

Programa de Desarrollo Local y Territorio

FLACSO, Ecuador

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Value Chain Promotion and the Role of Social Capital in

Ecuador: an Illustrative Study

Jennifer Hebets

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Table of Contents

I. Introduction	5
II. Literature Review: Social Capital and Local Development	8
<i>a) Defining Social Capital</i>	9
<i>b) Conditions for Productive Social Capital</i>	14
<i>c) The Role of Social Capital in Development</i>	17
<i>d) How to put Social Capital to Use in Developing Countries for Practitioners</i>	19
III. Local Economic Development Theoretical Background	25
<i>a) Defining Global Value Chains</i>	25
<i>b) How Value Chains Affect Local Economic Development</i>	29
<i>c) Value Chains in the New Globalization Context</i>	30
<i>d) The Role of Relationships and in Local Economic Development and Value Chains</i>	31
<i>e) The Role of Cooperation in Global Value Chains</i>	35
<i>f) The Role of Trust in Local Economic Development</i>	38
<i>g) Social Capital in Value Chains</i>	41
<i>h) Power Dynamics and Relationships in Value Chains</i>	45
<i>i) Value Chain Governance and the Role of Relationships</i>	46
<i>j) The Role of the Public Sector and Outside Actors (i.e. donors)</i>	47
<i>k) In Conclusion</i>	49
IV. Methodology	51
V. The Case Study: The Paja Toquilla Industry in Cuenca	58
<i>a) Introduction</i>	58
<i>b) Background on the Panama Hat in Ecuador</i>	61
<i>c) Defining the Problem: Description of the Region and Target Population</i>	63
<i>d) History of Paja Toquilla Sector in Cuenca</i>	64
<i>e) The Panama Hat Productive Chain</i>	66
<i>f) USAID Red Productiva/ Productive Network</i>	69
<i>g) Program Explanation</i>	71
<i>h) The Panama Hat Exporters</i>	73
<i>i) Serrano Hats</i>	73
<i>ii) Homero Ortgea</i>	73
<i>iii) Kurt Dorfzaun</i>	74
<i>iv) Bernal Hats</i>	74
<i>i) The Weavers</i>	75
<i>j) Ságitta Consulting</i>	78
<i>k) Government and Non-Profit Actors</i>	79
<i>l) Challenges to the Industry Prior to the Cluster</i>	79
<i>m) Vision of the Cluster and Level of Commitment From Actors</i>	82
<i>n) Social Capital Analysis: Relationships Between Actors</i>	85
VI. LED Analysis	90
VII. Project Analysis	95
VIII. Return to Cuenca Ten Months Later	98
IX. Conclusions	101
Bibliography	105

Annex I	110
Annex II. Value Chain Map of the Ecuadorian Paja Toquilla Hat Industr	116

I. Introduction

Have you ever touched a straw hat that was woven so tightly that its texture felt like soft Egyptian cotton? If you have, you probably then proceeded to glance at the price tag and gasp at a number of \$500 or more. Have you ever taken the moment to closely examine an straw hat and consider how many hundreds of row of straw have been laced together to create such an intricate, smooth pattern? If you have, you may have considered whose hands they were that maneuvered the fine strands for hours and days on end to create such a beautiful work. Those hands were more than likely the hands of a woman living in a place far away from the department store in New York or San Francisco where you stand holding her work. She is probably a woman whose only income comes from weaving this hat for less than \$10 a piece living in the beautiful and richly diverse country of Ecuador. In the following pages this study will take the reader on the journey of this hat and the pains and gains it has caused for each person whose hands it has passed through along the way. These pages will attempt to reveal the reasons why some people have been able to benefit more from these beautiful works of craftsmanship and the actors whose interventions attempt to disseminate these benefits.

Ecuador is a country endowed with a profound stock of natural and cultural resources. In the past twenty years the country has seen amazing improvements in GDP, poverty reduction, health, infrastructure, and internal industry. It is also the home to some of the most innovative foreign assistance programs in South America seeking to draw upon global markets to enhance revenue for local producers and therefore increase local incomes. On the other hand, Ecuador has witnessed more than its fair share of foreign and national assistance programs that have failed to have a lasting impact on the lives of the country's poor.

In the following investigation I seek to consider one particular program which has sought to promote Local Economic Development through strengthening of a local value chain. The program has been implemented through the efforts of the United States Agency for International Development and utilizes market-based strategies. Through an in-depth analysis of the program I seek, specifically, to understand the role of social capital. Ultimately, this investigation seeks to answer the question: Does social capital play a significant role on the local level in value chain and cluster poverty-reduction programs? Through a close analysis of this program funded by the United States Agency for International Development in a historically, economically and culturally dynamic regions of the country; we will have the opportunity to understand in-depth a program aimed at increasing incomes for local producers using market-based strategies.

In the following pages I will review the prominent authors in the fields of social capital and local economic development. In the vast pool of knowledge that exists regarding theories for promoting economic growth on a local level; the consensus among most authors is that the capacity amongst local stakeholders to meaningfully contribute to a program plays an essential role in the success of a program. Furthermore, most authors suggest that the more a community is able to organize internally, the more capable they will be to translate that organization into collective efforts to benefit the community as a whole. This theory has been proven in the context of a wide range of programs dealing with issues such as microfinance, irrigation, natural resource management, or cultural affairs. However, there exists relatively little research regarding the role of social capital and how it may or may not come in to play when implementing projects with a strictly economic focus. While the research suggests that efforts to integrate local producers with value chains and connect them to value added markets have great

potential; local social conditions for successful implementation of such programs is not yet clear. It could be that the level of internal cohesiveness within a community may have little importance of producers competent in other areas. Or, it could be that low levels of local social capital may inhibit LED programs from reaching their full potential, possibly even exhibiting a causal relationship with unsuccessful LED programs and low levels of social capital or vice versa. Furthermore, social capital is often a byproduct of deep seeded historical socio-cultural conditions. The relation between these often complex local social dynamics and the likelihood of successful value chain integration should be considered hand in hand. However, the current academic literature as well as the current academic literature tends to approach these aspects of local development from within a vacuum, often paying attention to only the social or only the economic situation. This study will attempt to analyze these two crucial aspects under the same light through a careful analysis of the Panama Hat value chain in the region of Cuenca, Ecuador.

Ecuador serves as a fruitful landscape for such analysis for several reasons. Primarily, the academic institutions of the country and throughout the Andean region have long been fascinated with the implications of social capital. Influential authors like Anthony Bebbington and Luciano Martinez and Kevin Healy have made landmark observations on the organizational and social capacity of various Andean indigenous groups. These organizations have turned the attention of the international community to the inequalities and injustices suffered by the indigenous, rural and poor citizens of the country. Because of these movements, the world has begun to understand the complexities of gender and ethnic discrimination and the centuries of indigenous isolation and oppression that many Ecuadorian citizens have endured. Volumes have been written about the historic indigenous movements and their ability to affect national political agendas. These movements are often fuelled by strong local level organizations. Thus, Ecuador

provides a cultural history rich with ethnic identities that have been able to utilize their organizational capacity and broker it in to a significant political voice; ultimately affecting the outcomes of important political decisions.

On the other hand, Ecuador receives one of the highest levels of foreign assistance in the region. Hundreds of millions of dollars have been directed towards efforts to strengthen local economies. As one of the most biodiverse countries on the planet, Ecuador exhibits great potential for mass cultivation of high end agricultural products. In addition, the strong history of indigenous artisanry has significant export potential. For years, foreign donors have invested in these industries in attempts to jump start local economic development. Numerous programs now seek to connect the beautiful artisan sector with the ever increasing tourism sector in order to give tourists to take home a memory of Ecuador while also contributing to local income generation. As a result, Ecuador has been the backdrop for many “success stories” and best practices which have been captured while implementing development projects. The subject of this case study has itself been the subject of many such stories.

The following pages will bring together these two distinct universes of thought in an attempt to understand a local economic development project within a complex social context. In order to do so, the study focuses specifically on one aspects of social context, that of social capital, and one aspect of economic development, that of value chain programs. Before we can go any further, it essential to clearly define the key phrases in this study and reach a clear understanding of the academic landscape upon which this research is based.

II. Literature Review: Social Capital and Local Development

Over the decades the academic literature of social capital and its implications in society have grown exponentially. When James Coleman first began to consider the social and

organizational structure within groups of people the idea was born that social capital can be seen as a form of capital that can be stockpiled and brokered in order to accumulate other forms of capital. Francis Fukuyama describes social capital as “an instantiated informal norm that promotes co-operation between individuals. In the economic sphere it reduces transaction costs and in the political spheres it promotes the kind of associational life which is necessary for the success of limited government and modern democracy” (Fukuyama).¹

a) Defining Social Capital

The first academic research credited for coining the phrase “social capital” is the French sociologist, Pierre Bourdieu. He defined it as “the sum of the resources, actual or virtual, that accrue to an individual or a group by virtue of possessing a durable network of more or less institutionalized relationships of mutual acquaintance and recognition” (Siisiäinen).² James Coleman is known as the pioneer who further expanded upon on the social capital discussion and the first in the field to look at levels of social organization as having an innate value (Coleman).³ The concept of basic neoclassical economic thinking is premised on the assumption that humans make decisions based on rational choice and in order to maximize utility. On the other hand, sociological thought is premised upon the assumption that humans act according to socialized behavioral norms and rules. Coleman was the first to couple these two perspectives and assert that rational action based on individual interest can also play a role in forming social norms and motivating social organization. We then must ask the question: How does social organization affect the functioning of economic activity? According to Granovetter, social relationships are

¹ Fukuyama, Francis. (2001.) Social capital, civil society and development. *Third World Quarterly*, 22(1), 7-20.

² Siisiäinen, Martti. (2000.) Two Concepts of Social Capital: Bourdieu vs. Putnam. ISTR Fourth International Conference: The Third Sector: For What and for Whom? Trinity College, Dublin, Ireland.

³ Coleman, James S. (1988.) Social Capital in the Creation of Human Capital. *The American Journal of Sociology*. Vol. 94, S95-S120.

still under emphasized in explaining economic activity (Granovetter).⁴ The concept of social capital provides space within economic analysis to account for the role of social phenomena such as concrete personal relationships, generating trust, establishing expectations, in creating and enforcing norms. If we consider the theory of rational choice in which each actor has at its disposal certain factors or certain types of capital, then social capital can be considered a particular type of resource available to the actor as well. That is to say that social capital can be defined by its function. As will be discussed in further detail, social capital consists of various aspects, all of which have some sort of social structures and also which serve some sort of purpose or further a goal. Considering that physical capital is created by changes in materials to form tools that facilitate production, human capital is thus created by changes in persons that bring about skills and capabilities that make them able to act in new ways. Social capital, similarly, is formed by changes in relations among individuals resulting in the formation of groups that facilitate actions. The value of this kind of capital results in the ability of groups to generate action of exponentially greater impact than as individuals. Social capital, like other forms of capital, can be productive and can serve to further some sort of goal that would not be possible otherwise. Another unique aspect of social capital is, compared to physical capital which is wholly tangible, and human capital, is characterized by the skills of an individual is less tangible; social capital is even less tangible, for it exists in the relations among people.

