Making Value Chain Development Work for the People

A Primer

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Philippine Legislators' Committee on Population and Development Foundation, Inc.
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March 2013

This publication was produced by PLCPD Foundation, Inc. with assistance from ICCO Kerk in Actie. Unless indicated, the contents of this publication do not necessarily reflect the official position of ICCO Kerk in Actie.

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Photos courtesy of Task Force Mapalad (TFM), Sentro ha Pagpauswag ha Panginabuhi (SPPI), and PLCPD.

Since the world entered the era of globalization, the challenge in penetrating the global market has began. For governments and the development community, this posed an opportunity to maximize globalization and use it towards the attainment of poverty reduction contributing towards the achievement of a better quality of life -- where people are afforded equal opportunities in the aspects of economics, health, and politics, among others.

The principles of Value Chain Development (VCD) have been very instrumental in attaining these objectives. Understanding VCD facilitated government and civil society interventions in ensuring participation of small-scale producers in the international trade – penetrating the international market.

But the task, as in any other development intervention, is not very easy. It requires adequate knowledge in trading, engaging with the various actors in the value chain, capacity building, and careful study of production risks and market availability. Most especially, inasmuch as being involved in the chain is required, especially during the early stages of the venture, value chain facilitators must also have an effective exit strategy and be able to implement the strategy.

In the Philippines, a number of VCD interventions have been undertaken by several development institutions working with grassroots organization that are usually engaged in the agriculture sector. Capitalizing on the available resources in the community and agricultural skills of its members, many VCD interventions have been successful on the production side. Penetrating the international market, however, remains to be a challenge. Be that as it may, it is still valid that VCD can be an effective instrument in poverty reduction in concrete terms.

For this reason, this primer seeks to discuss the fundamental concepts of VCD to help leaders and policymakers get an idea of how it works and later on outline the roles of various sectors, especially leaders and policymakers, in ensuring that VCD interventions do contribute in poverty reduction and sustainable economic growth.

1. What is a value chain development (VCD)?

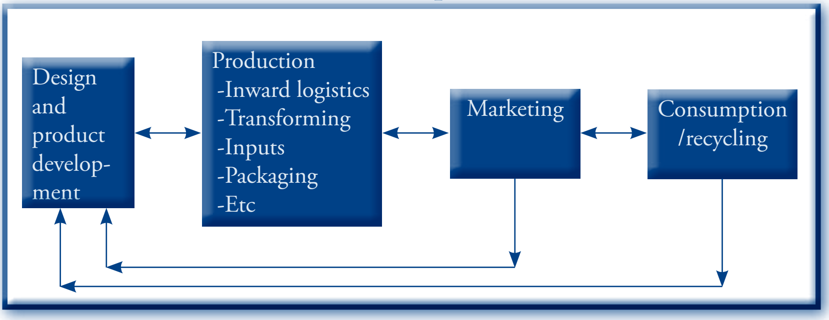
The value chain describes the full range of activities which are required to bring a product or service from conception, through the different phases of production (involving a combination of physical transformation and the input of various producer services), delivery to final consumers, and final disposal after use. (Morris and Kaplinsky, 2001) While the definition of a value chain may sound too technical, it is important to note that value chain development basically considers the contribution of every actor in the chain in the development of the product and the benefits of developing the products to the actors in the chain.

For years now, value chain development or VCD, has been a crucial entry point for development workers to contribute in achieving the objective of reducing poverty. By supporting poor communities, efforts in varying degrees have rendered the beneficiaries capable actors in the value chain – making them able to avail of opportunities in local, regional, and even international trading systems.

For development interventions, the Interchurch Organization for Development Cooperation (ICCO) spells out that value chain developments should contribute in achieving sustainable development and that sustainable development is operationalized in the framework of "Profit, Planet, and People." More clearly, the framework means:

1. To create longer term economic or business impact (Profit);
2. To nourish the environment (Planet); and
3. To advance the less favored groups in society or the world (People).

