Value Chain Development for Decent Work

A guide for development practitioners, government and private sector initiatives

Matthias L. Herr
Tapera J. Muzira
International Labour Office
This guide has been prepared in the context of the Paris Declaration for AID Effectiveness, which calls for efforts to harmonize aid and increase its effectiveness as well as to achieve development goals on the basis of national priorities, systems, structures and procedures. Further to this, joint assistance frameworks are strengthening national ownership and government leadership of the development process with cooperating partners aligned in accordance with national priority sectors for broad based job creation and economic growth.

The guide is mindful of the vision and strategy adopted by member states in the 2008 ILO Declaration on Social Justice for a Fair Globalization, reflecting the wide consensus on the need for a strong social dimension to globalization in order to “achieve an improved and fair outcome for all”.

It has been prepared at a time of profound global economic turbulence where governments, employers and workers are particularly concerned about the effects of the crisis on people, on enterprises and employment, on social cohesion and on stability. Promoting employment, social protection, and fundamental principles and rights at work as well as social dialogue through the ILO’s Decent Work Agenda constitutes an effective policy package in response to the current economic crisis.

The “Value Chain Development for Decent Work” guide has been prepared for use in facilitating and promoting growth in priority sectors already agreed in Decent Work Country Programmes that are based on national priorities owned and led by the constituents (Government and its social partners Employers/Business and Workers). Decent Work Country Programmes are part of national development frameworks focusing on national priorities; they are not ILO programmes. The Guide can thus be tailored to specific situations and used by both public and private sector entrepreneurs to facilitate and promote broad based growth in selected sectors. While there may be some good arguments for understanding trade-offs between profitability and social inclusion, this guide highlights the fact that in view of rapid contemporary technological advancements strategic human resources...
management is the only true source of sustainable competitive advantage today. It is unique and based on the principle that a workforce that is objectively motivated by better working conditions or Decent Work is simply good business and pivotal to sustaining competitiveness and productivity in any given sector as well as bringing other benefits such as pro-poor or inclusive socio-economic development.

The guide provides a systemic perspective, addressing not only value chain issues in the narrow sense but also important framework conditions, such as the relevance of the duration and cost of customs clearance, tariffs etc. Likewise, it addresses all relevant aspects that donors and other value chain facilitators need to take into account, including the need for institutional reform and its underlying incentive systems; issues of sustainability; the need to upscale project experiences; gender issues; etc. The chapters addressing these issues show that the authors have an excellent overview of good practices in private sector development.

It is worth noting that the focus on markets, e.g. for the provision of business development services, reflects the state of the art in PSD; for example, the authors show the relevance of different sources of service provision (other than public agencies) including private consultants, business associations, NGOs, and embedded services. The guide rightly highlights the need to address underlying causes (failure in the performance of market systems) rather than symptoms in individual chains. Likewise, the notion of grids of intersecting value chains is closer to reality than common “linear” chain concepts.

The guide also focuses on action research, whereby value chain mapping and research can already contribute to mobilizing stakeholders and seeking solutions on a participatory basis. It provides many helpful details of how to organize stakeholder processes in practice, how to set up a monitoring system, and so forth.
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The authors are especially grateful to Nikolai Rogovsky and David Lamotte for their assistance and guidance, their valuable feedback and comments on drafts, and their help in coordinating and bringing together relevant resource persons. A word of thanks also goes to Dr. Tilman Altenburg and Merten Sievers, whose reviews and comments have been much appreciated, as well as Julius Mutio for his support in bringing the guide to publication. And then there are of course all the others who have contributed in the background, provided useful information and, through this support, made this guide possible.

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The views in this guide express the personal opinions of the authors, which are not necessarily those of the ILO, and all references used are accurately reported.
Prologue: It’s the stupid cows!

Example: the Columbian leather industry value chain
The following story\(^1\) is told by a monitoring company that worked for the government and private sector leaders in Colombia to study and provide recommendations on how the leather producers of that Andean nation could become more prosperous by exporting to the United States, and how the leather industry could thus create employment and income opportunities for many people in both urban and rural areas of the country:

Retailers and consumers: quality bad, price too high!
We began in New York City to find the buyers of leather handbags from around the world, and we interviewed the representatives of 2,000 retail establishments across the United States. The data were complex but boiled down to one clear message: the prices of Colombian handbags were too high and the quality was too low.

