Platform creation:** Support coordination of SME training/support program design, quality assurance, etc. |  |
| ➢ **Pro-poor procurement and value chain development:** Improve “SME-Readiness”; develop and procure from SMEs along the public supply chain |  |
| ➢ **Support pro-poor interventions and initiatives** |  |
| ➢ **Leverage and incorporate learnings from experience** |  |

**Market access facilitation and FDI attraction**
## Stakeholders’ R&R

**Corporates must be “SME-Ready” and develop pro-poor products**

<table>
<thead>
<tr>
<th>Drivers</th>
<th>Key Linkage Requirements from Corporates in relation to...</th>
</tr>
</thead>
</table>
| **Hopes** | **PPP creation and support**: Form Public-Private-Partnerships (PPPs) aimed at developing local pro-poor value chains  
- Develop shared platforms, systems and tools (e.g. SME databases)  
- Embrace spirit of, and comply with pro-poor policy & legislative requirements  
**Improve state of “SME-readiness”**:  
- Ensure procurement practices and systems are SME-ready (e.g. Invoicing processes, admin requirements etc.)  
- Develop fair SME evaluation / partnership criteria  
**Investigate and invest in pro-poor opportunities**:  
- Identify and invest in SMEs along supply chain  
- Commit to inclusive practice  
**Support SME development**:  
- Sponsor entrepreneurship programmes  
- Identify work packages for SMEs  
- Identify categories for technical capacity building; facilitate training  
- Provide technical mentors |
<table>
<thead>
<tr>
<th>Hopes</th>
<th>Key support area</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fears</td>
<td></td>
</tr>
</tbody>
</table>
- Managing risk of SME complexity  
- Suffering loss out of compulsory pro-poor spending  
- To waste management time on non-core activities  
**Corporates (MNCs, TNCs, Local corporations)** |  
**Government** |  
**SMEs** |
Example of good PPP outcome:

The Generic Process

1: Develop Pipeline
   - Develop sustainable pipeline of youth seeking employment

2: Receive and Register
   - Develop network of participant reception and registration points

3: Outline Opportunities
   - Develop tools to describe & market opportunities

4: Stream and Vet
   - Develop vetting systems & assign to catalysisation streams

5: Refer to Platform
   - Develop streams, i.e. platform of networks & linkage programs

Platform

Networks for entrepreneurs

Matching

Networks for work seekers / other

6: Monitor and Evaluate

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**Stakeholders’ R&R**

**SMEs must increase their state of “Procurement Readiness”**

<table>
<thead>
<tr>
<th>Drivers</th>
<th>Key Linkage Requirements from SMEs in relation to...</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Hopes</strong> + An enabling environment + Cheap financing without collateral + Access to customers and clients + Subsidised support + Easy-to-use and easy-to-understand legislative requirements + Easy-to-negotiate customer procurement requirements</td>
<td><strong>Comply with required legislation:</strong> ➢ Company registration, taxation etc. ➢ Conditions of employment, environmental legislation, etc. <strong>Provide accurate information to facilitate linkages</strong> <strong>Improve “Procurement-readiness”</strong> ➢ Ensure customer readiness, i.e. Readiness as a supplier to corporates (admin systems, reliability of supply, etc.) ➢ Develop fair SME evaluation / partnership criteria <strong>Identify and develop appropriate products &amp; services</strong> Align choice of business with: a) Their own needs b) Existing opportunities, and c) Market needs and gaps d) Pro-poor opportunities <strong>Acquire required skills and resources</strong> <strong>Leverage, take advantage of, and help to build existing support and linkage networks</strong> ➢ Access and use BDS offerings ➢ Provide information, participate in networks &amp; linkages</td>
</tr>
</tbody>
</table>

**Fears**

- Administrative complexity
- Unrealistic demands (e.g. Degree of formalisation, degree of information provision)
- Allocation of limited management resources to non-operational issues (e.g. Sourcing funding)
Corporate/SME Networks & Linkages

Pro-poor opportunity creation

**Vertical Linkages**
- Market/supplier relationships
- Market opportunities
- Supplier development programmes
- e.g. Corporates (MNCs & local) create initiatives for suppliers