Four links in a simple value chain



IDRC, 2002

In the Philippines, VCD endeavors are generally directed at increasing the capacities of agricultural communities to participate in the chain. This involves increasing the quality of their product, organizing communities to build a bigger base of produce, increasing their awareness in trading systems, creating an enabling environment for the chain, and directing communities towards sustainable engagement in value chains, among others.

VCD is highly associated with the concept of governance as value chains may create environmental pressures. Furthermore, as various actors are involved in the chain, it is expected that relations and powers within and among value chain actors will affect the chain, either positively or negatively. Both concerns are very real in the Philippines considering the agricultural nature of VCD interventions and the traditional norms in the country in terms of powers and relationships.

2. What are the important aspects of VCD?

To ensure that VCD interventions are advantageous to the target beneficiaries, it is important to take note of several aspects. Kaplinsky considers three important aspects in VCD:

1. *The extent of access operators have to a value chain (barriers to entry)*

   Lowering the barriers to entry is perhaps the main concern of VCD interventions. It is in this aspect that the beneficiaries are able to decisively and actively participate in value chains. This can be achieved by ensuring financial sustainability, developing their technical skills, and establishing systems to ensure the quality of products, among others. What's tricky with addressing the concern on barriers to entry is that these should not be so high in the value chain in order for the target beneficiaries to be able to participate in the chain but these should also be high enough to ensure that target beneficiaries are able to engage meaningfully in the chain.

2. *The extent to which an operator can influence the chain or other operators (governance)*

   It is significant that powers and relationships in a value chain contributes in the development of the chain and not otherwise. This calls for good governance mechanisms to ensure that operators can influence the chain or other actors in a way that does not result in conflicts. To effectively undertake this, a considerable knowledge in how the value chain works and the characteristics and behaviors of the actors in the chain is significant. It is also important to have substantial knowledge of the market and the trading system and to ensure that the governance mechanism provides an enabling environment to the value chain.

3. *The extent to which a value chain can be developed (upgrading)*
   Basically, upgrading is a process by which actors in the chain are able to enhance their competitive position in the chain. This is very important for VCD as beneficiaries need to see ways to establish an essential role in the chain in order to sustain their participation in it. This can be done in various ways (i.e. process upgrading, product upgrading, functional or intra-chain upgrading, and inter-chain upgrading) but whatever type of upgrading one chooses, it is important to have a clear analysis on the feasibility of the upgrading that an actor will opt for – for example, taking into consideration the available technology and skills of the beneficiaries.

3. What is Value Chain Analysis?

Value chain analysis is a tool that is being employed by VCD practitioners to assess the various aspects of the value chain including the processes by which a product is developed, the actors within the chain and their relationships, and the market, among others. For those who have engaged in value chain analysis, the process has guided them in defining and concretizing their development interventions. For all the actors in the chain, on the other hand, value chain analysis allows them to study their weaknesses and strengths in the chain and therefore make adjustments to address these weaknesses or bank on these strengths (e.g. outsourcing of functions where their competency is lacking).

Based on various VCD experiences, undertaking value chain analysis provides the following benefits[1]:

- Recognizes the lack of economic power of target beneficiaries compared with more powerful firms setting the 'rules of the game' in the value chain, and how this constrains their choices;
- Has economic viability and commercial sustainability at its core because of its market focus;
- Is a powerful diagnostic tool that can identify critical issues and blockages for specific target groups – and provides a framework for interventions to change the circumstances of the resource-poor; and
- Identifies the core rents and barriers to entry that determine who in the value chain benefits from production.

In the context of rapid globalization, value chain analysis has become more important. According to Kaplinsky, Raphael and

[1] Mitchell, Jonathan and others. Upgrading Along Value Chains: Strategies for Poverty Reduction in Latin America. *Trade and Poverty in Latin America, Briefing Paper, December 2009*. COPLA, 2009.