Manufacturers: “No es nuestra culpa!”
We returned to Colombia to ask the manufacturers what lowered their quality and forced them to charge high prices. They told us, “No es nuestra culpa.” It is not our fault. They said it was the fault of the local tanneries that supplied them with the hides. The tanneries enjoyed a 15-percent protective tariff levied by the Colombian government, which made the price of competing hides from Argentina too expensive.

Tanneries: it’s the mataderos!
We travelled to the rural areas to find the tannery owners. The tanneries pollute the nearby ground and water with harsh chemicals. The owners were happy to answer our questions. “It’s not our fault,” they explained, “It’s the fault of the mataderos, the slaughterhouses. They provide low-quality hide to the tanneries because they can sell the meat from the cow for more money with less effort. They don’t care about damaging the hides.”

Slaughterhouses: the ranchers don’t care!
We went to the camp and found slaughterhouses with cowhands, butchers, and managers wielding stopwatches. We asked them the same questions and they explained that it was not their fault; it was the ranchers’ fault. “You see,” they said, “the ranchers overbrand their cows to keep the guerrillas? some of whom protect the drug lords from stealing them.” The numerous brands destroy the hides.

Ranches: it’s the stupid cows!
We finally got to the ranches, far away from the regional capital. We had come to the end of our search because there was no one left to interview. The ranchers spoke rapidly in a local accent. They told us that the problems were not their fault. “No es nuestra culpa,” they said. “Es la culpa de la vaca.” It’s the cows’ fault. The cows are stupid, they explained. They rub their hides against the barbed wire to scratch themselves and fend off the flies that bite them.

Are stupid cows the reason why Colombia cannot access the US market?
We had come a long way, banging our laptop computers over washboard-surfaced roads and getting our shoes destroyed with the chemicals in the tanneries and the mud. We had learned that Colombian handbag makers cannot compete for the attractive US market because their cows are dumb.

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The need to understand underlying systemic constraints

The example above provides us with a very useful lesson: in order to understand why the Columbian leather industry is not competitive and does not realize its full potential in terms of job and income creation, we need to look beyond the mere chain of business transactions. Business stakeholders in the value chain will point fingers at each other all too easily: it’s always someone else’s fault! This has been the experience of many value chain initiatives, and it often leads to deadlock (‘If the problem isn’t my fault, why should I do anything about it?’).

Value chain research and analysis thus needs to go beyond mere finger-pointing and understanding of core transactions within the chain: it needs to identify the underlying systemic causes of bottlenecks in the chain; it needs to understand the nature of relationships between businesses in the chain and other relevant market players; it needs to understand the role of specific market functions and (formal and informal) rules that govern the value chain; and it needs to identify incentives and capacities of market players.

So what should the team have asked instead?

Of course stupid cows are not the reason why the Columbian leather industry is unable to compete on the US market! The team of the monitoring company has spoken to various businesses in the value chain, but so far it has only identified symptoms (i.e. lack of quality, high price, lack of awareness, stupid cows, etc.). Consequently, it now needs to understand the underlying causes that are preventing the industry from realizing its full potential. Key questions would, for example, be:

- How is knowledge and information passed through the value chain – from retailers to ranchers?
- Who is responsible for providing information?
- Are there any industry mechanisms and organizations that facilitate better coordination between businesses?
- Why do the tanneries need a 15-percent protective tariff from the government?
- In general: which market functions and rules are currently underperforming, thus making the Colombian leather industry unable to compete on the US market?
- And which market player is responsible for performing these market functions? And what prevents this market player from performing better?
- Who else has the incentive to perform a certain market function?

Moving from symptoms to underlying systemic constraints

By asking ourselves these questions, we are moving quickly from symptoms to underlying systemic constraints. Only when these underlying constraints can be solved will the industry find a pathway to sustainable competitiveness.

The approach described in this guide moves away from a mono-dimensional view of value chains, towards a multi-dimensional vision in which a sector a) consists of a grid of multiple value chains – a value chain system, and b) is embedded into a market system consisting of various functions and rules and influenced by various private and public market players. It does so by reflecting in particular on Decent Work issues within the value chains. Poor and disadvantaged groups are always part
of value chains, whether as producers, workers or consumers. The essential question is thus: *how can we achieve competitiveness while creating new jobs and income opportunities for men and women and promoting better working standards in value chains?*

**Decent Work**

The authors hope that this guide will give you some ideas on how to address this crucial issue.