**Horizontal networks**
- Facilitated network of entrepreneurs
- Provision/ linkages to skills, product development, opportunities
- Aggregation of needs and services
- Facilitated end customer opportunity, e.g. market, fair etc.
- e.g. Corporates (MNCs & local) facilitate interventions and opportunities for network of entrepreneurs

**Business network with vertical linkages**
- Collection of businesses networked horizontally to provide market opportunities for SMEs
- e.g. Corporates (MNCs & local) accelerate provision of supplier based opportunities amongst range of market players (horizontal business network) in support of network of entrepreneurs

*Key focus area for high impact*
### Stakeholders’ R&R

**Enablers must support public platform creation and support SMEs**

<table>
<thead>
<tr>
<th>Drivers</th>
<th>Key Linkage Requirements</th>
</tr>
</thead>
</table>
| **Hopes** | **Contribute to policy-development procedures**  
+ Job-creation  
+ Sustainable SME development and growth  
+ Poverty reduction  
+ Service and product provision to the poor  
+ Alignment of commercial and social imperatives | **Facilitate public-private linkages**  
- Ownership of cluster development processes  
- Creation of PPP forums and facilities |
| **Fears** | **Provision of access and insight to global best practices**  
- Lack of public-private collaboration  
- Restrictive legislative and regulatory environment  
- Lack of political and commercial will | ** Provision of policy and legislative examples and guidelines** |

- **Develop and provide support programmes**  
- Design programme  
- Provide programme coordination  
- Monitor/evaluate programme results  

- **Support access to finance**  
- Facilitate access to financial resources  
- Ensure training on financial literacy  
- Mobilise co-funding  

- **Develop and maintain business linkage networks**  
- Develop and provide information- and contact-sharing platforms and systems  
- Mobilise business mentors  

- **Provide or ensure provision of BDS**  
- Provide access to technical expertise
Stakeholder Collaboration Constraints

Key Challenges

- Lack of pro-poor focus due to conflicting policy demands
- Lack of consistent long-term strategy and support
- Lack of dedicated resources and capacity

- Lack of coordination of activities with high degree of overlap
- Focus on other factors than commercial viability
- Lack of impact measurement

- Lack of commitment owing to lack of incentives to support pro-poor initiatives, and lack of alignment with business strategy
- For MNCs in particular, difficulty in understanding specificities of different markets

- Lack of procurement readiness
- Survival & operational focus and inability to focus on improved procurement readiness

- Lack of coordination
- Lack of access to finance
- Lack of access to information and support
- Lack of alignment of products and services with market needs
- Lack of reliable information
Backup slides
### Lessons Learnt:

#### Developing SME’s through Vertical Networks

*Developing Vertical Networks = Creating Business Linkages / Integrating SMEs into supply chains*

<table>
<thead>
<tr>
<th>Strategic factors</th>
<th>Operational factors</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Corporates’ commitment. Strong corporate commitment and alignment of staff incentives toward local procurement and SME development greatly contribute to the success of the programme</td>
<td>• Steering committee and programme coordinator</td>
</tr>
<tr>
<td>• Programme strategy. A clear programme strategy is needed for local procurement, finance, management, programme monitoring and communications.</td>
<td>• Active participation of SME</td>
</tr>
<tr>
<td>• Focus on SME development. While cost reduction is a potential outcome of the programme, the driving force is the desire to make the SMEs world class.</td>
<td>• Hand-on mentoring</td>
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<tr>
<td></td>
<td>• In-house mentors</td>
</tr>
<tr>
<td></td>
<td>• Monitoring and Evaluation</td>
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<td></td>
<td>• Post-programme diversification – SMEs encouraged to diversify client base</td>
</tr>
</tbody>
</table>
# Lessons Learnt: Linkage Challenges