Morris, the following are the three main reasons why:

1. With the growing division of labour and the global dispersion of the production of components, systemic competitiveness has become increasingly important;
2. Efficiency in production is only a necessary condition for successfully penetrating global markets; and
3. Entry into global markets which allows for sustained income growth – requires an understanding of dynamic factors within the whole value chain. (IDRC, 2002)

4. What is Value Chain Facilitation?

Value chain facilitation is simply assisting in making value chains successful. This is the role most often played by development institutions to make way for the target beneficiaries to engage in value chains. By doing so, target beneficiaries, and therefore the value chain facilitators, become effective contributors in achieving economic growth and poverty reduction.

Value chain facilitation, for that reason, is not an easy task. It is important that value chain facilitators are credible and acceptable to all actors in the chain to be able to facilitate the chain effectively. If such is not met, value chain facilitators may fail from achieving the task. In addition, value chain facilitators should be able to distinguish the precise role or

roles that they are required to perform in the chain so that efforts are focused and sustainable. These roles can be identified in the course of value chain analysis.

Based on its vast experience in VCD, ICCO defined four essential roles in VC facilitation[2]:

- matching and connecting (as against full brokering where a broker makes the deal and gets paid out of it which is more of a chain actor role);
- bridging interest differences (one may have pro-poor biases but transparency and objectivity should prevail);
- coaching at chain level only (as against capacity building which, although useful, is not part of VC facilitation); and
- stimulates capacity building processes where needed (catalyst rather than implementer).

ICCO also pointed out guidelines for development institutions when engaging in value chain development.[3] These guidelines were identified by the Donor committee for Small and Medium Enterprise (SME) development. These are:

1. focus on changing processes and behaviour and not just solving identified problems;
2. avoid taking up functions that are part of the business cycle (.i.e. take care not to substitute local entrepreneurs);
3. work with existing commercial initiatives and do not establish new marketing channels that are not sustainable, even if they offer fairer terms for farmers during the project life span;

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[2] ICCO. *Paper on Value Chain Analysis and Value Chain Facilitation.* (modified)
[3] ICCO. *Value Chain Development in ICCO/Kerkinactie.* Netherlands: ICCO, 2010.

Interventions will always have to take into account the specific situation and context, but the following general rules should apply:

- VC outsiders (i.e. people who have no intrinsic role to play in a VC, such as development agencies) should only intervene where they can add real value to existing capacities of VC operators and VC service providers, and only if there is a real demand. The motivation and goals of development agencies must be communicated clearly towards the VC players.
- Development agencies should intervene only in support of existing local operators, entrepreneurs or organizations that may become potential change agents. Changes will only be sustainable if they are implemented and owned by local entrepreneurs, local public agencies and / or local civil society.
- VC development itself can be a commercial venture. Development agencies or publicly funded agencies should avoid to assume roles that can be commercially operated, and thereby sabotage the emergence of truly sustainable and viable enterprises.
- Before intervening in any value chain, development agencies must have a minimum understanding of markets, operators, informal rules and laws, embedded and other services.

Value Chain Development in ICCO/Kerkinactie, 2010.

4. do not set up interventions which compete with existing business and other services, unless you are very sure about their viability and sustainability; and
5. address market imperfections and withdraw when markets function.

5. Why should a participatory approach be considered in VCD?

As in all development interventions, it is most crucial that a participatory approach is ensured in order for the target beneficiaries to have a sense of ownership of the undertaking. For poor households (communities), their assets and their ability to accumulate and use those assets effectively, are critical to their participation in value chains and their ability to benefit from participation in the chain.[4] That is primarily the reason why the participation of target beneficiaries in value chains is usually defined by what resources are already at hand or what activities they are already engaged in (e.g. agricultural activities).

The value chain approach necessitates consideration of all actors in a market system—the private-sector firms in the value chain from input supply through to end market retailers, service providers, and public and private decision-makers in the enabling environment—and is therefore intrinsically participatory to some degree. However, emerging best practice in value chain development recommends a greater level of participation: explicitly engaging key actors from

4 McKay, 2009. As cited in "Under what conditions are value chains effective tools for pro-poor development? *A Report for the Ford Foundation*." D. Seville, A. Buxton, and B. Vorley. IIED, Sustainable Food Laboratory, 2011.

different levels of the value chain throughout the project lifecycle and devolving to them a high level of goal setting, decision making and responsibility for action.

