

IDS Policy Briefing

The latest development issues for policy-makers from the Institute of Development Studies

Small firm clusters: working to reduce poverty

Clustering together can help small firms compete in local and global markets. Cluster development also helps to reduce poverty. It can create employment, generate incomes and reduce vulnerability for small producers and poor workers. The critical policy challenge is how to make cluster development strategies more effective for the poor. This Briefing reviews the links between clusters and poverty reduction, identifies the policy implications and presents a framework for poverty and social impact assessment of cluster development.

Industrial clusters and the poor

Industrial clusters can have a direct effect on poverty – generating employment, incomes and well-being for workers within the cluster. They also have indirect effects on the local economy, creating secondary jobs, attracting service providers and generating economic growth. The very presence of a cluster changes the context in which the poor live by enhancing the ability of individual workers and producers to improve their capabilities and their well-being. This aspect of the gains from clustering has often been ignored by researchers and policymakers. Addressing poverty raises critical questions for cluster development policy.

Small firms, global markets

Industrial clusters – or geographical concentrations of firms working in the same industry – offer small and medium-sized enterprises (SMEs) the prospect of competitive growth. There are numerous examples of small firm clusters in developing countries successfully competing in global markets – from the shoemakers of Brazil's Sinos Valley to the garment producers of Tiruppur and Ludhiana in India. Many such export clusters began as informal networks in resource-poor regions and at early stages of industrial development. For such communities, clusters offered a gradual and sustained path to industrial growth.

Being in a cluster offsets some of the constraints regularly faced by SMEs, including scarce resources and limited human and financial capital. It generates agglomeration benefits, from skilled labour and specialised inputs to know-how and information. This in turn lowers costs and reduces the need for extensive capital. In addition, clusters attract traders who connect local producers to larger and more distant markets. Thus by locating within clusters small firms can transform under-utilised assets, from small-scale savings to family labour in ways that would not



Khalid Nady/IDS

be feasible if they operated in isolation.

The strength of the cluster model is its focus on local linkages, although recent research shows that external linkages also matter. This emphasises how local clusters are inserted into global value chains that connect clustered firms to local and global markets. Global value chains bring together dispersed actors into networks of production, trade, finance and other activities that turn raw materials into finished goods and services for end markets. Such networks are organised by lead firms, including global buyers and retailers, who exercise power over the chain, coordinating activities and directly influencing the potential for local upgrading.

The value chain framework also provides a basis for mapping local and external ties. This can be extended to show how such ties affect workers, their families and the wider community. Mapping can help identify poverty groups within a cluster – such as small producers who lack assets or capacity, or poorly remunerated casual wage labourers. Poor groups may also have a particular gender, ethnic or religious composition that restricts access to the means to enhance their position.

Key questions

- How do industrial clusters reduce poverty?
- In which types of clusters is this most significant?
- How are poverty impacts felt by different types of producers and workers within clusters?
- How can cluster development initiatives better address poverty reduction goals?
- What is the appropriate methodology to assess the poverty and social impact of cluster development?
- What insights does the cluster model offer to standard poverty alleviation strategies?

UNDERSTANDING POVERTY

Definitions of poverty traditionally focused on income and consumption.

There is growing consensus on the need for a broader definition of poverty which also includes social dimensions of well-being, risks and the vulnerability of poor groups.

This draws out the multi-dimensional and dynamic nature of poverty. It can also include a participatory approach which allows poor people to voice their own concerns on how their well-being can be improved.

Clustering and poverty: conceptual links and empirical evidence

Conceptually, clusters and poverty are related in three distinct ways:

- **Cluster features:** certain types of clusters can have more direct impact on poverty. These include rural clusters and, in the urban informal economy, clusters with a preponderance of SMEs, micro-enterprises and homeworkers, clusters in labour-intensive sectors and clusters that employ marginalised and poorer groups of workers, such as women, minority groups, migrants and unskilled labour.
- **Cluster processes:** agglomeration economies reduce costs and allow small firms to access markets, thereby raising the capabilities of workers and producers through income and employment. Cluster joint action can take such capabilities further by strengthening the capacity of local firms and reducing their vulnerability to external shocks. The presence of social capital can be critical to this, strengthening trust and fostering collaboration. It can also contribute to informal social protection, easing the burden on vulnerable groups.
- **Cluster dynamics:** cluster growth produces winners and losers among firms and workers, underlining the importance of processes of differentiation. For a poverty reduction agenda, it is critical to note which types of firms, and workers, gain over time and which lose out.

Cluster development provides an important survival and growth opportunity for poor regions in developing countries – from rural artisan clusters that provide critical off-farm incomes to poor households and women workers (Central Java, Indonesia), to urban informal sector clusters engaged in low-skilled and labour-intensive garment production (Lima, Peru) and vehicle repair (Kumasi, Ghana). Such clusters generate work and incomes for poor, often migrant, households. Moreover, there is clear evidence that producers and workers within clusters fare better, in terms of their well-being, than those in non-clustered settings.