As the concept of social capital has gained more and more credibility, even mainstream economists are beginning to pay more attention to social structures. Robert Lucas, the founder of the school of “rational expectations” economics acknowledges the fact that the accumulation of human capital is a “fundamentally social activity, involving groups of people in a way that has

⁴ Granovetter, Mark. (1983.) The Strengthening of Weak Ties: A Network Theory Revisited. *Sociological Theory*, Vol. 1., 201-233. State University of New York: Stony Brook.

no counterpart in the accumulation of physical capital” (Putnam).⁵ Just as physical capital and human capital facilitate productive activity, social capital does as well. For example, a group within which there is extensive trustworthiness is able, in theory, to accomplish much more than a comparable group without that trust. Once social capital is identified within a social structure, it become necessary to analyze how this resource can be used to facilitate productivity and how it can be brokered to obtain further benefits or goals.

Coleman identifies three forms of social capital that can be brokered and converted in to other forms of productive capital. First, he analyzes structures based on “trustworthiness, obligations, and expectations” (Coleman).⁶ This structure implies that actors are in a constant process of lending and owing tangible resources amongst one another. This form of social capital depends on trustworthiness within the social environment, which means that obligations will be upheld and repaid. This structure can vary based on the level of need and openness within a given society. In more affluent communities in which individuals are more self-sufficient, there may be fewer outstanding credits among actors. However, in social structures with higher levels of outstanding debts the level of social capital is generally higher. This is because the availability of tangible resources is amplified by the openness and availability of exchange within a community when they are needed. This form of social capital serves as an important indicator of the level of social unity within both of the communities included in the case study of this investigation.

⁵ Putnam, Robert D. (1993).” The Prosperous Community: Social Capital Public Life.” *The American Prospect*, No. 13. <http://epn.org/prospect/13/13putn.html>.

⁶ Coleman, James S. (1988.) “Social Capital in the Creation of Human Capital.” *The American Journal of Sociology*. Vol. 94, p95-120.

The second form of social capital that Coleman classifies is the use of “information channels” (Coleman).⁷ Information can be time consuming and costly. One manner of obtaining that information is through social contacts maintained for other reasons. For example, through casual interaction with friends, neighbors, colleagues, one can stay up to date on new developments in various realms of information without having direct contact with the primary sources of such information. These relations do not hold the same sense of reciprocal obligations as the relations described above. When taking a closer look at the case study in this investigation, both of which are in the context of value chain building projects, access to information is a key element to the success of these projects. In the following pages we will explore the presence of information channels as an indicator of social capital and its relation to value chain building programs.

Lastly, Coleman refers to “norms and effective sanctions” as the third form of social capital (117).⁸ Norms are important for maintaining things like safety in a city or high achievement in schools. Norms maintained within a social structure are also important for promoting the attitude of forgoing self-interest and working in the interest of the collectivity. These kinds of norms, reinforced by positive incentives (awards, recognition bonuses etc.) are crucial for strengthening nascent social organizations. In the context of the case study, we will look at norms equally from the Coleman perspective as from the Meyer-Stamer perspective which refers to the term “norms” in the context of industry standards.

This study considers social capital with the understanding that it is a public good. Individuals usually participate in social organizations that build trust, provide information, or sustain norms for their own personal benefit. However, it is the sharing of these benefits which is

⁷ Coleman, James S. (1988.) “Social Capital in the Creation of Human Capital.” *The American Journal of Sociology*. Vol. 94, p95-120.

⁸ Ibid.

the very motivation for participating in such social organizations and therefore prompting social capital. According to this logic, social capital is a public good in which the group either suffers or benefits as a whole depending on the addition or subtraction of additional individuals.

Whether or not a group actively takes on this attitude will likely be another indicator in the case study of whether or not an organization's social capital can be successfully brokered in to other forms.

Robert Putnam, another prominent scholar in the area of social capital also reinforces the idea social capital in the forms of networks and the associated norms of reciprocity have a public value in addition to individual value (Putnam).⁹ Putnam confirms this assertion through his in-depth research of social networks in the United States. He proves a strong correlation between wealthy communities and a high tendency towards civic engagement. He is the first author to use vast quantitative data to suggest that the presence of things like norms, networks, and civic engagement, all aspects of social capital, are “a precondition for economic development and effective government (Putnam).”¹⁰ The rationale of such findings suggests that civic engagement fosters norms of reciprocity. It also fosters better trust and access to information. “When economic and political dealing is embedded in dense networks of social interaction, incentives for opportunism and malfeasance are reduced; therefore promoting collaborative and transparent business transactions”(Putnam).¹¹ Thus, as this study moves forward, it is important to understand that the varying forms of social capital, as described by Coleman, have a tendency to be “self-reinforcing and cumulative” (Coleman).¹² Putnam therefore asserts that groups that are able to collaborate, and thus build connections and trust, are more able to apply these abilities

⁹ Putnam, Robert D. (1993) “The Prosperous Community,” Social Capital and Public Life.” *The American Prospect*. no. 13. <http://epn.org/prospect/13/13putn.html>

¹⁰ Ibid.

¹¹ Ibid

¹² Ibid

towards other endeavors. As we further analyze the case study at hand we shall see if this theory holds true.

b) Conditions for Productive Social Capital

With a clear idea of what aspects within a social structure can be considered social capital, it is also important to understand the necessary conditions for local level organization to actually translate in to *productive* social capital. Furthermore, we must consider the conditions needed in order to broker social capital in to other forms of capital.

For example, Coleman asserts that closure of networks within a community plays a crucial role in making social capital a valuable resource. This is because when cohesive linkage exist within all levels of actors within a social structure, a community is more likely able to combine efforts to enforce norms and impose sanctions on violators of the norms. It is closely tied with the concept that the whole community is better than the sum of its parts if there is a high density of internal linkages. Closure also gives rise to the role of reputations and how they can be manipulated collectively as a way of mutually enforcing norms. Having a reputation at stake, therefore, also gives rise to trustworthiness. In addition, closure within a group is highly dependent on the level of perceived equality within a group as well. Groups with more defined structures of superiority and rigid power structures are less likely to form cohesive internal linkages.

Eduador Moyano also refers to closure as “embeddeness,” which refers to a high level of cooperation between individuals within a community. Moyano goes a step further in his analysis and asserts that edmbdedness is necessary but not sufficient for social capital to function as development tool. It is also necessary that a community is able to exercise “autonomy,” which refers to the ability of individuals to establish connections with people and groups beyond their

own immediate network. On a micro scale, a community which possesses embeddedness and autonomy is more able to harness the potential of all its members in order to establish strategic and productive linkages with outside members. On a macro level, a community which possesses embedded autonomy is also able to coordinate internally between varying private and public institutions and increases the overall organizational efficiency in their ability to pursue actions in accordance with a common goal or vision (Moyano).¹³ This concept is very similar to Lorenzen's concept of tightly and loosely coupled economic relations that will be explored in the next chapter.

On a similar note, Fukuyama and Granovetter insist on the importance of a group's ability to form relations not only internally, but externally as well. In Mark Granovetter's work "The Strength of Weak Ties" he asserts that a group's ability to establish contact with groups outside their own (i.e. weak ties) increases access to information and opens up opportunities that would not be available to a group that was only internally bonded (Granovetter).¹⁴ Traditional social groups tend to possess a lower quantity of what Granovetter calls "weak ties." He defines "weak ties" as the ability of an individual or a group to that is able to move between various social networks and thereby gain access to a wider range of ideas and information. Therefore, a "traditional society" which is often geographically and socially isolated, consisting only of self-contained homogeneous family units, is more likely to lack these weak ties (for example an isolated, poor, indigenous community of Ecuador). Thus, despite a high level of relative cohesion within a community, there are fewer opportunities to establish contact with outsiders in

¹³ Moyano Estrada, Eduardo. Garrido Fernández, Fernando E. "Capital Social y Desarrollo en Zonas Rurales." IESA-CSIC. Córdoba: España.

¹⁴ Granovetter, Mark. (1983.) The Strengthening of Weak Ties: A Network Theory Revisited. *Sociological Theory*, Vol. 1, 201-233. State University of New York: Stony Brook, NY.

order to gain access to information, innovation and human resources. This concept plays a crucial role when looking at the ability of a community to build economic value chains.

Michael Woolcock coined some of the most commonly used terminology in the social capital discussion: bonding, bridging, and linking. This concept goes beyond Putnam's relatively horizontal perception of social capital as only consisting of relationships among members of a given group or communities. It puts forth a useful framework for categorizing different levels of social capital stocks and the ability to use it as a building block for accruing other forms of capital. "Bonding," is considered the level of trust and norms within members of a homogenous social group (i.e. a family, association of similar businesses, a civic organization etc.). Bridging refers to a group that is able to create "weak ties" or establish "information channels." Bridging is a parallel concept to Moyano's reference to "embeddedness" which allows a group to form ties with other groups within a community or region. This is considered an even more valuable form of social capital than bonding. Lastly, the ability of a group to "link" refers to its ability to establish strategic relationships with groups of power. This often refers to the ability of a group to pressure or persuade financial or governmental organizations for their support (Woolcock 195).¹⁵ Linking is similar in meaning to Moyano's concept of embeddedness on a macro level which helps a group to create strategic alliances with actors even further removed from their own social and geographic radius.

Another aspect of social capital that can be brokered is referred to as "appropriable social organization" (Putnam).¹⁶ This kind of organization refers to the utility of organizations initiated for one purpose, but later serves other functions as well. Once an organization has been formed

¹⁵ Woolcock, Michael. (2001.) "Microenterprise and social capital: a Framework for Theory, Research, and Policy." *The Journal of Socio-Economics.* Vol. 30. pp-193-198.

¹⁶ Putnam, Robert D. (1993) "The Prosperous Community," Social Capital and Public Life." *The American Prospect.* no. 13. <http://epn.org/prospect/13/13putn.html>

and trust has been established within a group; then the social capital formed amongst the members in the process than later can be used to further other goals and initiatives. This will play a role in the analysis of social capital within the producers association highlighted in the case study.

c) The Role of Social Capital in Development

With a clear understanding of the fact that social capital has an intrinsic and brokerable value and an understanding of the situations in which it is created; we can now move forward to look at the importance of this concept in the field of international development. That is to say, how does the presence or lack of social capital help or hinder economic development?

According to Francis Fukuyama, the presence of social capital facilitates economic activity by reducing the transaction costs associated with formal co-ordination mechanisms like contracts, hierarchies, bureaucratic rules, and the like. Parties which enter in to an agreement with a high level of mutual trust will be less likely to try to find loopholes and therefore will have less need to draw up complex contracts that are expensive to create and enforce. “The fact of the matter is that co-ordination based on informal norms remains an important part of modern economies, and arguably becomes more important as the nature of economic activity becomes more complex and technologically sophisticated” (Fukuyama 10)¹⁷ This particularly true in the context of modern industries working in the context of highly integrating global value chains where ensuring oversight of every single transaction is costly and time consuming.