The degree of stakeholder participation ranges from low—where there is consultation with stakeholders through questionnaires and interviews; to high—where stakeholders have the opportunity to contribute substantially to the formulation of an intervention, are in part responsible for its implementation, and are involved in the selection of criteria by which success is measured. This range generally correlates to the level of buy-in or commitment to the process: from a minimal, passive interest in the intervention, to ownership of and a commitment of resources to the intervention.

The adoption of participatory approaches is hindered by a number of factors. First, while the need to obtain stakeholder buy-in has often been reiterated, practical steps to ensuring participation and local ownership have not been clearly articulated.

Second, there is sometimes concern that promoting the participation of a wide range of actors is a resource-heavy distraction from the real business of stimulating commercial transactions, especially when project targets are ambitious and timeframes short.

Third, high-profile stakeholders are sometimes asked by numerous donors and implementing agencies to participate in surveys, interviews and workshops, and are consequently reticent to commit their time to yet another development initiative. In such cases, participation can become less strategic, with heavy representation by small-scale producers (especially if provided incentives such as per diems or the expectation of project subsidies) and little or no involvement by private-sector decision-makers and change agents such as larger-scale processors, end market buyers, exporters or even innovative producers.

Participatory Approaches to Value Chain Development, USAID

6. Why should development organizations get involved in value chains?

Value chain development provides us opportunities to help target beneficiaries engage the market and use it in such a way that it contributes to poverty reduction and economic growth. In the Philippines, small-scale producers, especially in the agriculture sector which is predominant in the country, have little or no links to the market rendering them vulnerable in the trading system. Investing in VCD facilities can link the poor sector of the society, help them establish their products in the market, and hopefully embark on a sustainable venture.

ICCO outlines the following reasons why development organizations need to get involved in value chains:[5]

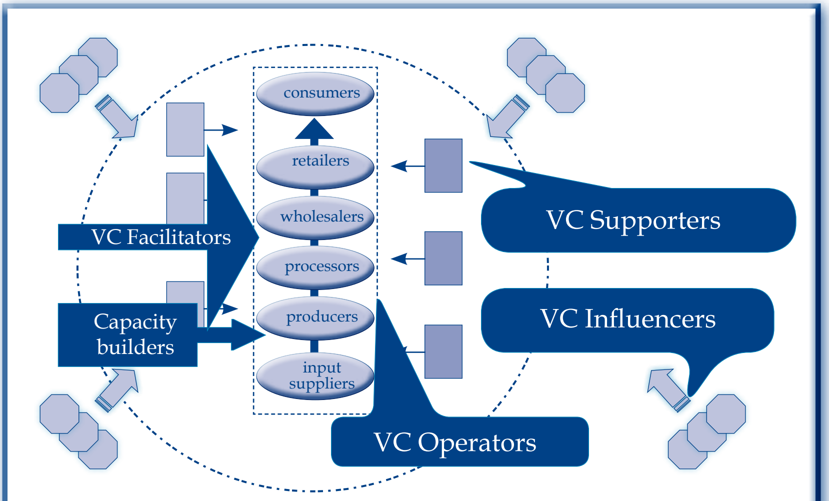
- Some people (particularly our target group) need support for becoming operators in existing value chains (to counter exclusion);
- More important than belonging to a value chain is the role people play in it, i.e. their negotiation power in the value chain; and
- Some operators are stuck in value chains that exploit low income possibilities. They require support to explore new opportunities by strengthening one operator in value chain there is the possibility of creating competitive advantages for the whole system. In such a case a large number of people competing in local, regional or global markets can benefit from these advantages.

[5] ICCO. Value Chain Development in ICCO/Kerkinactie. Netherlands: ICCO, 2010.

However, development institutions should be clear in their objectives when getting involved in value chain development – if such strategy would be best in reaching their core objectives, mission, and vision. An assessment of the core competencies and mandates could be done to define whether it is fitting for the institution to embark on VCD efforts.