## Challenges in forming market access linkages (1 of 2)

<table>
<thead>
<tr>
<th>Operational Challenges</th>
<th>Solutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Securing internal commitment</td>
<td>Procurement policies</td>
</tr>
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<td></td>
<td>Performance measures and incentives</td>
</tr>
<tr>
<td></td>
<td>Culture of long-term thinking</td>
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<tr>
<td>Obtaining reliable, actionable market</td>
<td>Dedicated staff or department</td>
</tr>
<tr>
<td>information</td>
<td>Supplier databases</td>
</tr>
<tr>
<td></td>
<td>Network Leveraging</td>
</tr>
<tr>
<td>Measuring impact</td>
<td>Collection developed frameworks</td>
</tr>
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<td></td>
<td>Participatory monitoring and evaluation</td>
</tr>
<tr>
<td>agreements</td>
<td><strong>Reputation &amp; Relationship Management</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Challenges</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Solutions</strong></td>
</tr>
<tr>
<td>Managing expectations</td>
<td>Social responsibility agreements</td>
</tr>
<tr>
<td></td>
<td>Advance purchase agreements</td>
</tr>
<tr>
<td>Reducing dependence</td>
<td>Market diversification services for suppliers</td>
</tr>
<tr>
<td></td>
<td>Local economic development “beyond the value</td>
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<tr>
<td></td>
<td>chain”</td>
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<tr>
<td></td>
<td>Peer networking</td>
</tr>
<tr>
<td></td>
<td>Appropriate exit strategies</td>
</tr>
</tbody>
</table>

### Lessons Learnt: Linkage Challenges

#### Challenges in forming market access linkages (2 of 2)

<table>
<thead>
<tr>
<th><strong>Systemic Challenges</strong></th>
<th><strong>Solutions</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Building knowledge and skills</td>
<td>Standardised training modules</td>
</tr>
<tr>
<td></td>
<td>Best practice guidelines</td>
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<tr>
<td></td>
<td>Ongoing coaching</td>
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<tr>
<td></td>
<td>Enterprise Centres</td>
</tr>
<tr>
<td></td>
<td>Peer networking</td>
</tr>
<tr>
<td>Improving access to finance</td>
<td>Own financing institutions or arms</td>
</tr>
<tr>
<td></td>
<td>Capitalisation of external (often joint) funds</td>
</tr>
<tr>
<td></td>
<td>Links with microfinance institutions</td>
</tr>
<tr>
<td></td>
<td>Links with commercial banks</td>
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<tr>
<td></td>
<td>Non-traditional collateral</td>
</tr>
<tr>
<td></td>
<td>A focus on financial literacy</td>
</tr>
<tr>
<td>Strengthening regulatory and public policy environments</td>
<td>Collective engagement in public policy dialogue</td>
</tr>
<tr>
<td></td>
<td>Public sector capacity building</td>
</tr>
<tr>
<td>Addressing inadequate physical infrastructure</td>
<td>Supply collection centres</td>
</tr>
<tr>
<td></td>
<td>Shared infrastructure</td>
</tr>
<tr>
<td></td>
<td>Information &amp; communications technologies</td>
</tr>
<tr>
<td>Filling gaps in complementary markets</td>
<td>Marketplaces</td>
</tr>
<tr>
<td></td>
<td>Direct sales</td>
</tr>
</tbody>
</table>

## Common Business Linkage themes

### A birds-eye view of landscape and challenges

<table>
<thead>
<tr>
<th>Systems Thinking</th>
<th>Collaboration</th>
</tr>
</thead>
</table>
| • Systemic challenges faced by BOP suppliers/distributors/customers make stability, sustainability and profitability hard to achieve.  
• Market systems are full of holes and unreliable.  
• Examples are BOP suppliers defaulting on loans or not being able to access preferential procurement opportunities due to costs of legal incorporation.  
• The whole value chain has to be organised end-to-end to fill in the missing pieces that make it possible to find stability and earn a profit. | Up to recently two approaches to filling in missing pieces:  
• Companies fill in the missing pieces themselves – part of cost of doing business, but it can be costly  
• When this does not make business sense, they look to corporate foundations and social responsibility departments to make the difference.  
Third approach, increasingly common, is to reach out to external collaborators, e.g.:  
• Companies in complementary lines of business,  
• Government agencies  
• Civil society organisations  
• Microfinance institutions  
Collaborative models are characterised by:  
• Multiple actors  
• Finding complementary business (or mission based) cases  
• Specialising in what they do best  
• Together filling in gaps in the market system of the BOP  
• Reducing and targeting need for subsidies to make systems work  
• Enabling BOP business models to achieve great sustainability and scale. |