In incipient clusters, small producers advance by taking small steps in coordination with others. This allows them not only to survive, but to grow, raising their capabilities and improving their well-being. Local agglomeration economies are central to this, as is joint action. This is observed in incipient and mature clusters from rural Indonesia to the urban informal sector of Nairobi, to the export clusters of Mexico, Brazil, Pakistan and India. Joint action is

also important, especially in the context of assisting local producers and workers to confront external shocks. Cooperation through local institutions reduced the vulnerabilities of clustered producers in Sialkot, Pakistan and in the Palar Valley, India. And there is some evidence that social capital in both these areas strengthened cluster capacities, raising the well-being of local workers and producers.

Despite these positive findings, it is also evident that cluster growth trajectories can result in differentiated outcomes. Local linkages often give way to external linkages as outside knowledge and know-how become critical to survive in global markets. Conflicts between the competing interests of large and small firms can become more apparent, with smaller producers often being squeezed. Finally, there are signs that particular categories of workers, especially women and unskilled workers, can lose out as clusters upgrade.

Making cluster policy development work for the poor

The United Nation's Industrial Development Organisation (UNIDO) assists small firm clusters in many developing countries through a three-pronged cluster development policy:

- **Enterprise development:** helping existing groups of firms to upgrade and new ones to emerge
- **Business environment:** promoting business development services that channel information and services to local firms
- **Local governance:** facilitating cooperation among firms but also developing cluster-wide institutions.

Each of these three strategies can have direct positive effects for small producers and workers. Enterprise development can raise incomes, improve workers' skills and generate work for marginalised groups. Business linkages can raise the security of firms and workers by improving competitiveness, and diversifying markets. Local governance can improve the responsiveness of local institutions to the needs of small firms and poor workers. Through such strategies entrepreneurs and workers can raise their assets and entitlements through higher incomes, employment rights, access to markets, social capital and social protection.

The challenge for UNIDO is to understand better the poverty consequences of its cluster development policies. This requires developing poverty and social impact assessment methodologies that measure impacts on poor groups within clusters, thereby strengthening the pro-poor aspect of cluster development policy.



A participatory poverty assessment in the Sindhudurg cluster, India

UNIDO PRO-POOR CLUSTER PROGRAMMES IN INDIA

In two clusters UNIDO's interventions have sought to blend traditional cluster development policies with strategies targeting the needs of the poor.

The Sindhudurg cashew processing cluster in Maharashtra generates incomes for poor marginal farmers, micro-entrepreneurs and workers, many of whom suffer poor health and have restricted access to means to enhance their livelihoods. Assisting the formation of a food processors' association helps local producers address common problems.

The Chanderi handlooms cluster in Madhya Pradesh employs nearly 10,000 weavers. A participatory poverty assessment exercise revealed that the vast majority of households suffered from bad health, poor working conditions and limited access to credit. Cluster support is leading to local weavers and traders forging new market linkages by participating in national and global trade fairs, while skill upgrading means better quality and more diverse products and new norms of entrepreneurial behaviour also emerge.

Women are strongly over-represented among the poor in both clusters. Recognising this has led to more concerted efforts to improve women's access to markets. Self-help groups are bringing about improvements in local health service delivery – especially for women – and have identified training needs that have enhanced local skills and capabilities.

Poverty and social impact assessments of cluster development

A better understanding of the links between cluster development programmes and poverty can be gained through poverty and social impact assessment. This measures the differential impacts, positive and negative, intended or unintended, which result from policy interventions. Impact assessment can help examine how cluster development policies affect the lives of small producers and workers within clusters. By adopting a sustainable learning approach the focus moves from proving impact to improving ongoing policy, making it more effective and enhancing the pro-poor dimension of cluster development policy in the future.

Poverty is likely to be greater for certain groups within a cluster. Mapping the effect of policy on value chain and cluster ties provides a framework for:

- Identifying which groups experience the greatest level of deprivation;
- Tracing poverty impacts of a policy, via enterprises and service providers, on poor groups in a cluster.

Poverty groups are those who have common experiences of low income and low levels of well-being within the cluster. They have relatively few assets, capabilities and entitlements compared to other groups. This could be reflected in their inability to achieve a minimum standard of living, their insufficient skill or training, their poor health or their lack of participation and empowerment. Women and ethnic or religious minorities are often among the most disadvantaged. Poor

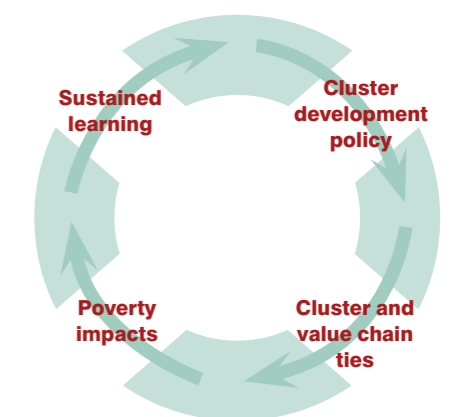
groups themselves need to participate in assessing their own well-being and how they can achieve a fuller life.