It must be clear, on the other hand, that the role of development institution in value chain development is not constant. The ICCO Strategy Paper points out that value chain facilitation should address market imperfections and withdraw when markets function. It is therefore important for development institutions to be constantly conscious that their role in value chain development may be dissolved as the chain actors become more capable and the chain becomes more sustainable. Considering this, an exit strategy should be formulated in such a way that the termination of partnerships does not affect the chain.

Schematic overview of actors in a value chain



Adapted from Hans Posthumus Consulting 2009

Source: Value Chain Development in ICCO Kerkinactie, 2010

7. What is the role of the private sector in VCD?

While VCD facilitation is usually undertaken by development institutions, the private sector can also undertake such endeavors. These are often conducted under the corporate social responsibility (CSR) programs of companies through their corporate foundations – or whatever CSR arm is in place in the company.

Through CSR programs, companies are able to provide assistance to target beneficiaries usually linked to the kind of industry the company is involved in. Be that as it may, these interventions still contribute in the efficiency of the chain and in achieving poverty reduction and economic growth.

Having different takes in the value chain and greater resources, the private sector can actually position itself at different points in the chain, making it a vital player. The challenge therefore is to influence the private sector to be more sensitive in other advocacy issues related to the development of the value chain such as gender, environment, and participation, among others. This should make their engagement in the value chain more meaningful, effective, and contributory to sustainable development.

8. What is the role of policymakers in VCD?

Successful VCDs do not rely solely on the actors in the chain. An enabling environment must also be established in order to ensure the sustainability of the chain. This includes the availability of natural resources (and therefore the ability to sustain these), support system of the actors in the chain (e.g. financial institution), and policies at different levels of government (i.e. local and national levels), among others.

This is where policymakers play a crucial role. Policy formulation supporting value chains are very critical to ensure that gains are sustained. At the local level, this may mean policies that provide support to, or protects the rights of, organizations involved in VCD; inclusion in the programs of the local governments; or support from local government agencies involved in the industry, among others. At the national level, this may mean policies or programs instituting regulatory mechanisms to ensure that the rights of the stakeholders are protected, benefits are secured, and product quality is guaranteed.

This clearly points out that working within the realms of policy advocacy is a necessary undertaking for VCD actors and facilitators. Ensuring that policy champions are developed at the local and national legislature will provide greater advantage that will contribute in ensuring the sustainability of the chain. On the other hand, this also provides legislators a venue to widen their perspectives in terms of economic growth, poverty reduction, and sustainable development. Also, engaging actors in the value chain provides policymakers additional avenue to promote their advocacies.

Working on enabling environment

The environment for value chain development is influenced by people, organisations and institutions that are responsible for setting up and managing the regulatory framework. A favourable and enabling business environment provides economic and political stability, ensures low costs for business transactions, and allows for efficient business operations, which lead to greater innovation and creativity. Development agencies can influence an enabling business environment for VCD in four different ways:

1. Enable local operators to lobby at the policy level through the local government or civil society (e.g. chambers of commerce).
2. Influence public and private local operators to come together and define a regional policy favourable for businesses and value chains operating in their area.
3. Support governmental agencies with technical assistance, so they are able to offer a demand oriented and efficient service to rural entrepreneurs (bureaucracy can be a business killer).
4. Gain experience through small field-level projects (action research and R&D) and use the lessons learnt for direct policy dialogue. (SDC 2007, p 18)

Value Chain Development in ICCO Kerkinactie, 2010

9. What have been the lessons so far?

Various VCD undertakings have already been conducted worldwide supported by different development institutions and involving diverse industries. In the Philippines alone, various VCD undertakings have been carried out among the muscovado, seaweed farming, banana, and organic rice industries, among others. Some of these have succeeded and are still operational; some have failed to achieve sustainability.

Accordingly, a number of research projects have already been undertaken to assess these various efforts worldwide. The following are lessons identified in some of these researches:

Upgrading Along Value Chains: Strategies for Poverty Reduction in Latin America. Trade and Poverty in Latin America (COPLA), Briefing Paper, December 2009.

