Industrial Clusters Promotion as a tool for private sector development: The UNIDO experience in Ethiopia

Policies aimed at boosting the interaction and cooperation of economic actors in industrial clusters might represent a crucial strategy for industrial upgrading and development in poor countries. This policy brief discusses some recent industrial cluster programmes carried out by UNIDO in Ethiopia and highlights the main advantages of cluster policies and the lessons learned.

ADVANTAGES OF INDUSTRIAL CLUSTERS AND THE CASE FOR POLICY INTERVENTION

Industrial clusters, which are defined as the geographic concentration of economic activities producing similar and closely related goods, give scale advantages for MSEs providing relatively easier and cheaper access to resources such as credits and inputs. Industrial clusters include not only the concentration of output producing enterprises, but also input suppliers, output buyers, various service providers and in some cases government and non-governmental institutions (see Figure 1).

Often clusters arise in the economic landscape of several countries in the world as a result of spontaneous agglomeration forces which lead to the co-location of producers of similar products. The reason why industrial clusters have received considerable attention by policymakers in every corner of the world is due to the established fact that these agglomerations provide a wide range of advantages to the enterprises that belong to them (Schmitz and Nadvi, 1999):

- availability of inputs, specialized labor and various services in nearby locations help reduce costs of doing business within clusters;
- the presence of various actors close to each other facilitates easy flow of knowledge and information exchange;
- the trust that naturally develops within clusters helps provide the basis for joint actions (cooperation) to invest in common facilities and facilitate smoother commercial transaction, reducing risk and uncertainty;
- industrial clusters typically lead to large markets that enable enterprises operate at a larger scale arising from the division of labor within a cluster. The available large markets within clusters also provide consumers greater choice and convenience by reducing search cost.

The overall effects of clustering might result in a significant increase in the competitiveness and profitability of enterprises, in particular MSEs which, at least partly, overcome in this way the dis-advantages of their small size.

The rationale for cluster initiatives lies on the existence of several constraints and "market
approach of UNIDO is to initiate joint actions among enterprises in the cluster and various institutions in order to embed a spirit of collaboration and trust that could lead to “a dynamic cluster in which actors can use collective power to innovate their ways of doing business”. In order to achieve this, UNIDO’s cluster development initiative rely on the engagement of facilitating agents, known as cluster development agents (CDAs), who operate as impartial brokers among cluster actors and help producers share information and coordinate their endeavors. Through the employment of CDAs, the cluster development approach of UNIDO try to initiate assistance to natural clusters by: 1) building trust in order to enable cluster stakeholders with different or conflicting interests to work together; 2) fostering cluster governance, often through the establishment of a formal governing body, in order to ensure the sustainability of cluster initiatives; 3) promoting business networks among entrepreneurs who share commercial interests and work together towards shared objectives; 4) institutional capacity building in order to enhance dialogue and collaboration between entrepreneurs and supporting institutions and strengthen the capacity of supporting institutions to provide efficient and effective services.

Following this approach, UNIDO firstly launched a cluster development project in Ethiopia from 2005 until 2009 on MSEs. The program identified four natural clusters in Ethiopia; the Gullele Handlooms Cluster, the Readymade Garments Cluster; the Merkato Leather Footwear cluster and the Mekelle Metal and Wood Works Cluster. See Box 1 for some of the interventions by UNIDO and the results. A second cluster initiative was carried out in 2010-2013, jointly with FAO, as a fundamental component of a larger programme aimed at boosting the Ethiopian edible oil value chain, see Box 2.

Lessons learned from the cluster development approach of UNIDO in Ethiopia:
The interventions have highlighted the need
for having sector specific interventions that would trigger the active participation of stakeholders. The assignment of CDAs to each specific cluster further ensured the assessment of the specific needs of each cluster and to have tailored interventions accordingly. Since UNIDO’s methodology of cluster development is largely based on strengthening trust, the commitment of CDAs throughout the period of the project enabled the development of trust with the local community including the main beneficiaries, clustered enterprises. The strong involvement of public-sector institutions in the program contributed for trust and governance-building in order to assure the continuation of the cluster development initiatives once the project has phased out. In addition, the close collaboration between public and private sector stakeholders in the project helped to draw a joint plan and pooled efforts and resources together that were essential for an efficient delivery of various services and supports to enterprises. The cluster development program by UNIDO also worked closely with various support institutions. By supporting and building the capacity of various support institutions, the project was able to assure the delivery of problem solving and quality services to enterprises. The more recent ‘Ethiopia Edible Oil Value Chain Enhancement’ programme suggests the importance of combining cluster development initiative with policy actions aimed at promoting agro-business value chains (see UNIDO 2013 for more details).