Over the past ten years the World Bank has played a pivotal role in researching and putting in to practice the concept of social capital as a development tool. The social capital debate has served to bring the focus away from market-based strategies in the Post-Washington Consensus era and place a stronger emphasis on the localized socio-political and the role of

¹⁷ Fukuyama, Francis. (2001.) “Social capital, Civil Society and Development.” *Third World Quarterly*, 22(1), 7-20.

organizations and institutions. The pivotal moment in this process came when the economic analysis unit of the World Bank produced in-depth research on the “links between social capital and poverty, constructing regressions that modeled poverty as a function of human, social and financial capital, and suggesting that the effect of social capital on poverty was positive and statistically significant, and at least as important as human capital in influencing household poverty reduction” (Bebbington 42) ¹⁸ Around the same time, the Social Policy Division of the World Bank produced an econometric study using data from a participatory poverty assessment in Tanzania and concluded that social capital (measured by various indicators of participation in local organizations and trust) had a strong positive correlation with household poverty. This information then served to generate a significant qualitative study in Indonesia on the social conditions under which community groups could effectively negotiate with local governments. These study, both qualitative and quantitative, catalyzed new interest in the essential importance of social relations in the process of economic development. However, despite this evidence, social development practitioners point out that these innovative efforts to adapt economic development practice to the particularities of local contexts cannot be examined with an overly micro perspective. Efforts to harness or increase stocks of local capital will be futile if we fail to recognize “broader structures of class, ethnicity, gender and power in which social relationships are embedded a neo-liberal global economy” (58). ¹⁹

Given this irrefutable evidence from the World Bank, the question begs: why exactly is social capital viewed as a tool for economic development? The answer lies in the assumption that the poor have more access to social capital than to any other form of capital. According to the theories mentioned above, once a poor population is able to gain access to social capital, they are

¹⁸ Bebbington, Anthony. Guggenheim, Scott. Olson, Elizabeth. Woolcock, Michael. (2004.) “Exploring Social Capital Debates at the World Bank.” *The Journal of Development Studies*, Vol.40, No.5, pp.33 – 64.

¹⁹ Ibid.

more able to accumulate other forms of capital. This study recognizes the essential other side to this equation: that governments and private businesses also depend on the participation of local populations who contribute inputs, votes, and labor. According to the many theories examined above, the ability of a community to broker their social capital can assist them in creating strategic and mutually beneficial relationships with actors at all levels.

In effect, if social capital is an important factor for the success of development programs, it is important to incorporate an understanding of the social relations existent within a community and between the community and other outside actors. Furthermore, it is important to further understand how the social, cultural, and historical context of a local population is articulated in day-to-day relationships and power structures (Moyano).²⁰

The discourse on social capital to this point has expressed a generally positive outlook on the prospects for utilizing social capital in the development process. However, what remains unclear are the circumstances in which this holds true. Furthermore, there also remains much debate about whether or not social capital can be generated from outside interventions or whether it must exist prior to trying to harness its potential. Moreover, this investigation explores whether or not it is a necessary condition to the success of local economic development. If so, is this true in every context, or, is the presence of social capital more relevant in some kinds of local development programs than others? Can there be local economic development in a context in which stakeholders possess “bonding” capital but lack “bridging” or “linking?” These are questions being asked by practitioners today.

d) How to put Social Capital to Use in Developing Countries for Practitioners

²⁰ Moyano Estrada, Eduardo. Garrido Fernández, Fernando E. “Capital Social y Desarrollo en Zonas Rurales.” IESA-CSIC. Córdoba: España.

Over the course of this discussion it has been made clear that social capital can be thought of like any other form of capital such as human, physical, or cultural capital. Capital has value because it can be converted into other forms. There is no doubt that the poor and disadvantaged have access to fewer stocks of human, financial, technological capital. However, unlike the other forms of capital, social capital does not require any pre-existing capital in order to accumulate it. We could say that it is the “cheapest” form of capital. Therefore, it is the one form of capital that the poor are most likely to have some limited ability to create and maintain. Ideally, if the poor are able to obtain social capital, they can cultivate its growth and eventually trade it in to other forms of capital that will ultimately better their economic situation (Light 148).²¹ On the other hand, if possession of one form of capital begets other forms of capital; one can argue that the poor are likely to possess lower levels of social capital because they have less physical and human capital to build upon. Many authors suggest that the poor can spontaneously and endogenously generate social capital. The case study discussed in this study suggests that this is not always true. Furthermore, it must be recognized that those who possess other forms of human and physical capital are much likely to possess stronger social capital. This often results in exclusionary and unequal social dynamics.

Yet these concepts are only useful if they can be translated from a “framework for description in to a framework for action. (Putnam 147).²² At this point in the analysis, it is crucial to look at ways in which social capital can be employed in programs seeking to reduce poverty and empower the poor. More specifically, this study will look at how social capital can

²¹ Light, Ivan. (2004). Social Capital's Unique Accessibility. In Hutchinson, Judy. Vidal, Avis C. (Ed.) Symposium: Using Social Capital to Help Integrate Planning Theory, Research, and Practice. *Journal of the American Planning Association*, 70(2), pp143-150.

²² Putnam, Robert. (2004). Preface. In Hutchinson, Judy. Vidal, Avis C. (Ed.) Symposium: Using Social Capital to Help Integrate Planning Theory, Research, and Practice. *Journal of the American Planning Association*, 70(2), pp143-150.

contribute successful local economic development programs. With a broad understanding of the nature of social capital, the conditions under which it can be harnessed, and its significance in poverty reduction: it is now crucial to deduce palatable approaches and tools. If social capital is to be evoked in the planning and implementation of local economic development, the first essential step is for practitioners to closely assess whether they are seeking to build upon and utilize pre-existing forms of social capital; or whether they are trying to create social capital in a situation where none existed prior to that.

This question is often overlooked in the process of planning a program, and often results in disappointing or failed results. Based on the work of Fukuyama and Putnam, there is a clear distinction between effectively drawing upon existing social capital and attempting to create it. According to Fukuyama, efforts to induce social capital from the outside are nearly impossible. This criticism should be taken in to consideration amongst practitioners who may be tempted to treat the idea as a panacea for jump starting the development process.

Both Fukuyama and Putnam bring to attention to the cultural and historic situations that determine a group's stock of social capital. Putnam's research reveals a distinct correlation between densities of social capital closer to the Canadian border and less dense stocks of it within populations located further south. The historic correlation with this data reveals that former slave territories of the US, where social capital was presumably repressed for generations, exhibit distinctly lower stocks of social capital. Fukuyama also points out that the world's largest religions have the power to transmit certain social behaviors and cultural norms from generation to generation. He refers to this phenomenon as "path dependence" which means that norms are transmitted through a process of socialization that involves much more habit than reason

(Fukuyama).²³ These norms clearly have the ability to persist for very long periods of time. Both authors suggest that the social and historical structure operating in the background of a given community can have huge impacts on a program which attempts to utilize social capital. In the case that there is a low level or non-existent level of social capital, the historical forces at play make any attempt to impulse the creation involve a level of difficulty paramount to trying to reverse the byproducts of generations of historical experiences.

Any program that enters a community from the outside should be aware of already existing forms of social capital, but more importantly, it must be aware of the strength of historically embedded attitudes and values. A community that has traditionally given limited power to women or one in which paternalistic outside donors have created a culture accustomed to receiving handouts very well may be unable to harness any social capital. Often, practitioners fail to do a thorough assessment of the level and nature of social capital in a community before assuming that it can be co-opted and converted in to other forms of capital. Therefore, when determining the tools necessary in order to harness social capital's potential, a social capital assessment survey and analysis should always be utilized. This will be discussed at greater length in the following section. By doing an in-depth assessment of a community's level of social capital, programs can avoid the mistake of failing to recognize that the concept of a "community" is not equivalent understanding the ways in which culture and class tend to organize and interact within that community.

Once a practitioner has gained a thorough understanding of the level of social capital existent within a community, they can also assess the particular dynamics, power relations, strengths, and weaknesses amongst a community's social fiber. Using the knowledge discussed

²³ Fukuyama, Francis. (2001.) "Social capital, civil society and development." *Third World Quarterly*. Vol 22, No 1. pp 7– 20.

above of how to make social capital productive, practitioners can then intervene to strengthen and support particular aspects of the social structure that may be lacking. However, it is important to be aware when focusing targeted interventions on groups that have a narrow radius of trust, that social capital can produce negative externalities and be detrimental to the larger society (Souza Brigga 151).²⁴

Social capital can be fostered and supported through a wide variety of interventions. Xavier Souza Briggs suggests at least four areas of intervention that can catalyze existing social capital in to a more brokerable asset (153).²⁵ First, practitioners can encourage behavior that promotes joining, participating actively in, and leading new and renewed civic institutions that tackle tangible problems. Second, programs implemented by outside actors should help people “acquire new civic skills, with special attention to the next civic generation (young people) and those with less status in the community” (155).²⁶ These skills should include running a meeting, defining a public issue, persuading others to act, deliberating with others, and participating in shared decision making. Thirdly, outside actors have the ability to facilitate bridging between local groups and to facilitate linking opportunities with actors outside of the community. In most cases, the relationship between an outside practitioner and community groups can be considered a form of linking in and of itself. Lastly, Briggs suggests that practitioners can help cultivate new norms that place increased importance on mutual responsibility within the group, open dialogue amongst members, and a mentality of working towards a common goal that will benefit all involved.

²⁴ Souza Brigga de, Xavier. “Social Capital: Easy Beauty or Meaningful Resource? Social Capital's Unique Accessibility.” (2004.) In Hutchinson, Judy. Vidal, Avis C. (Ed.) “Symposium:Using Social Capital to Help Integrate Planning Theory, Research, and Practice.” *Journal of the American Planning Association*, 70(2), 151-158.

²⁵ Ibid.

²⁶ Ibid.

Fukuyama also asserts that outside actors, although they cannot create social capital, can in a select few ways, foster its growth when it is pre-existent. Primarily, outside actors probably have the greatest direct ability to generate social capital in education. Educational institutions do not simply transmit human capital; they also pass on social capital in the form of social rules and norms. Secondly, outside actors, particularly governments, can indirectly foster the creation of social capital by efficiently providing necessary public goods, particularly property rights and public safety. Given a stable and safe environment for public interaction and property rights, it is more likely that trust will arise spontaneously as a result of iterated interactions of rational individuals. I will apply this aspect to see if a program's ability to foster favorable market conditions can also create a social capital-friendly environment (Fukuyama).²⁷

However, Fukuyama argues that outside actors can have a serious negative impact on social capital when they start to undertake activities that are better left to the private sector or to civil society. "The ability to co-operate is based on habit and practice; if the state [or outside practitioners] get into the business of organizing everything, people will become dependent on it and lose their spontaneous ability to work with one another" (Fukuyama).²⁸ Fukuyama's anecdotal evidence suggests that "it is difficult for outsiders to foster civil society in countries where it has no local roots. Foundations and government aid agencies seeking to promote voluntary associations have often simply managed to create a stratum of local elites who become skilled at manipulating donor resources. This often leads to the creation of organizations that are not sustainable and tend to disintegrate after the donor funds have been exhausted. In the following pages we will examine precisely this argument.

²⁷ Fukuyama, Francis. (2001.) "Social capital, civil society and development." *Third World Quarterly*. Vol 22, No 1. pp 7– 20.

²⁸ Ibid.