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Introduction: What it's all about
**Introduction: What it's all about**

**Growing competitive pressure and need for better integration**

Enterprises of various sizes – ranging from multinational companies to medium, small and micro enterprises – are not only increasingly interconnected, but are also interdependent. Large companies rely on small enterprises either as suppliers of various inputs and preliminary products, or as service providers catering for various needs of production units – such as food and beverages, or as part of their marketing and distribution network for reaching markets, especially in rural areas. If enterprises are increasingly interdependent, so are the jobs and incomes they generate.

At the same time, sectors in emerging markets are increasingly finding themselves competing against companies from other countries operating in the same sector – not only for export market shares, but also increasingly for shares on their own domestic markets. Where competition is about price and reducing costs of production, small enterprises and workers/employees are often at the losing end. Small producers find it difficult to meet market requirements because they do not possess the necessary technology and skills – or they do not have access to sufficient market information in the first place.

**Box 0.1: Competing T-shirt value chains**

<table>
<thead>
<tr>
<th></th>
<th>Sourcing</th>
<th>Production</th>
<th>Delivery</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Import Dependence</td>
<td>Raw material costs</td>
<td>labour costs/shirt</td>
</tr>
<tr>
<td><strong>Kenya</strong></td>
<td>65%</td>
<td>$2.30</td>
<td>$0.40</td>
</tr>
<tr>
<td><strong>Honduras</strong></td>
<td>80%</td>
<td>$0.80</td>
<td>$0.25</td>
</tr>
</tbody>
</table>

**High tariffs:**
- Honduras = 9.6%
- Kenya = 21.9%

**High cost of logistics:**
- Honduras = $658 / TEU
- Kenya = $1475 / TEU

**Lengthy customs clearance for imports:**
- Honduras = 4 days
- Kenya = 15 days

**Lower wages:**
- Honduras: $12 / man-day
- Kenya: $9.40 / man-day

**Lower labour productivity:**
- Honduras: 45-50 shirts/day
- Kenya: 20-25 shirts/day

**Lengthy customs clearance for exports:**
- Honduras = 1 day
- Kenya = 2 days

**High incidence of rejects:**
- Honduras: <1%
- Kenya: >3%

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3 This guide uses Emerging Markets as a substitute for the term “developing countries”, thus no longer regarding developing countries as the recipients of aid and development programmes, but acknowledging that they are serious players in the market – both as suppliers to global markets, and also as consumers, workers/employees and providers of services.
### Introduction: What it's all about

#### Disconnect between formal and informal economy

The informal nature of many economies in emerging markets poses additional challenges: relations between large companies and small enterprises remain unstable (e.g. due to the lack of contracts and legal enforcement) – leading to high production costs and problems in quality consistency; small enterprises are unable to access many business services such as credits, training and research facilities, government support, etc.; in quality-sensitive sectors such as the food industry, buyers are unable to trace products to their origins; workers and employees in informal enterprises are deprived of their rights for social protection and labour standards. There are many more challenges which indicate the imminent disconnect between formal and informal economy in emerging markets – these are but a few examples.

The value chain approach helps multinational companies, governments and their development partners to understand and address these challenges within a market-oriented framework.

### Box 0.2: Definition of value chains

**What is a value chain?** A value chain “describes the full range of activities that are required to bring a product or service from conception, through the intermediary phases of production (involving a combination of physical transformation and the input of various producer services), delivery to final consumers, and final disposal after use.”

This includes activities such as design, production, marketing, distribution and support services up to the final consumer (and often beyond, when recycling processes are taken into account).

The activities constituting a value chain can be contained within a single firm or divided among different firms, as well as within a single geographical location or spread over wider areas.

The term ‘value chain’ refers to the fact that value is added to preliminary products through combination with other resources (for example tools, manpower, knowledge and skills, other raw materials or preliminary products). As the product passes through several stages of the value chain, the value of the product increases.

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Figure: Herr, Matthias (2008): Local Value Chain Development for Decent Work, International Labour Organization, Enterprise for Pro-Poor Growth project, Sri Lanka.