VALUABLE LESSONS

Emerging from our studies are several key lessons for policymakers and practitioners seeking to assist the entry, participation and upgrading of the rural poor in value chains. Beyond taking a broader view of upgrading strategies, we underline the importance of:

1. **Clarity on the rationale for the (possible) intervention:** In particular, it is important to distinguish whether the primary aim of an intervention is to reduce poverty or to simulate growth in the local economy. Whatever choices are made regarding the aim of the intervention, it should be accepted that, as with any sustainable private sector development project, the non-poor will necessarily gain from the intervention as well as the resource poor.
2. **Selecting an appropriate value chain to develop, with suitable demand requirements:** The choice of value chain has important implications for the barriers to entry for the poor and for the sustainability of the initiative.

3. **Rigour in applying research methods:** Value chain analysis and development requires robust evidence-based research of the current market system and a clear appreciation of which blockages poor people can overcome and how. Poor quality research can result in project failure, with disastrous consequences for target beneficiaries.
4. **Defining appropriate interventions:** It is important that the interventions proposed for value chain development spring from, and are constrained within, the logic of the VCA and the market development approach.
5. **Identifying the key rents that allow poor producers to participate gainfully and sustainably:** Participation in markets does not, in itself, provide for sustainable income growth. The key goal is to locate rents in the chain that can be captured by poor people and that are unlikely to be eroded through time as a result of competition.
6. **Understanding about barriers to entry:** The trade-off in developing barriers to entry which are not so high that all the poor are excluded, but which are sufficiently high to allow participants to gain rent, lies at the heart of pro-poor value chain development.
7. **Avoiding obsessing about the production node in agricultural value chains:** Poor people engage with value chains at all nodes as producers, intermediaries, workers and consumers. It is not necessarily the case that the largest pro-poor impact should centre on the production node.
8. **Analysing the enabling environment carefully:** A careful analysis of the operation of value chains will often identify state failures as well as market failures. It is not unusual for the main impediment to poor people engaging with value chains to be the state that purports to represent them.
9. **Taking action:** Upgrading the position of poor people in value chains on a sustainable basis is not easy. It requires the cooperation of many stakeholders in the chain, an inclusive policy process, which must include the lead firms, and a pragmatic and non-ideological approach towards value chain restructuring.

Participatory Approaches to Value Chain Development, USAID

RECOMMENDATIONS AND LESSONS LEARNED

Be explicit about how the participatory approach will be applied. Participation does not happen automatically: project implementers must be proactive in applying a participatory approach. Staff must be prepared to let stakeholders take the driver's seat, realizing that stakeholder buy-in is an incremental process; and donor expectations must be managed. Participatory "monitoring benchmarks" should be used throughout the project cycle. The goal of the approach should be kept in mind: not participation for its own sake, but to foster firms working together to increase industry competitiveness

Ensure that donor support is appropriate. Donor funds must be flexible and responsive to stakeholders' needs, and sufficient in terms of amount and duration to enable stakeholders to continue to implement the competitiveness strategy. Just because a process is participatory does not necessarily imply that it can be left to the stakeholders without assistance, particularly if value chain actors are geographically dispersed.

Gain the interest and buy-in of key actors. It cannot be assumed that important stakeholders will want to use their scarce time and resources to participate in a value chain development initiative. Facilitators must identify vital issues or "hooks" to show the opportunity costs of non-participation. Value chain actors need incentives to be involved, but the goal is to tap into existing energy, resources and aspirations rather than create dependency through temporary subsidies. An example of a typical "hook" is addressing quality issues: actors want to participate because they recognize that low quality is stopping them from achieving higher returns.

Identify common interests to facilitate the development of trust. Value chains are often characterized by adversarial relationships and mistrust, so projects must conduct activities to promote the development of trust - or at least of understanding - among stakeholders, to facilitate information sharing and cooperation. It is important to clarify with stakeholders that the purpose is not a re-distribution of margins from one group of actors to another. Rather, the value chain development process focuses on stakeholders' shared interests. However, care should be taken not to foster collusion that limits upgrading. Effective competition drives innovation.