The following case study analyzes the actions of outside donors and their attempts to spark local economic development by harnessing units that supposedly possess social capital. The study will reveal an analysis of the strength and nature of the local social capital as well as an analysis of the interventions of the outside actors and whether or not they were able to successfully transform social capital in to another form of capital. Given that the program defines its primary goal as promoting local economic development, it is also important to distinguish the difference between creating development through social capital *or* if it has been created through other forms of capital investment. In order to determine this difference, a discussion of the economic approach to the program in the case study is crucial. In the past ten years, market based poverty reduction programs have become the standards for international foreign assistance methodology. These programs are now heavily focused on integrating local economies and local producers with the larger regional and international markets. Such processes present unprecedented exposure to learning opportunities significantly higher prices to be fetched on the world market. These programs also involve many more levels of actors, transactions, and relationships than ever before seen in rural economies. The following chapter will discuss how these programs function and the crucial role of social relations.

III. Local Economic Development Theoretical Background

a) Defining Global Value Chains

The current global context for this study is inextricably linked with a world that is every day increasingly interconnected. The structure of the market as we know it is now a complex web of relations between buyers and sellers spanning the globe. In this context, the stage for promoting local economic development has changed dramatically. Today, development initiatives must think of how any given local scenario in a developing country is currently linked

in to the globalized context of today's economy, and, more importantly, how local populations in developing countries can integrate in to the global marketplace. In this context, the idea of integrating local producers with global value chains has gained nearly super-star status among development practitioners around the world. This approach continues to grow in popularity in both the academic and practitioner realms of development.

In this section the predominant theories on global value chains and local economic clusters will be presented. More importantly, I will review the prominent literature available on the role of social capital and social relations within the context of local economic development efforts. The literature brings to light analysis on the role of trust and the kinds of relationships which play a crucial role in the efforts assist local producers gain a larger, more specialized and more profitable share of the international markets through innovation and integration in to the value chain.

Let us begin then with a basic introduction to the theory of value chains and what they mean for development. One of the foremost authorities on the value chain discussion is Jorg Meyer-Stamer. Value chains are “the sequence of activities involved in transforming raw materials into a product that is acquired by the final customer” (Meyer-Stahmer).²⁹ These activities range from the creation of basic inputs, the processing and transformation of those goods, and the manufacturing or packaging and branding of the final good that ultimately ends up in the hands of the consumer. These processes involve interactions between businesses as well as governments and supporting institutions that work in the areas of finance, research and development, training or certification.

²⁹ Meyer-Stahmer, Jörg. Wältring, Frank. “Value Chain Analysis and “making markets work for the poor: Poverty reduction through value chain promotion.” Technische Zusammenarbeit (GTZ): Germany.

Value chains can involve relatively few steps such as in raw foods that initiate with the growers, pass through an intermediary which provides processing or packaging, and generally end on the stands of a retail grocery store. They can also be incredibly complex as in the case of technology items in which the various parts and various stages of production can involve interaction between actors from around the world.

Meyer Stamer points out that “value chains exist at the subnational regional level, the national level, and the global level.” At the subnational region they are often referred to also as “clusters.” Essentially this terminology refers to the interaction between local entities involved in various aspects of production in a particular industry. The emphasis is on the geographical proximity of such actors. At the global level, academic literature refers to value chains as the series of transactions that must occur in order for, for example, a bean of coffee produced in the Yungas of Bolivia to end on the shelves of a US grocery store. In that sense, the term “value chain” is used in place of what can also be called a supply chain. The primary difference between these phrases is simply the “angle of analysis” (Meyer-Stahmer).³⁰

The traditional supply chain perspective stems from the perspective of large businesses concerned with efficient, timely, and cost effective management of the supply chain. The classic case study used in this body of literature are Walmart and Ikea which are large corporations that are able to masterfully manage logistics such that large quantities of products arrive to various locations around the globe while maintaining low costs and timely delivery.

The body of literature concerned with value chains is based not upon business strategies, but upon development theories. As development studies have come to grasp the increasing power of global companies and their increasingly active role in developing country economies, academics and practitioners began to consider “development prospects of companies that are

³⁰ Ibid.

dependent on Wal-Mart or Ikea for their export sales, and that are thus integrated into the global economy in a dependent way. The main focus is at the analysis of power structures in the world economy” (Meyer-Stahmer).³¹

One of the key motivations for the emergence of value chains as we know them today is that as firms increasingly outsource more and more of the production process, coordination among actors along the chain becomes more important. That is to say that buyers have found it more cost effective to occupy a smaller role in the chain, but their ability to fulfill that niche is contingent upon their ability to obtain inputs that meet the markets demands for quality and quantity. Lead firms must set the parameters for production and increasingly, cooperation between buyers and suppliers is crucial to ensure that product demands are met.

As a development practice, value chain programs have in recent years evolved from “practitioners’ insight in the need to connect producers to the market, and indeed understanding and verifying the market before engaging in upgrading activities with producers and manufacturers” (Meyer-Stahmer).³² Development practitioners have observed this process and spotted an opportunity for poverty alleviation programs driven by market demands. Research has shown that when rural producers, particularly agricultural producers, are able to integrate in to value chains, their ability to sell higher volumes and receive better prices from larger buyers has a directly positive correlation with increased income levels. This literature is also well aware of the risks of the value chain approach. Poor producers will only stand to gain if they are able to produce at the required quality and quantity levels demanded by the buyers. This often requires material investment and capacity building on the part of the producers. The role of the donor in this case is crucial at providing the initial investment and helping to establish the relationships

³¹ Meyer-Stahmer, Jörg. Wältring, Frank. “Value Chain Analysis and “making markets work for the poor: Poverty reduction through value chain promotion.” Technische Zusammenarbeit (GTZ): Germany.

³² Ibid.

between buyers and suppliers. In the case study examined below is one such example in which the United States Agency for International Development sought to link buyers and sellers in the Panama Hat industry with the global market.

Meyer Stamer makes a crucial observation about the fairly limited scope of the academic literature regarding the role of global value chain integration and local development. Most of the work that has been done to date focuses on firms in developing countries “that are already highly competitive [and] . . . are able to consistently satisfy the sophisticated demand of leading companies in industrialized countries bears witness of this.” He notes that “only occasionally does the value chain literature trace the evolution of producers in developing countries and the stages that preceded their integration into global value chains. The exact mechanisms of how producers in developing countries become integrated into global value chains are not at all clear. In this respect, the literature is only of limited value to practitioners who want to upgrade producers in developing countries so that they appear on the radar screen of global buyers” (Meyer-Stahmer).³³

In the literature produced the realm of practitioners, the differences between complex and simple value chains is often underplayed. Meyer-Stamer addresses this dangerous over simplification when he states that “concepts that have been developed in settings with highly competitive industries cannot easily be transferred to survivalist sectors” (Meyer-Stahmer).³⁴

b) How Value Chains Affect Local Economic Development

The benefits and opportunities of trade liberalization for developing countries have been well documented by many authors. Gereffi points out that in order for developing countries to partake in the many opportunities presented by trade liberalization, then producers must be able

³³ Meyer-Stahmer, Jörg. Wältring, Frank. “Value Chain Analysis and “making markets work for the poor: Poverty reduction through value chain promotion.” Technische Zusammenarbeit (GTZ): Germany.

³⁴ Ibid.

to have a comparative advantage to producers in developed countries. Traditionally, low cost of labor has been the comparative advantage in labor intensive products such as clothes, shoes or fresh produce. “Increasingly, trade in these products is organized and led by global buyers, who may work for, or act on behalf of, major retailers or brand-name companies” (Humphrey).³⁵ Benchmark case studies such as the Gereffi’s study of the garments trade between East Asian countries and the US, Dolan and Humphrey’s study of horticultural products between Africa and the UK and the Schmitz and Knorrnga study of trade in footwear from China and Brazil to the US and Europe, reveal that “access to developed country markets has become increasingly dependent on entering into the global production networks of lead firms situated in developed countries” (Humphrey).³⁶ For development practitioners, it thus follows that understanding the structure of these chains and is paramount to helping developing country producers understand how to position themselves as an actor within these chains. As the following pages will reveal, these value chains consist essentially of disperse networks of interdependent actors all of whom base their transactions upon a dense network of relationships. Understanding these relationships and their implications for development is essential for designing successful opportunities for developing country producers to assume a self-benefitting role in these networks (Humphrey).³⁷

c) Value Chains in the New Globalization Context

Gereffi suggests that the key feature of the current phase of globalization is “the functional integration and co-ordination of internationally dispersed activities” (Gereffi 114).³⁸

Indeed, the current macro-level historical context of this discussion is acutely important to

³⁵Humphrey, John. Schmitz, Hubert. (2001.) “Governance in Global Value Chains.” *IDS Bulletin*, 32.3.

³⁶ Ibid.

³⁷ Ibid.

³⁸ Gereffi, Gary. 1994.. “The Organization of Buyer-Driven Global Commodity Chains: How U.S. Retailers Shape Overseas Production Networks.” pp. 95–122. *Commodity Chains and Global Capitalism*, ed. Gary Gereffi and Miguel Korzeniewicz. Westport, Conn.: Praeger.

understanding the relevance of relationships and how they matter in promoting local economic development. The concept of promoting value chains as a means of assisting local producers to obtain a place in the value chain which generates greater income must be understood within the paradigm of a globalized world that is increasingly interconnected and interdependent.

In addition for opportunities to proactively take advantage of global market, the demands of global competition are increasingly requiring leading firms to work jointly with suppliers, including developing world suppliers. This closer relationship between lead firms and suppliers is creating a unique window of opportunity for suppliers to assume more competencies. Hubert Schmitz suggests that “joint action is particularly important when clusters confront major turning points.

d) The Role of Relationships and in Local Economic Development and Value Chains

The next progression in the value chain literature was to deduce from studies such as the Italian and Brazilian case a way to characterize and classify relationships between actors in value chains. Hubert Schmitz characterizes value chain relationships based upon the breadth and depth of upgrading available to agents involved with each prescriptive relationship. The four types of relationships he describes are:

Market based: enterprises deal with each other in arms length transactions.

Balanced network: enterprises co-operate and have complementary competences but no control over each other.

Captive network: the lead firm sets the parameters under which others in the chain operate; the relationship is quasi-hierarchical.

Hierarchy: enterprises are vertically integrated; the parent company controls its subsidiaries (Humphrey).³⁹

Understanding the nature of relationships among actors in a value chain or cluster is important for understanding and determining the level of opportunity for local producers for upgrading. Essentially, the notion of integrating in to a value chain is based on the assumption

³⁹ Humphrey, John. Schmitz, Hubert. 2001. “Governance in Global Value Chains.” IDS Bulletin, 32.3.

that integration affords a producer more opportunities to improve various aspects of production and eventually fetch a higher price for that service or good. These kinds of improvements are referred to as “upgrading.” Firm upgrading is what ultimately leads to higher income generation and poverty reduction and is thus the crux of development projects which focus on value chain integration. Although there is no space to cover in great detail a discussion of upgrading, there are generally four categories which characterize how a firm advances. The four categories are:

Process upgrading: transforming inputs into outputs more efficiently by reorganizing the production system or introducing superior technology.

Product upgrading: moving into more sophisticated product lines (which can be defined in terms of increased unit values).

Functional upgrading: acquiring new functions in the chain (or abandoning existing functions) to increase the overall skill content of activities.