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Drivers of change that prompt value chain development

Having established what value chains are, what exactly is value chain development? For definition purposes it is useful to make a distinction between five drivers of change that could prompt value chain development:5

1. System efficiency

There are opportunities for reducing costs and increasing efficiencies on the market if value chain stakeholders – large and small – work together. Buyers want to buy products the highest possible quality at the lowest possible price; they want quick and flexible responses to their orders and short delivery times. In order to achieve these market requirements all opportunities for increasing system efficiency need to be explored – and this requires cooperation and coordination of activities amongst value chain stakeholders.

5 Taken from Value Chain Initiative (2004): Value chain guidebook – a process for value chain development, Agriculture and Food Council of Alberta, Nisku (Canada). Available from www.agfoodcouncil.com. The Value Chain initiative focuses mainly on product quality, differentiation and system efficiency as drivers of value chain development. These have been taken up and further developed in this guide.
2. Product quality
Markets today are changing fast and competition is becoming increasingly fierce. If enterprises want to stay in the market, they need to make sure that their products and services meet continuously changing market requirements and demand conditions. **What counts, is the end product that the consumer receives, and the level of satisfaction that it creates.** Value chains can compete against each other in terms of production cost and/or **product quality.**

3. Product differentiation
The better stakeholders cooperate along the value chain and coordinate their activities, the harder it will become for competitors to copy the product and the production process – because it is not just the product they need to copy, but the entire system. It is therefore important to understand what competitors are doing, and how they are doing it, and then to find ways of achieving a competitive advantage over them. This is mainly a matter of continuous **innovation and learning** within in the value chain – i.e. how do I make my products different from those of my competitors? Large companies also need to understand that it is important to share knowledge and information also with small enterprises in their supply or retail chains. This is purely in their commercial interests and has nothing to do with Corporate Social Responsibility (CSR). Innovation and learning has to take place throughout the entire value chain if sectors want to remain competitive on world markets.

4. Social & environmental standards
Consumers are becoming increasingly aware of **social and environmental standards** and are increasingly demanding products that fulfil these requirements. Retail and multinational companies are feeling pressure from consumer organizations, media, governments and NGOs to improve social standards in their supply/retail chains and to minimize environmental impact. The ILO’s **International Labour Standards** are playing an increasingly important role and are being included in codes of conduct of private sector CSR initiatives – such as the global Ethical Tea Partnership. Here again, it is more than a matter of doing business in a socially responsible way: it is in the commercial interests of companies to react to this consumer demand. Ensuring good social and environmental standards also means being able to trace products and services all the way back to their origin. This requires that businesses along the value chain cooperate.

5. Enabling business environment
**Enabling business environment:** Value chains do not exist in isolation but they are embedded into a highly complex social, economic, political and cultural environment, which determines the nature and success of business transactions within the chain (e.g. investments or business start-ups). As **Box 0.4** illustrates, the business environment can be seen as consisting of an immediate environment in which enterprises are part of markets in which they use various

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7 See www.ethicalteapartnership.com
resources and markets in order to produce products and services. The market in turn is influenced by regulations, institutions and interventions that immediately affect a particular sector (such as health safety regulations for the dairy industry).

Apart from the immediate and sector-specific environment, there is also a wider business environment, consisting of broader government policies, macro-economic stability, public services, international and bilateral trade agreements, but also cultural and social factors (such as attitudes to doing business and demographic trends) and climatic and environmental conditions.

**Box 0.4: Business environment**

*Source: The Springfield Centre, www.springfieldcentre.com*
Putting value chains and drivers into a systemic and operational market system framework

The value chain as described above consists of transactions from one business to another. The line of transactions from producer to consumer constitutes the value chain. However, we have also learned that the value chain of a particular sector is always embedded into a market system consisting of various supporting functions and rules. Within this market system different market players are either directly engaged in business transactions or part of supporting organizations such as BDS providers, government institutions or NGOs. The knowledge of how market systems work is of particular importance to governments and development organizations for developing upgrading strategies that target systemic root causes for competitive constraints.