**Inclusive Business Model**

**Summary of challenges and solutions**

<table>
<thead>
<tr>
<th>Value Chain</th>
<th>Procurement</th>
<th>Product/Service Development</th>
<th>Distribution</th>
<th>Sales and Marketing</th>
<th>Customer Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Challenges</td>
<td>Achieving quality, stability, and cost-competitiveness of supply</td>
<td>Developing a high-value, low-cost offer</td>
<td>Ensuring product accessibility while minimizing distribution costs</td>
<td>Ensuring willingness and ability to pay</td>
<td>Strengthening the value proposition, retaining customers, and fueling positive word of mouth</td>
</tr>
</tbody>
</table>
| Solutions   | Aggregation • Collection centers • Producers’ associations  
Capacity-building • Extension agents • Farmer field school • Demonstration plots  
Access to inputs • Bulk purchasing • Sell inputs at cost • Give inputs away  
Access to finance • Input purchase on credit • Cash loan • Third-party financing | Adding value • High quality • Income generating potential • Accreditation • Bundled product • Technology  
Reducing cost • Standardization • Bulk purchasing • Low-cost design • Energy efficiency • Leveraging existing customer knowledge  
Matching customers’ cash flows • Small package size • Modular product • Shared access | Expanding reach • Leveraging established retail and constituent networks • Leveraging existing retail outlets • Employing specialized, independent distributors • Virtual distribution • Evening hours • Convenient locations  
Customized delivery • Frequent, small drops • Custom assortments  
Capacity-building • Training • One-on-one coaching  
Access to finance • Inventory purchase on credit  
Reducing cost • Efficient distribution technology • Public funding | Communicating value • Customer awareness-raising • Word of mouth • Key message • Incentives  
Affordable pricing • Tiered pricing • Public funding  
Increasing collection rates • Business training • Smart metering • Sense of ownership • Leveraging existing retail outlets • Payment incentives  
Access to finance • Purchase on credit • Third-party financing | After-sales support • Customer education and training • Maintenance and repair • Resale support • Career services • Continuous access to cash |

“Inclusive Business models expand access to goods, services and livelihood opportunities for those at the base of the pyramid in a commercially viable, scalable way.”

Source: Accelerating Inclusive Business Opportunities: Business Models that make a difference, IFC 2010
# Production linkages

## Increasing marketing and trade

*Three main, non MECE* modalities of linkages exist in industry, which can co-exist and interrelate across industries, production sectors and countries*

<table>
<thead>
<tr>
<th>Alliances</th>
<th>Clustering</th>
<th>Networking</th>
</tr>
</thead>
</table>
| Firms come together in contractual arrangements e.g.  
• Subcontracting  
• Licensing – permission to manufacture under licence  
• Joint venture – creation of a third firm  
• Strategic alliance – essentially JV without creation of third firm  
• Consortium – group of firms joining to form buying group to make purchases which they share.  
Alliances between large companies and SMEs usually take form of vertical linkages. | Firms come together in contractual arrangements e.g.  
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• Consortium – group of firms joining to form buying group to make purchases which they share.  
Alliances between large companies and SMEs usually take form of vertical linkages. | Collection of firms working in cooperation, though not necessarily in the same place.  
• Main characteristics:  
  • Arms length interactions between firms  
  • Neither formal links nor equity participation are necessary  
  • Does not require geographical proximity to be efficient  
  • Can link firms whose activities are distributed across the world.  
• Horizontal networking:  
  • Small group of firms cooperate in production of final product by specialising in specific steps of the production process  
  • Firms producing similar product lines benefit the most  
  • No firm performs a dominant role (unlike vertical linkages)  
• Networking can enhance marketing and trade:  
  • Enables firms to share risks and costs and access market  
  • Increases knowledge about market, suppliers, customers and competitors. |

Source: “Linkages between SMEs and Large Industries for Increase Markets and Trade: An African Perspective”; M. Nureldin Hussain

* MECE = Mutually Exclusive, Comprehensive and Exhaustive