Inter-sectoral upgrading: using the knowledge acquired in particular chain functions to move into different sectors (Schmitz).⁴⁰

These four scenarios are essentially the manifestation of the four types of relationships described above. If the objective of local economic development is to improve the competitiveness of local companies so that they can integrate in to a broader marketplace, then the actions taken to do so must aim to “to increase the competence of local firms in terms of production, quality, technology, human resources and financial management, so that they can manufacture products of acceptable quality at competitive prices in the hope that they may attract recognition from global buyers” (Meyer-Stamer.)⁴¹ Meyer Stamer also categorizes the types of upgrading that a local firm may engage in when trying to become part of a global value chain:

a) *Product and process upgrading:* Often this mainly concerns running to stand still: It implies joint upgrading with other participants in the value chain, but it does not imply a change in position in the value chain. This is a challenging task that involves only a limited risk. It is in everybody's interest including the global

⁴⁰ Schmitz, Hubert. 2004. “Local Upgrading in Global Chains: Recent Findings.” DRUID Summer Conference on Industrial Dynamics, Innovation and Development: Elsinore, Denmark.

⁴¹ Meyer-Stamer, Jorg. “Why is Local Economic Development so difficult, and what can we do to make it more effective?” mesopartner working paper 04 /;2003.Duisburg 2003 www.mesopartner.com

buyer, who is also interested in fundamental activities, to improve locational quality, such as infrastructure and vocational training institutions.

b) *Strategic functional upgrading*: This entails taking over functions previously handled by other companies, usually from other locations within the same value chain. This is a more risky option, as the to-be-replaced competitors will probably fight back. Global buyers may be expected to tolerate this (as long it does not threaten their own core competence), as fierce rivalry between locations strengthens their bargaining position vis-à-vis each of them.

c) *Improve their competitiveness in order to move to a different value chain*: In a given sector, there are various value chains that cater for different segments of the consumer market. As long as margins are higher in more sophisticated or in differentiated markets, it may be tempting to switch from one value chain to another that serves higher-margin markets. This involves the risk of falling between a rock and a hard place; the old buyer may anticipate this and move to a different source, whereas the prospective new buyer might fail to close the deal.

d) *Attempting to take over the value chain or trying to take the main power position in the value chain*: This is clearly the most challenging option. It may be viable in cases where the buyer's power position is limited; the ceramic tile industry is case in point (Meyer-Stamer).⁴²

Practitioners and academics should recognize that there is no automatic guarantee that “insertion in captive global chains provides a route to functional upgrading, i.e. moving into the design, branding and marketing functions in the chain.” The truth is that there exists “some evidence of firms progressing to design but very little sign of producers developing their own brand or setting up their own marketing channel” (Schmitz).⁴³ In fact, the evidence suggests that most developing country firms remain in the role of supplier to lead firms once integration has been achieved. Schmitz asserts that “the source of power in global value chains lies increasingly in non-production activities, notably in branding, marketing, product development and the coordination of inter-firm relations. Lead firms (global buyers) focus on and invest in these

⁴² Meyer-Stamer, Jorg. “Why is Local Economic Development so difficult, and what can we do to make it more effective?” mesopartner working paper 04 /;2003.Duisburg 2003 www.mesopartner.com

⁴³ Schmitz, Hubert. (2004.) “Local Upgrading in Global Chains: Recent Findings.” DRUID Summer Conference on Industrial Dynamics, Innovation and Development: Elsinore, Denmark.

activities as they regard them as their core competence” (Schmitz).⁴⁴ Therefore, lead firms often try to protect this strategic role by discouraging supplier firms from seeking to obtain greater competences. Local firms ‘adopted’ by global buyers often progress fast, but often come up against a glass ceiling. Knorringa refers to integration into such chains is a “double-edged sword [that] facilitates inclusion and rapid enhancement of product and process capabilities [but also] inhibits functional upgrading. Progressing into design, branding and marketing often conflicts with the core competence of global buyers. In some cases, however, clusters of developing country producers have become able to offer comprehensive combinations of products and related services at great speed, enabling them to have more balanced relationships with their buyers” (Knorringa).⁴⁵ When developing country firms do attempt to make this leap along the value chain the associated investments in human and physical capital can be unrealistically large. Thus, it should be noted that these captive network buyer-supplier relationship is not a desirable scenario for promoting growth for the developing country actors.

A more beneficial alternative to captive networks are the “balanced networks” as defined by Schmitz. In this type of relationship “there is a stronger mutual commitment between firms than in market-based relationships, but the relationship is more symmetrical than in captive networks. Such balanced networks, based on sharing of competences and focused on developing new products and processes, are common in developed countries, as shown in the literature on innovation networks. Recent research in developing countries has however brought up a new type of balanced network, based on sharing competences and focused on rapid product delivery to tight specifications and requiring only limited innovation by the suppliers. In most cases, the

⁴⁴ Schmitz, Hubert. (2004.) “Local Upgrading in Global Chains: Recent Findings.” DRUID Summer Conference on Industrial Dynamics, Innovation and Development: Elsinore, Denmark.

⁴⁵Knorringa, Peter. Van Staveren, Irene. (2007) “Unpacking Social Capital in Economic Development: How Social Relations Matter.” *Review of Social Economy*. Vol. 65 (1).

developing country suppliers are in captive relationships with these buyers but in a few cases the relationships have become more balanced” (Schmitz).⁴⁶

Based on these distinctions these authors suggest that the nature of relationships between actors in a value chain is very likely to affect the level of upgrading available to actors at the bottom of the chain. Furthermore, the ability to actively maneuver or strengthen these relationships suggests a direct correlation with the ability to enhance upgrading opportunities.

e) The Role of Cooperation in Global Value Chains

At the forefront of most discussions on how to successfully promote further integration in to the global marketplace is a realization of the importance of the role of interaction, cooperation between actors and individual relationships between actors.

The role of local cooperation in local development began with the export success of Italian industrial districts. One of the first groundbreaking studies dedicated exclusively to this subject was the book “Industrial Districts and Inter firm Co-operation in Italy” (Becattini).⁴⁷ The emphasis on co-operation did not imply a lack of competition amongst clustering enterprises. The study was the first to demonstrate that local competition in a common industry did not preclude collaboration for addressing common obstacles. It also revealed that “firms whose outputs complement each other are more likely to co-operate than firms with near identical products” (Humphrey).⁴⁸

Meyer-Stamer also provided pivotal research in his 1999 study of how the ceramic tile cluster in Santa Catarina (Brazil) “overcame a major crisis in the early 1990s and concludes that

⁴⁶ Schmitz, Hubert. (2000.) “Does Local Co-operation Matter? Evidence from Industrial Clusters in South Asia and Latin America.” *Oxford Development Studies*. Vol. 28, No. 3. International Development Centre: Oxford.

⁴⁷ Becattini, Giacomo. Pyke, Frank. Sengenberger, Werner. (1990). “Industrial Districts and Inter-Firm Cooperation in Italy.” Geneva: ILS.

⁴⁸ Humphrey, John. Schmitz, Hubert. (2001.) “Governance in Global Value Chains.” *IDS Bulletin*, 32.3.

an increase in inter-firm co-operation was a key factor” (Meyer-Stamer 460).⁴⁹ He brings to light several outcomes of cooperation such as benchmarking between local firms, rejuvenating the business associations, learning trips to leading tile cluster in Italy, the creation of a technology center for ceramics which resulted from collective effort to harness funding from the state. The case also demonstrates the comparison of other clusters in Santa Catarina which were unable to bundle local efforts and were less successful in restructuring and upgrading (455).⁵⁰ Through these landmark studies, the importance of cooperation and strong relationships and its direct relation to successful value chains or local clusters was solidified.

The proposition is that closer co-operation is essential in order to respond successfully to major crises or opportunities. The new global competition constitutes such a turning point.”⁵¹ This logic suggests that enterprises which have increased co-operation are performing better than those which have not (Schmitz).⁵² To test this hypothesis Schmitz asks the question: could a correlation be established between increases in co-operation and improvements in performance? In his studies of 4 clusters in Pakistan, India, Mexico and Brazil in the footwear and related industries and one in surgical instruments he measure firm performance against four categories of inter-firm cooperation (see table below).

⁴⁹ Meyer-Stamer, Jorg. “Industrial Policy to Regional and Local Locational Policy: Experience from Santa Catarina/Brazil.” (1999.) *Bull. Latin Am. Res.*, Vol. 18, No. 4, pp. 451-468.

⁵⁰ *Ibid.*

⁵¹ Schmitz, Hubert. (2000.) “Does Local Co-operation Matter? Evidence from Industrial Clusters in South Asia and Latin America.” *Oxford Development Studies*. Vol. 28, No. 3. International Development Centre: Oxford.

⁵² *Ibid.*

Types of inter-firm co-operation		
	Bilateral	Multilateral
Horizontal	e.g. Sharing equipment	e.g. Sectoral association
Vertical	e.g. Producer and user improving components	e.g. Alliance along local value chain

Figure 1(Schmitz)⁵³

The results show that consistent results covering all four clusters in each category of co-operation do not emerge. However, in three clusters there is a positive and statistically significant correlation between improvements in performance and:

- *horizontal multi-lateral co-operation and;*
- *vertical bi-lateral co-operation with suppliers (Schmitz).*⁵⁴

Furthermore, the qualitative material (in-depth interviews) further supports Schmitz's conclusion that increased vertical co-operation (between manufacturers and suppliers/subcontractors) was most critical increasing firm performance. The informants reveal that vertical cooperation allowed firms to enhance competition on the key areas of quality and speed. The study suggests that improvements like the Brazilian shoe manufacturers that were able to reduce the time between order and delivery by two-thirds and substantially raise quality, would not have been possible without the co-operation of their suppliers and manufacturers (i.e vertical integration). Schmitz's study also shows that the leaders in bringing about the change in inter-firm relationships tend to be large firms and small firms tends to be followers. He also reveals that even the leaders tend to limit the new practices to core partners. This suggests the possibility for exclusionary results strong bonding social capital. Horizontal cooperation between multiple

⁵³ Schmitz, Hubert. (2000.) "Does Local Co-operation Matter? Evidence from Industrial Clusters in South Asia and Latin America." *Oxford Development Studies*. Vol. 28, No. 3. International Development Centre: Oxford.

⁵⁴ Ibid.

firms occupying the same link on the value chain also shows some statistically significant correlation with firm performance in three of the four cases. These findings were supported by the qualitative investigation, which showed how joint action helped to cope with new challenges such as cooperation on quality assurance certification (Schmitz).⁵⁵

f) The Role of Trust in Local Economic Development

Having established the importance of value chain integration for local economic development and the importance of relationships among actors in an integrated globalized context; we now turn to a closer look at the nature of these relationships. One of the fundamental elements of social capital as described in the previous section is trust. Most of the most prominent authors in the area of local economic development draw upon the role of trust in building inter and intra agent relationships.

In the seminal work by John Humphery and Hubert Schmitz, “Trust and Inter-Firm Relations in Developing and Transition Economies,” the authors laud trust as the “missing factor that explains why some countries or regions develop rapidly and others lag behind” (Schmitz).⁵⁶ They define two levels of trust present in relations formed for economic purposes: minimal and extended trust. Minimal trust is that which is required for “basic market transactions.” Extended trust is defined as “relationships which sustain the cooperation seen in industrial supply chains and clusters” (Schmitz).⁵⁷ Humphery and Schmitz concur with other authors in the field by recognizing that “trade liberalization exposes industries in developing countries to increase competitive pressures. Firms can respond to these pressures by restructuring their links with

⁵⁵ Schmitz, Hubert. (2000.) “Does Local Co-operation Matter? Evidence from Industrial Clusters in South Asia and Latin America.” *Oxford Development Studies*. Vol. 28, No. 3. International Development Centre: Oxford.