**Cluster development strategy of the Government of Ethiopia**

In line with the current MSE Development Strategy of Ethiopia, the government formulated a Cluster Development Strategy (CDS) in January 2011. The main objective of the CDS is to alleviate problems of working and selling premises often faced by MSEs through the construction of standard working and selling premises where a number of enterprises that work on similar and closely related goods can enter and operate. The provision of premises to similar and related enterprises is believed not only to resolve their space limitations but also help create markets, facilitate technology transfer and induce network and collaboration among enterprises. According to the CDS, various support packages will be given to MSEs operating in government built premises such as training and information about saving and access to credit, business development services, industry extension services, training and linking enterprises with big companies. See Box 3 for the nature and types of government created clusters.

**Lessons learned from government cluster development policy:** Case studies conducted on existing government created clusters reveal that although there were few positive outcomes where the working premise problem of enterprises were solved, in general it was challenging to create the envisioned advantages of clustering from the intervention. Despite the highly subsidized rent and in some cases free

**BOX 1: CLUSTER DEVELOPMENT INTERVENTIONS BY UNIDO IN ETHIOPIA: SELECTED EXAMPLES**

**Technology upgrading in Addis Ababa Ready Made Garment Cluster**

The ready-made garment cluster in Addis Ababa comprises of 26 large-scale and more than 4000 small scale firms producing garment, embroideries and knitwear. Poor access to modern and appropriate machinery and equipment was identified as the main problem facing enterprises in the cluster. In order to facilitate technology up-grading, workshops were held with firms in the cluster and various equipment suppliers in order to facilitate network formation and raise the awareness of producing firms about the available technologies. As a result, increasing interest and orders in machinery and equipment from machinery suppliers was seen in the cluster. In addition, business development services were provided by the supplier in terms of providing training and advice related with the new technology (UNIDO, 2010).

**Skill upgrading in Addis Ababa handloom cluster**

The handloom cluster in Addis Ababa comprises of weavers that have migrated from rural areas of the country who have acquired the skills and know-how through informal and on the job trainings. It was identified that enterprises in the cluster lack product development skills and produce traditional cloths with little innovation, product diversification and value addition. In order to address the issues related with skills, a one month skill-upgrading training was given in the areas of raw material selection, and development of new products and design for selected enterprises in the cluster. As a result of the training, more weavers became aware of the need to diversify their product range and improve their designs in order to remain competitive (UNIDO, 2010).

**Network and subcontractor development in metal and wood work cluster in Mekelle, Tigray**

The metal and wood work cluster in Mekele, Tigray includes more than 250 enterprises and 24 cooperative associations. The main products of the cluster include household equipment, office furniture, agricultural implements, construction materials, and simple machines. The cluster experienced an exponential growth in the period 2001 to 2005 due to public procurement measures and the growing demand for machinery fuelled by a boom in agricultural production. Starting from 2005, however, the cluster underwent significant decline mainly due to shrinking market access. In addition, enterprises in the cluster faced increasing difficulties in meeting quality requirements which excluded them from participation in tenders and public procurement. In order to help the cluster regain competitiveness, UNIDO promoted the development of networks among enterprises in the cluster and initiates subcontracting agreements with one of the largest manufacturers of metal products in Ethiopia, the Mesefin Industrial Engineering (MIE). MIE provided training within its facilities to MSEs in welding, drawing, design and quality control among others (UNIDO, 2010).

**BOX 2: ‘ETHIOPIA EDIBLE OIL VALUE CHAIN ENHANCEMENT’ PROGRAMME: A SHORT DESCRIPTION**

Ethiopia has huge potential for scaling up its production of edible oil: favourable agro-climatic conditions for increased oil seeds cultivation, the labour intensive nature of the sub-sector, conducive business environment, the willingness of the oil seed crushers to work at full capacity and the high local demand. Despite this potential however, the edible oil processing industry remains underdeveloped. Main constraints are: low production, poor quality of seeds, inadequate trading infrastructure and poor agro-processing facilities, weak business development services for upgrading the processors and limited access to local and international markets. Weak linkages among the chain’s actors and lack of working capital also constitute major obstacles. A Joint-Programme was carried out by UNIDO, ILO and FAQ - sponsored by the MDG-F fund – between 2010 and 2013 with the following goals: “enhance the sustainable supply of oil seed raw material at desired quantity and quality, promote efficient processing capacity and improve the access to markets”.

The programme was conducted in several districts in two regions; Oromiya and Amhara and focused on two high-potential oil seeds; niger seed and linseed.

The cluster initiative was targeted to edible oil processors and several measures were undertaken in order to improve their technological and entrepreneurial capabilities, establish a formal organization for carrying out collective actions and investments and improve the quality of products and market access (UNIDO 2013).
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Asia, the Middle East and Latin America.

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CMI Briefs can greatly contribute also by identifying weaknesses in existing cluster value chains and attract investors and businesses to fill those gaps in order to strengthen the forward and backward linkages. However, it is crucial to take into account the possible heterogeneity in enterprise performance, capabilities and production history and avoid to apply a ‘one size fits all’ cluster policy in all sectors and context. Like in any policy action, cluster policies should be tailored on the existing (and evolving) local circumstances of the different clusters.

REFERENCES