Impact assessment can facilitate this process, developing indicators such as levels of income, skill, occupational health, discrimination and participation through which the poverty impact of a cluster development programme can be assessed. Indicators can be quantitative or qualitative, and the use of participatory tools helps to ensure involvement of poor groups.

Value chain mapping helps identify the key stakeholders and actors within a cluster. In addition to providing essential sources of information for the impact assessment, partnerships can contribute to pro-poor initiatives. For example corporate social responsibility programmes linking firms and actors inside and outside a cluster can help to address the terms and conditions of work for poor producers and labourers. Cluster stakeholders can play a key role in developing a more pro-poor cluster development programme.

Sustainable learning is critical if impacts are to be maintained. This implies that impact assessment should identify ways in which stakeholders and poor groups within clusters can monitor and address poverty impacts on an ongoing basis, and that it should inform pro-poor cluster development policies relevant to all stakeholders. This results in a virtuous policy circle (see Figure 1) where cluster development policy is continuously improved upon and made more effective for poor groups through a sustainable learning approach to poverty and social impact assessment.

Figure 1. Cluster development policy and poverty impacts: achieving a virtuous circle



The Chanderi handlooms cluster in India employs nearly 10,000 weavers

USING CLUSTERS TO ADDRESS POVERTY

A CASE STUDY OF ELIMINATING CHILD LABOUR AND PROMOTING SOCIAL POLICY IN SIALKOT, PAKISTAN

The active collaboration of the ILO, UNICEF, the Save the Children Fund, global buyers, the local Chamber of Commerce, and local NGOs helped eliminate the widespread use of child labour in the Sialkot sports goods cluster. It also addressed the root cause of child labour through education, income generation and targeted social protection programmes for the poorer households which relied on the incomes of their children. The cluster not only made the programme feasible, it accelerated its spread, lowered costs and was strengthened through local collaborative networks. Consequently, Sialkot is the first district in Pakistan to have a targeted strategy for universal primary enrolment. Improving the local skill base through the education and training of children can have direct pro-poor gains as well as enhance the cluster's overall competitive position in consumer markets where ethical and labour concerns are significant (Nadvi 2004).

Clusters and poverty: the policy challenge

There is a clear link between clusters and poverty reduction which is evident in incipient rural and urban clusters that directly generate income for the poor – especially unskilled women and migrants. It is also apparent that mature clusters can be 'engines of growth' resulting in wider impacts on the local economy. Through agglomeration benefits and joint action, clustering can strengthen pro-poor impacts by enhancing the well-being of small producers and workers, reducing their vulnerability to external shocks. Social capital can further promote this and provide a basis for local social protection, especially for the most vulnerable households.

Many cluster development initiatives address such concerns by targeting training to poorer or marginalised groups of workers and artisans and through forms of collective joint action. Yet most cluster development programmes do not explicitly factor poverty concerns into their goals. Thus the challenge in making cluster development more pro-poor involves:

- **Poverty targeting:** identifying poverty groups and paying greater attention to their specific needs in cluster development. This could imply addressing the specific constraints (such as credit and training) of poorer entrepreneurs and workers.
- **Focusing cluster gains to the poor:** identifying key agglomeration benefits for the poor and fostering cooperative strategies.
- **Recognising cluster difference:** identifying winners and losers and ensuring that marginal groups of workers and producers are not weakened.
- **Promoting social protection:** using formal and informal interventions to strengthen social provisioning around poverty concerns relating to health, occupational hazards, vulnerability and risks.
- **Using cluster mapping** to identify key public and private stakeholders for pro-poor policy interventions.
- **Emphasising labour standards** and improved work practices as a pro-poor endeavour within corporate social responsibility.
- **Using a sustainable learning approach** in impact assessment to develop and improve pro-poor cluster programmes.

Through such strategies, cluster development can become a critical policy tool in the struggle to reduce poverty and achieve the UN's Millennium Development Goals.

Further reading

- Nadvi, K. and Barrientos, S. (2004) 'Industrial Clusters and Poverty Alleviation', UNIDO, Vienna.
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- World Bank (2000) *World Development Report 2000/2001: Attacking Poverty*, Washington DC: World Bank.
- Nadvi, K. and Schmitz, H. (1999) 'Clustering and Industrialisation: Introduction', *World Development* vol. 27, no. 9.
- Roche, C. (1999) *Impact Assessment for Development Agencies: Learning to Value Change*, Oxfam, Oxford.

Useful websites

- IDS Globalisation Team (cluster page) www.ids.ac.uk/ids/global/coleff.html
- UNIDO www.unido.org/clusters
- Enterprise Development Impact Assessment Information Service (EDIAIS) www.enterprise-impact.org.uk

Credits

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