⁵⁶ Ibid.

⁵⁷ Ibid.

other firms, but this requires trust” (Humphrey 36).⁵⁸ Trust between agents is essential when considering that agents inevitably face risks when they enter exchange. Because it is impossible for agents (i.e. actors, firms etc.) to anticipate all possible scenarios and it is costly to incorporate all contingencies in to contracts, all economic transactions rely to some degree on the good will of ones counterpart in the transaction. When firms feel uncertain about the reliability of a client or supplier they rely on “flea market mode of transacting: inspect the good on the spot, pay cash and walk away with it” (45).⁵⁹ This form of interaction is conducive to promoting business transactions on any large or reoccurring scale. Thus, trust is required to operate “with any degree of predictability . . . to be able to take and place orders, arrange the future delivery of goods and services and seek and provide warranty” (52).⁶⁰ When agents seek to participate in value chains or clusters, agents grow more dependent upon one another to uphold their end of the deal in order to generate economic success for all actors. Therefore, trust is “no longer limited to the expectation that explicit promises will be fulfilled: the partners make commitments in the expectation that the other side is committed to developing the relationship. This transaction is often characterized as a shift towards trust-based relationships” (43).⁶¹

The next logical question is thus; how do actors in developing countries develop such trust? Humphrey and Schmitz point out that the key concern with building trust relationships is the problem of the vulnerability of the supplier. In developing economies, the buyer supplier relationship is often characterized by an uneven power dynamic in which the supplier is often the smaller player. The greatest risk for the buyers are usually surrounding the reliability of quality and delivery of the product; which have become critical factors in gaining greater market shares.

⁵⁸ Humphrey, John. Schmitz, Hubert. (1998.) “Trust and Inter-Firm Relations in Developing and Transition Economies.” *The Journal of Development Studies*. Vol. 34, No. 4. pp.32-61.

⁵⁹ Ibid.

⁶⁰ Ibid.

⁶¹ Ibid.

The suppliers often risk vulnerability to opportunistic behavior on the part of the customer either by forcing down prices or revealing “secrets” of production to other suppliers. These risks are exacerbated in a country where a strong regulation or legal enforcement system is lacking.

The Humphrey and Schmitz research reveals an interesting correlation between opportunities for supplier upgrading and the characterization of the trust relationships between buyers and suppliers. The evidence suggests that in supplier-customer relationships driven primarily by the suppliers need to maintain price competitiveness, the opportunities for the supplier to progress in the upgrading process are limited. In the case in which the supplier’s competitive advantage is in speed of delivery or in product innovation or quality, then the suppliers are able to play a larger role in the strategy of product development. These relationships allow the supplier exposure to learning opportunities from the actor above them in the value chain. In former case the trust relationships remain uneven. In the later case, Humphrey and Schmitz insist that as the supplier-customer relationships is characterized more as collaborative partnership, then the level of trust is correspondingly higher. Thus “the transformation of relationships requires not only a change in attitude, but also a change in the division of labor between enterprises and a change in competitive strategy.”

Social ties also play an important role in the construction of trust in economic relationships. The literature on the success of the Italian clusters emphasize the “embeddedness of enterprises in communities and the socio-cultural ties which facilitate trust and sanctions” (37).⁶² However, more recent research on clusters and value chains in developing countries suggests that trust between actors of similar socio-economic status used to be the foundation for creating trusting and collaborative economic relationships. Today, with the increasing pressure

⁶² Humphrey, John. Schmitz, Hubert. (1998.) “Trust and Inter-Firm Relations in Developing and Transition Economies.” *The Journal of Development Studies*. Vol. 34, No. 4. pp.32-61.

of market demands, actors must reach out to agents in different geographic locations and in different socio-economic circles. To foster these new relationships between actors who previously had little or no interaction, it is crucial to form trusting relationships. Thus, ties between actors today are still as important as ever, but they are increasingly based more on conscious investments (“process based” rather than “character based.”) (58).⁶³ This kind of cooperation is most likely to emerge when firms face challenges they cannot face on their own.

g) Social Capital in Value Chains

Another important aspect of the discussion involves an analysis of the level of social capital within the internal structure of a group that is participating or attempting to participate in a value chain or cluster scenario. When groups are able to draw upon internal social capital, there are three areas of economic opportunity that can emerge.

(1) *Reducing transaction costs;*

(2) *Enabling and reinforcing of collective action:* In this case, the underlying mechanism of social relations is solidarity and cooperation. Cooperation between individuals and organizations creates economies of scale. Such trust-confirming cooperation can also enhance bargaining power in the market, leading to increased access to, or better negotiation terms in markets.

(3) *Generating learning spin-offs and creating learning spill-overs:* Here, the underlying mechanism of social relations is social cohesion and sociability. By working together, workers learn from each other on the job. This process is stimulated in a setting of teamwork, where new team members learn on the job under the guidance of workers who are more experienced. A dynamic workforce, in particular when it is a specialized workforce possessing special skills, helps to transmit human capital through learning from one company to another . . . Another form of learning spill-overs is through collective learning by jointly acquiring or quickly transmitting new technology, for example, through business networks. In both ways social cohesion and sociability enhance total factor productivity (Knorringa).⁶⁴

⁶³ Humphrey, John. Schmitz, Hubert. (1998.) “Trust and Inter-Firm Relations in Developing and Transition Economies.” *The Journal of Development Studies*. Vol. 34, No. 4. pp.32-61.

⁶⁴ Knorringa, Peter. Van Staveren, Irene. (2007) “Unpacking Social Capital in Economic Development: How Social Relations Matter.” *Review of Social Economy*. Vol. 65 (1).

Furthermore, Mark Lorenzen highlights that economic competition has shifted from the need for efficient production to additionally needing to innovate rapidly. This market demand reveals the importance of the efficiencies of learning. Social factors are crucial to facilitating learning “and hence lead to product innovations and above average export potential of local firms.”⁶⁵ He asserts that “because social capital is collective and formed within communities through processes of interaction and institutional learning, it is a unique collective asset which is technically impossible to trade or imitate.” Collective assets such as this can help a region as a whole to gain a competitive advantage over producers of similar products in other regions. Although there is not enough space to delve in to here, there is a breadth of literature discussing the interactive nature of technological learning (Lorenzen 801).⁶⁶ Many authors emphasize the importance of buyer – supplier innovation, interactive learning, inter-organizational innovation and so on while asserting that collaborations and relations among firms are drivers of technological learning. The classic example of collaboration and innovation in learning is the Silicon Valley case of technological firms in California. Lorenzen suggests that in such cases “firms receive not only incentives for innovating along the vertical dimension of value chains— i.e. from customers and suppliers—but also valuable information feeding into the innovation process” (812).⁶⁷

Knorringa utilized the definitions of bridging and bonding used in the social capital discussions to characterize types of economic relationships. He describes bonding social capital as having predominantly negative consequences for the economic relationships needed for value chain building because as a consequence of the social cohesion in a group, bonding social capital

⁶⁵ Lorenzen, Mark. (2007.) “Social Capital and Localised Learning: Proximity and Place in Technological and Institutional Dynamics.” *Urban Studies*, Vol. 44, No. 4, 799–817.

⁶⁶ Ibid..

⁶⁷ Ibid..

generates a particular type of trust that is ascribed only to members of the group. “Through the norms the group establishes they have the opportunity to control trust to a certain extent, for example by punishing those who take advantage of the trust ascribed to them. Ascribed groups are relatively closed . . . Hence, bonding social capital may create segmented markets with entry barriers for non-group members” (Knorringa).⁶⁸

Knorringa also utilizes Granovetter's term “weak ties” within the economic context. He defines them as “ties [that] exist among members of social groups that are heterogeneous, having different social identifications. Weak ties can occur horizontally, creating networks between loosely connected individuals, organizations and groups, as well as vertically, in hierarchical relations. These are much more open relations, compared with those of bonding social capital, relying on earned trust among loosely connected people rather than on ascribed trust among a homogenous, strongly related group. Hence, bridging social capital is likely to be more beneficial than bonding social capital through a wider spread of positive externalities of social norms, although without bonding social capital there is no fertile ground for bridging social capital to develop”(Knorringa).⁶⁹ This approach is very similar to Humphrey's approach to the importance of first establishing minimal trust between actors so that extended trust can develop later. James Murphy also supports this analysis by saying “in essence, an agent's ability to foster relational proximity with another can be viewed as an important first step toward the development of trusting business ties as it is indicative of one's knowledge, legitimacy, or credibility in the context of a business interaction” (Murphy 446).⁷⁰ Specifically, James Murphy

⁶⁸ Knorringa, Peter. Van Staveren, Irene. (2007) “Unpacking Social Capital in Economic Development: How Social Relations Matter.” *Review of Social Economy*. Vol. 65 (1).

⁶⁹ Ibid.

⁷⁰ Murphy, James T. (2006.) “Building trust in economic space.” *Progress in Human Geography*. Vol. 30, 4. pp. 427–450.

demonstrates how bridging and bonding ties are likely to play a role in local economic development endeavors. Murphy makes the following observations:

Clusters are more likely to initially rely on bonding ties; successful clusters are often characterized by high-density relationships among a variety of actors within a cluster and they usually express a mutual awareness of a common goal.

Value chains are more likely to embody bridging ties; but the transformation of bonding into bridging relationships is difficult to develop at the international level and risky to invest in; power asymmetries in global value chains, particularly in buyer-driven value chains, may enable process and product upgrading for SMEs but are unlikely to allow functional upgrading.

Business associations and regional innovation systems can reinforce the economic impacts of social relations, but they also risk “lock-in” into bonding relationships (Murphy 431).⁷¹

Lorenzen’s work similarly refers to tightly coupled versus loosely coupled social relations. He defines “coupled relations” as the kind of relation that bonds agents together among homogeneous social groups. Tightly coupled relations are “direct (with no intermediaries), encompassing frequent interactions among the agents involved, they are interdependent and often they are firmly coordinated through regulation.”⁷² Such ties are seen in economic relations in the form of long-term networks such as stable value chains and strategic alliances. Lorenzen defines loosely coupled ties as relations which “are fluctuating (on–off) or short-lasting and with relatively little, or only temporary, interdependence. They typically bridge different social groups that are internally strongly coupled” (Lorenzen).⁷³ In business terms these relationships take form in “temporary market organizations: business relations that are established quickly and are not meant to last, as when a furniture-maker buys a shipment of standard components or an

⁷¹ Murphy, James T. (2006.) “Building trust in economic space.” *Progress in Human Geography*. Vol. 30, 4. pp. 427–450.

⁷² Lorenzen, Mark. (2007.) “Social Capital and Localised Learning: Proximity and Place in Technological and Institutional Dynamics.” *Urban Studies*, Vol. 44, No. 4, 799–817.