Box 0.5: Value chains as part of market system framework

Introduction: What it's all about
Introduction: What it's all about

Chapter 1

Sector selection for Decent Work
Summary

Sector selection is important and sectors are often already defined in national development frameworks in accordance with national priorities. The “Value Chain Development for Decent Work” guide has been prepared for use in facilitating and promoting growth in priority sectors already agreed in Decent Work Country Programmes based on national priorities owned and led by the national constituents (Government and its social partners, Employers/Business and Workers). In this case monitoring and evaluation frameworks are in place, as would be steering committees and working groups for planning and implementation.

You may therefore want to skip this section if you are part of a priority sector yourself or if this topic is not relevant to you for this and other reasons.

Where there are no country strategies for private sector development and there is some scope for demonstrating the potential impact of sectoral strategies such as value chain development, this section can be used to identify sectors that have the potential for Value Chain Development for Decent Work. In doing so, sector selection uses not only financial or economic criteria such as a) good return on investment b) sustainable competitive advantage c) potential for growth, innovation and value creation but also social criteria such as (a) partner country priorities, ownership and participation (b) technological and environmental factors (c) potential for inclusive development - pro-poor economic growth, job creation and poverty reduction amongst other criteria for achieving Decent Work.

Outcomes:

• A sector with potential for profitability, growth and Decent Work
• Socio-economic indicators for monitoring and evaluation
Sector selection requires justification

Sector selection is a delicate issue: why do we select the garment industry and not fruit and vegetable processing? Or spices rather than paddy/rice cultivation? Such a decision requires careful consideration of the social and economic factors which shape the sector.

1.1 Defining sectors as socio-economic system frameworks

Definition of sectors

By “sectors” in the first place, we refer to socio-economic activities in which a) core transactions are similar in production and processing, b) businesses share certain supporting functions with one another, c) specific rules and regulations govern the way firms do business, and d) market players can be attributed to specific businesses, functions and rules. Within sectors we will often find several value chains and clusters (which are generally part of value chains themselves). Many would speak of three economic “sectors”: agriculture, industry and services. However, we adopt a narrower definition here, such as the tea sector, the coconut coir industry, the embroidery sector, the dairy sector, or the Jatropha bio-diesel industry. These are often also called “sub-sectors” of the three main economic sectors. However, let’s not dwell on terms.

Box 1.1: Definition of sectors
1.4 How to select sectors using Decent Work criteria

So how do we select sectors?
The following section will explain how to select sectors for value chain development initiatives in 4 steps: 1) defining objectives and target groups, 2) deciding on selection criteria, 3) rapid assessment of available sectors, and 4) application of selection criteria in a consultative meeting with

1.4.1 How to select sectors using Decent Work criteria

Step 1:
Defining objectives (Decent Work) and target group
In order to select a sector for a value chain initiative, you need to be sure about your own objectives: What do I want to achieve? Who is my target group (the market and beneficiaries)? Decent Work Country Programmes facilitated by the ILO among its national constituents (government, employers and unions) provide a guideline for projects as to which selection criteria best match a country's Decent Work agenda. By placing a value chain initiative for a sector within the framework of Decent Work Country Programmes (which reflect the constituents' development priorities), it will also be easier to generate support and link up with other development initiatives.

Putting sector selection in the context of Decent Work Country Programmes
Examples for objectives in Decent Work Country Programmes include: poverty reduction through creation of decent work opportunities with a focus on young women and men (employment and income creation), reducing incidences of child labour and its worst forms, mitigating the socio-economic impact of HIV/AIDS at the workplace, promoting gender equity, improving occupational health and safety, enhancing skills, etc. So where does your value chain initiative fit in?

The target group
Assuming that as a reader of an ILO guide to Value Chain Development for Decent Work, you share similar objectives as we do – i.e. the promotion of Decent Work in value chains, we might ask ourselves: which are then the most disadvantaged groups in value chains in terms of Decent Work? We might come up with the following answers:

- Small and medium-sized enterprises (SMEs) which either supply to or buy from larger companies,
- Workers and employees in medium to larger business units (e.g. factories, offices, etc.),
- Women working in various occupations along the value chain (e.g. as home-based workers, employees, or micro-entrepreneurs),
- Young people and youth also working in various occupations in the value chain and looking for a career or trying to enter employment in certain sectors,
- Other disadvantaged groups such as disabled people seeking employment, ethnic minorities, children (in the case of forbidden child labour), etc.
Sector selection for Decent Work