Build MSEs' capacity to participate. If MSEs are to effectively participate in a process that involves other, more powerful stakeholders then it is likely that projects will need to help them to become more confident and articulate. While not the starting point, empowering producers can be critical to a successful value chain project.

Develop a communication strategy. Having a clear plan of how to communicate project objectives and the results of stakeholders' activities is important, particularly to attract key stakeholders and keep their interest and commitment. The media can be strategically engaged as a partner that is involved from inception. Other mechanisms for communication include conferences, sector-specific seminars, case studies and written materials.

Build the capacity of facilitators. Strong facilitation skills are essential to encourage and maintain stakeholder participation. Facilitators must be flexible and have a deep understanding of both the project's aims and the local context. A consultant with industry-specific expertise can add credibility to the project team, but must be willing to serve as a resource rather than lead the analysis, strategy development and implementation processes.

IFAD on the important lessons related to two VCD projects: (1) The Department of Agrarian Reform (DAR)/IFAD Northern Mindanao Community Initiatives and Resource Management Project (NMCIREMP); and (2) the Cordillera Highland Agricultural Resource Management Project (CHARM)

Several important lessons related to sustainability emerge from the two projects:

1. There is a theoretical imbalance between the number of communities reached and the sustainability of the effort, given the local context and budget. In the quest to serve as many beneficiaries as possible, projects often end up spreading staff too thin, having minimal contact with community members and institutions, and unable to monitor areas that need shoring up.
2. NGOs should be treated as partners and not contractors, and should have a large stake in project planning and implementation. Their work needs to be appropriately phased so that community-led processes are well along before other dimensions of the programme take place.
3. Gains in natural resource management (NRM) are associated with livelihood systems. Where there is a clear link between NRM and livelihoods, people will become engaged in NRM activities if they see a potential short-to-medium term return. Where returns are longer (watershed rehabilitation, agroforestry, soil regeneration) there has to be an entirely different strategy and set of expectations. In addition, moving from the resource planning stage (usually a resource management plan or a land use plan) to the activity or implementation phase has proved challenging in almost all projects. For one, the time horizon for observing measurable change is usually much longer than with other project components, so that NRM activities quickly get out of sync with other activities. This often results in communities losing momentum or interest in the NRM sector.

4. Projects need diversified instruments and strategies to achieve desired change. They must have strong leadership and make use of local knowledge and experience. The different components of the project have to come in and out of play at the appropriate time, and any missing factor will be noticed in the outcome.
5. NRM must include the promotion of indigenous knowledge systems and practices, natural resource management and enhancement, and the use of natural resources in production systems. These concepts have to be introduced early and in a manner that will ensure participation in resource management (especially off-farm) in the long term.
6. Risk mapping should be made a prerequisite and be instilled as part of the project design process. Sustainable strategies for remote areas and areas with diverse groups need a risk management lens to identify what kinds of risk management capacity needs to be in place at the household and community level, what types of safety nets need to be available at various levels in case local capacity to manage risk becomes overwhelmed, and what kinds of social protection mechanisms need to be in place at the provincial level in case the lower levels are not able to respond to a shock (productive safety nets to rebuild assets).
7. Foundation processes for sustaining gains need to be instituted from the beginning of each project. Improved participation, ownership and wider capacity-building would contribute to a greater likelihood of sustainability. Ensuring that these foundation processes are recognized and integrated into project components would be facilitated by the development of a sustainability plan (replacing the term 'exit strategy') during Year 1 of any project.
8. Attitudinal and behavioural change regarding protection of the environment was brought about through links with cultural traditions and by first promoting self-interest (e.g. protecting sources of potable water) rather than moralistic entreaties regarding biodiversity or heavy enforcement and stiff penalties.

9. As is common, maintenance emerged as an issue in sustainability. No fee structures were implemented for maintenance and communities remain mostly reliant on local government for maintenance funding, which is both bureaucratic and time-consuming. More creative combinations of maintenance strategies are required to ensure sustainability, and sustainability plans are crucial for defining these strategies early in the project.

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