⁷³ *Ibid.*

advertising agency uses a freelance photographer”(Lorenzen).⁷⁴ Loosely coupled ties assist businesses in forming short-lasting and flexible interactions, spanning the borders between the stable and closed relations constituted by strong ties, and providing agents with access to gossip or information and opinions that strong ties or bonding relationships cannot provide.

h) Power Dynamics and Relationships in Value Chains

The literature on social capital and local economic development both place a strong emphasis on the potentially negative outcome of social capital or strong relationships. Knorringa asserts that “trust is often affected by power relations, which result in inequalities having a negative impact on trust” (Lorenzen).⁷⁵ Thus, it is important to take a realistic view of social capital in the context of real economic relationships which are so often characterized by strong inequalities in power dynamics (Knorringa).⁷⁶ Social structures inevitably incorporate power asymmetries that lead to inclusion and exclusion, relationships of authority and control, as well as to inequalities between people that could range from implicit differential treatment to sheer oppression of one group by another (Knorringa).⁷⁷ Thus, analysis and awareness of the nature of the relationships present in a given local development scenario is crucial for programming. While functional upgrading is not necessarily impossible for a value chain with power asymmetries; outside donors or government actors must understand the proper starting point. In a case where power relationships in value chain are uneven, then programming must start by focusing on how to promote a more even playing field between actors before it can focus on technical assistance with upgrading. Interestingly, these suggestions for practitioners are

⁷⁴ Lorenzen, Mark. (2007.) “Social Capital and Localised Learning: Proximity and Place in Technological and Institutional Dynamics.” *Urban Studies*, Vol. 44, No. 4, 799–817.

⁷⁵ Ibid.

⁷⁶ Knorringa, Peter. Van Staveren, Irene. (2007) Unpacking Social Capital in Economic Development: How Social Relations Matter. *REVIEW OF SOCIAL ECONOMY*, VOL. 65 (1).

⁷⁷ Ibid.

remarkably similar to the suggestions for utilizing social capital pronounced in the previous chapter.

i) Value Chain Governance and the Role of Relationships

The discussion in the previous pages has clarified the opportunities for suppliers who are able to produce to the specifications of large global buyers and how it provides a fast track to upgrading processes and products. A question that economists have asked when studying this phenomena is: “why do global buyers set and enforce the parameters under which other firms in the chain operate.? Why do they go to the trouble and expense of setting up and supervising supply chains? Why do they not simply buy the required products on the market” (Schmitz)?⁷⁸ Hubert Schmitz suggests two reasons:

- *Product definition:* The more the buyers pursue a strategy of product differentiation, for example, through design and branding, the greater the need to provide suppliers with precise product specification and to monitor that these specifications are met.
- *Risk of supplier failure:* The increasing importance of non-price competition based on such factors such as quality, response time and reliability of delivery, together with increasing concerns about safety and other standards, means that buyers have become more vulnerable to shortcomings in the performance of suppliers (Schmitz).⁷⁹

Despite this rationale as to why lead firms would want to oversee supplier firms along the chain, the truth remains that it is expensive for buyers to do so. “Governance by the buyer is costly, requiring asset-specific investments in relationships with particular suppliers.” Buyers have no choice but to specify and enforce parameters when there is a strong risk of profit loss if suppliers do not perform according to the standards or scheduled demanded by the consumer. Schmitz suggests that there are several ways to over time reduce the costs of such oversight. First is through the involvement of external certification authorities. However in many developing

⁷⁸ Schmitz, Hubert. (2004.) “Local Upgrading in Global Chains: Recent Findings.” DRUID Summer Conference on Industrial Dynamics, Innovation and Development: Elsinore, Denmark.

⁷⁹ Ibid.

countries the presence of government oversight authorities or industry associations is not strong enough to ensure the level of governance that global buyers need. In addition “widely applicable process parameters may not be a guarantee of good performance in areas such as quality . . . reliability of delivery and willingness to develop long-term partnerships [cannot always be] captured by certification schemes. Thus, the role of close relationships between buyers and suppliers may remain indispensable (Schmitz).⁸⁰

j) The Role of the Public Sector and Outside Actors (i.e. donors)

In Knorringa’s study he examines the impact of social capital on the performance of two sectors working in a value chain context in Ethiopia and Vietnam. Ultimately, studies such as the Knorringa case studies suggest that trusting attitudes are less important in assessing economic impacts of social relations than measuring what entrepreneurs are actually doing (in terms of investing in networks, or trying to selectively share and cooperate). This was particularly true in the Vietnam case where the government was actively investing in fostering relationships between actors involved in the value chain. Consequently, all indicators for the economic impacts of trust in that case are statistically significantly related to performance, upgrading, and to all firm classifications (Knorringa).⁸¹ This evidence suggests that in developing countries where integration in to a value chain or a local cluster is in its nascent stages, the presence of a facilitator or active broker of relationships is crucial. Despite the fact that many social capital authors contest that social capital is inherently an endogenous phenomenon and cannot be imposed from the outside; there is ample evidence to suggest that outside actors can be effective by facilitating the brokering of social capital by linking previous disjointed actors. In other words

⁸⁰ Schmitz, Hubert. (2004.) “Local Upgrading in Global Chains: Recent Findings.” DRUID Summer Conference on Industrial Dynamics, Innovation and Development: Elsinore, Denmark.

⁸¹ Knorringa, Peter. Van Staveren, Irene. (2007) “Unpacking Social Capital in Economic Development: How Social Relations Matter.” *Review of Social Economy*. Vol. 65 (1).

“while social capital is not an asset that can be imitated from place to place as it is built through organic, bottom–up accumulation, public authorities and policy-making may play a vital role in setting this process in motion” (Lorenzen).⁸²

Based on the need to facilitate the creation of relationships that lead to chain linkages as well as the lack of resources to provide chain governance, there exists a strong need for outside assistance. Essentially, these needs are based on the need to initiate the process of building weak-ties. Humphrey and Schmitz recognize that “multilateral and bilateral donor agencies have for decades sought to find ways of providing effective technical assistance to developing country producers. Progress was at best modest.” Recently these agencies have embarked on experiments of fostering local Micro Small and Medium Enterprise partnership. The central idea is to combine technical assistance with connectivity. The lead firms of chains become the entry point for reaching out to a multitude of distant small and medium sized suppliers. It is recognized, however, that some buyers may require ‘mentoring’ in order to fulfill this funnel and transmission function” (Humphrey).⁸³ Among a few, the UN (through the Global Compact), USAID, UNCTAD, UNIDO, GTZ, and DFID are experimenting with this approach. The following pages will examine one such USAID project that attempted to facilitate the linkages between actors and the technical assistance to the buyer firms in providing mentorship to the suppliers.

Furthermore, strong social capital does not always lead to leveraging those ties for economic use. A region that is rich in social relations may be poor in the type of institutions that add to social capital. Lorenzen points out that “some regions experience institutional learning through social relations, but rather than leading to socially beneficial institutions that promote

⁸² Lorenzen, Mark. (2007.) “Social Capital and Localised Learning: Proximity and Place in Technological and Institutional Dynamics.” *Urban Studies*, Vol. 44, No. 4, 799–817.

⁸³ Humphrey, John. Schmitz, Hubert. (2001.) “Governance in Global Value Chains.” *IDS Bulletin*, 32.3.

openness and dynamism, hence facilitating further institutional learning in a cumulative causation, institutional learning processes in these regions have amounted to misunderstandings and failed experiments with openness and collaboration” (Lorenzen).⁸⁴ This can often be the case in communities which have received outside assistance in building clusters or value chains from donors but program methodology was flawed and ultimately unsuccessful, over time leading to discouraged attitudes towards collaborative economic efforts. In a region low on social capital, such a first co-operative move would, ideally trigger an institutional learning process that will eventually redesign social conventions into co-operation (ultimately facilitating further institutional learning and social capital accumulation). The public can be that one agent that dares to cooperate first, in order to set off a cumulative process of institutional learning (Lorenzen).⁸⁵ This was the clear intention of the Acudir agency in Cuenca as well as the intention of USAID in Cuenca that will be discussed at length in the following pages.

k) In Conclusion

Based upon these findings, it is safe to conclude that social capital in local economic relations is not a simple or clear-cut arena of investigation. We have seen that social capital cannot be regarded as an “individual characteristic or resource” and it can often result in negative power asymmetries. Thus, it is clear that social capital cannot be measured as a single variable within a growth equation. Social relationships do play an extremely important role in local economic development, but impact of such relations is completely context dependent. Knorringa summarizes by saying “social relations are likely to affect every single other economic variable in a production function as a productivity scale factor for each individual production factor,

⁸⁴ Lorenzen, Mark. (2007.) “Social Capital and Localised Learning: Proximity and Place in Technological and Institutional Dynamics.” *Urban Studies*, Vol. 44, No. 4, 799–817.

⁸⁵ Ibid.

representing the (in) efficiency impact of context-specific social relationships” (Knorringa).⁸⁶ Murphy also summarizes the role of social capital in economic development by saying that the “broader significance lies not in describing how factors at different scales influence trust but rather in its unpacking of trust *in relation to* the actual agents, spaces, and places where it emerges and in its *contextualization* of the micro-social processes that drive the relationships and networks that ultimately constitute firms, industries, markets, and economic regions” (Murphy).⁸⁷ This analysis assists the development community to see social capital and trust not simply as an instrument that can be drawn upon, but rather as an entire framework for analysis. It is more important to understand not whether or not it exists in a given context, but rather, how it functions. Murphy eloquently points out the need for “a relational understanding of how the means for establishing and sustaining collaborative relationships influences the development and potential of such ‘ends’ as clusters and production networks” (Murphy).⁸⁸

In sum, the academic community concurs that social capital can play an enormous role in fostering productive relationships between agents operating within a cluster or along a value chain. In conjunction with the discussion social capitals’ potential to be brokered in to different forms of capital; these findings suggest a wide universe of income generating opportunities for economic agents in developing countries. However, these opportunities are wrought with caveats, exceptions, and even potential for abusive relationships and negative growth outcomes.

In the following pages, the case study of the Paja Toquilla, or Panama Hat industry in Cuenca, Ecuador will exemplify many of the aspects discussed in the previous pages. The case will apply the breadth of these theories to a real example of a USAID Value Chain intervention

⁸⁶ Knorringa, Peter. Van Staveren, Irene. (2007) Unpacking Social Capital in Economic Development: How Social Relations Matter. *Review of Social Economy*, Vol. 65 (1).

⁸⁷ Murphy James T. (2006.) “Building trust in economic space.” *Progress in Human Geography*. Vol. 30, 4. pp. 427–450.

⁸⁸ Ibid.

and measure the stock of social capital present among the relevant agents. The question at hand is whether or not this case is consistent with the majority of authors which laud the potential of social capital to create economic links, or, if the reality falls more to the side of the many caveats and expectations and possibly ultimately discrediting the idea of social capital as vehicle for getting on the road to local economic growth.

IV. Methodology

The methodology behind this study is based primarily on an analysis of a case study which exemplifies many of the themes discussed above. Qualitative methodologies were the predominate measure applied.

The goal of the case study approach is to apply the theories behind both social capital and value chain promotion and assess how they manifest in a particular cultural, geographic, and economic context. Ultimately, the goal of this work is to provide guidance for practitioners of development, thus a context based assessment of current projects being implemented in Ecuador will provide a realistic and complex view of the realities of implementing projects based on the theories discussed above. The analysis of a case study serves to highlight the various factors which play a role in the effectiveness of a value chain project – both related and unrelated to the strength of local social capital. The case study will bring to light the importance of individual relationships between real actors and will serve as a basis for applying the theories of value chains and social capital and how they play out in a real-world context. For example, the analysis will bring to light the effects on social relationships and the of the value chain project if there is the presence of an active foreign agent. Furthermore, by applying the theoretical background to a case-specific context, this research is forced to take in to account underlying or overarching themes which may affect the outcome of the projects which are the subject of study; which is to

say that the research takes full account for current and past economic, social, political, and geographic factors which affect the behavior of the subjects and the outcome of the production and may be unrelated to the theories under analysis in this scope of work. Although it would not be realistic to engage in an exhaustive discussion of the many factors which can alter the outcome of the projects being studied, it warrants mention that the author has accounted for such externalities and will mention them as necessary in the analysis of the case study.

A context-based analysis will allow the research to draw conclusions on the validity of the theories presented as applied to reality. Ultimately, such analysis lends itself to drawing conclusions which can also be adapted in to suggestions for best practices and guidelines for project implementation in the future. Ultimately, this research intends to serve as a guide for practitioners and contribute to the body of knowledge on how to effectively implement value chain projects while accounting for the role of social capital in reality-based context.

While conducting field research for the case study the methodology used was primarily qualitative. The most important method for information gathering was through interviews. Information was triangulated through interviews with actors along various links in the value chain and with various actors involved in the implementation of the projects. The interviews were conducted in a semi-structured fashion which allowed for the freedom to delve in to specific topics which provided a more in depth insight to a particular subject matter as it arose. This style also allowed the informant to talk freely, which helped immensely to gauge the kinds of relationships and power dynamics that exist between actors. By interviewing a variety of actors involved in each project, I was able to obtain a comprehensive view of the many factors at play which ultimately affect the outcome of the value chain project. Triangulation of information helped to explain the history and the processes of implementation behind each case. It also

assisted in better understanding the fundamental structure and organization of the various actors involved in each productive sector. By better understanding how the Panama Hat industry functions, the social dynamics of the value chain project became more apparent. The interviews enhance the research by understanding the vision, goals, and concerns of all actors ranging from the foreign donors, the private sector actors, the public sector actors, and the producers themselves. As the analysis will show, each of these actors demonstrated greatly varying perspectives which indeed ultimately played a large role in the relationships between the actors.

Although it was not possible to engage in the traditional definition of “participant observation” research, the semi-structured interviews often took on an active nature as I visited individual producers homes and communities or accompanied consultants to conduct training sessions, toured production plants, observed planning meetings between private sector actors and participated in strategic planning meetings with foreign donors in their Quito offices. This kind of active, observatory research was also useful for understanding the day-to-day process of implementing value chain projects and how the social dynamics between actors are enacted on a daily basis. Moreover, simply by being present and partaking in some cases taking on responsibilities in the implementation of the projects, I was able to absorb a multitude of details about the various factors behind each project than I would have been able to simply through interviews. One of the key dimensions of the participant observation methodology was taking in a “mini internship” with the organization responsible for implementing the projects discussed in this study. By establishing a solid affiliation with the organization and taking on distinct roles and responsibilities, I was able to better understand the goals and visions of USAID and of the implementing organizations. This kind of day to day participation ultimately helped the analysis of relationships between actors to flourish because I was able to compare the perceptions and

communication flows (or lack thereof) amongst actors. This insight allowed me to rapidly understand the general historic, political, geographic and political context of the case study that would have taken much longer to obtain solely through interaction with the project stakeholders. It also allowed me to rapidly gain an overview of the challenges and opportunities of the project and its beneficiaries.

In addition to employing the interviews and participant observation methodologies; this research also reflects the outcome of a survey applied to the members of the weavers associations.

The second survey was applied to each of the hat weavers. The survey is based on the World Bank methodology for measuring stocks of social capital within a given organization or geographical area. The World Bank has published an exhaustive library of tools available such as the Community Profile Interview, the Household Questionnaire, the Organizational Score sheet, the Community Questionnaire, and the Organization Profile.⁸⁹ In general, these tools are designed to help a researcher assess the 6 key dimensions of social capital as defined by the World Bank. In the survey applied to the members of the producers associations, the questions were derived from a mix of the various World Bank tools mentioned above. While it was unrealistic to include all of the questions included in the World Bank tools, the survey employed in this study included questions which allowed the researcher to conduct a general assessment of each of the 6 dimensions. Given the personnel and time restraints of this study, the Social Capital Assessment was adapted by including some questions from each dimension, but not all. To see the survey that was applied to communities in the case study please refer to Appendix 1. The dimensions are defined by the World Bank as follows:

⁸⁹ World Bank Social Capital Assessment Tool, <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTSOCIALDEVELOPMENT/EXTTSOCIALCAPITAL/0,,contentMDK:20193049~menuPK:418220~pagePK:148956~piPK:216618~theSitePK:401015,00.html>

Dimension 1: *Groups and Networks*. The questions here consider the nature and extent of a household member's participation in various types of social organizations, community activities and informal networks, and the range of contributions that one gives and receives from them. It also considers the diversity of a given group's membership, how its leadership is selected, and how one's involvement has changed over time.

Dimension 2: *Trust and Solidarity*. In addition to the canonical trust question asked in a remarkable number of cross-national surveys over many years, this category seeks to procure data on trust towards neighbors, key service providers, and strangers, and how these perceptions have changed over time.

Dimension 3: *Collective Action and Cooperation*. This category explores whether and how household members have worked with others in their community on joint projects and/or in response to a crisis. It also considers the consequences of violating community expectations regarding participation.

Dimension 4: *Information and Communication*. This category of questions explores the ways and means by which poor households receive information regarding market conditions and public services, and the extent of their access to communications infrastructure.

Dimension 5: *Social Cohesion and Inclusion*. "Communities" are not single entities, but rather are characterized by various forms of division and difference that can lead to conflict. Questions in this category seek to identify the nature and extent of these differences, the mechanisms by which they are managed, and which groups are excluded from key public services. Questions pertaining to everyday forms of social interaction are also considered.

Dimension 6: *Empowerment and Political Action*. Individuals are "empowered" to the extent they have a measure of control over institutions and processes directly affecting their well-being (World Bank 2002). The questions in this section explore household members' sense of happiness, personal efficacy, and capacity to influence both local events and broader political outcomes" (Nyhan).⁹⁰

By analyzing all six dimensions, the investigation is able to gauge a much broader understanding of the local context. Furthermore, by inquiring about seemingly unrelated aspects of the local scenario, researchers are more able to discover innovative opportunities for interventions. Although the World Bank methodology suggests the use of both qualitative and quantitative skills the interest of conciseness, this investigation only employs qualitative surveys. As the ultimate objective of this research is to discover connections between social capital and local development, the use of qualitative tools allows the researcher to explore issues

⁹⁰ Nyhan Jones, Veronica. Woolcock, Michael. (2007.) "Using Mixed Methods to Assess Social Capital in Low Income Countries: A Practical Guide." *BWPI Working Paper 12*. The World Bank: Washington, D.C.

of process and causality that cannot be inferred from quantitative data. Qualitative methods allow unanticipated responses and issues to arise. In addition, the study of social relationships, which are inherently complex, lends itself to the use of qualitative measures which allow for the space to demonstrate these complexities that quantitative measures do not.

The actual application of the social capital survey at times functioned more as an interview guide. As a field-based researcher it is crucial to understand how the results of the study could be altered if the methodology was not sufficiently culturally sensitive. In the rural communities outside of Cuenca the members of the weavers associations possessed very low levels of education. Therefore, to hand out a paper survey and ask people to fill it out would most likely have resulted in an incomplete set of responses due to a low level of literacy and ability to understand the questions of the survey. Ultimately, the survey was conducted in small groups of homogenous gender groups of 3-4 people. In Cuenca the surveys were conducted at association meetings but in smaller break-out groups. This setting allowed the participants to feel at ease speaking with me. This allowed the informant to be surrounded by a handful of people with whom the participants could engage in some level of discussion about each question. This allowed the participants to ask the researcher for clarification on the questions and also allowed them to thoughtfully consider the answers to each question. These smaller groups also facilitated a very open and trusting environment between the researcher and informant in which the surveys could act as a conduit to other conversation topics; thus allowing the researcher to fully gauge the informants true feelings on the level of social cohesion and social capital within the association and across the community at large.

An important consideration for the methodology of this research also involved a self-assessment of the researcher, particularly given the fact that the author is not a native Spanish

speaker and is not an Ecuadorian citizen. This awareness was important when deciding on an approach for gaining access to the subjects. In both cases, it was logistically most feasible to obtain introduction to the producers associations through the foreign donors who already possessed a relationship with the subjects. In the case of Cuenca, the consulting firm Ságitta served as the primary connection. While these contacts were crucial in gaining access to the subjects, the researcher must also be keenly aware of the perception of the subject when introduced by the foreign donors. In both locations, it was important to explain to the subjects that the research was being conducted for purely academic reasons and that it was not affiliated in any way with the NGOs. This distinction was important to encourage subjects to speak in confidence without fear of causing any conflict with the donors who were providing very important sources of funding for their projects.

It also warrants mention of the author's particular background and how that influences the perspective of the investigation. As an American citizen living in Ecuador, the author had the opportunity to observe the case study as a relatively objective outsider. However, albeit the fact that this is an academic work, the author's background as a development professional for an international USAID consulting firm should not be overlooked. At the time of publication, the author was actively involved in the research and design for very similar programs in Ecuador funded by USAID. Experiences gained through field research were complemented in many ways by other experiences working in Washington, DC for one of the largest USAID consulting firms and engaged in similar programs all over Latin America. Furthermore, the author was engaged in with several donor funded projects prior to and during the time of research, which allowed her to compare and contrast and ultimately extract important lessons learned for practitioners in the future. Although these experiences are not explicitly referenced in the research, they represent a

depth of experience and breadth of both academic and professional perspectives that substantiate the author's decision to extract applicable lessons learned from the research. Therefore the tone of the research is not meant to be didactic, but rather should be considered a valuable culmination of various valid experiences compounding in to an in depth analysis of a subject area the author is intimately familiar with from a multitude of angles.

In conclusion, this methodology is based on a comprehensive approach to understanding the context of each case study and directly applying both World Bank criteria for measuring social capital and the academia theories on implementation of successful value chain integration projects. This is done not through quantitative analysis of benchmarks and indicators, but through qualitative analysis of social relationships and first hand observation of project implementation. The methodology employed allows for ample triangulation of resources and informants as well as a diverse set of approaches to information gathering. Ultimately, this methodology resulted in research that is not based solely in the ideology of the foreign donors nor in the complexity of local context; it is a blend of the perspective of all the actors involved. Based on this information I have extracted my own analysis.

V. The Case Study: The Paja Toquilla Industry in Cuenca

a) Introduction

In April, 2008 the United States Agency for International Development mission in Ecuador launched a new project called Productive Network (Red Productiva in Spanish). The Productive Network program, established in 2007 seeks to link lead buyers with local producers and suppliers in various industries in Ecuador. One of the several programs included in the portfolio is a project based in the historic colonial city in the south of the country, Cuenca.

The program was originally proposed by the Agencia Cuencana para el Desarrollo e Integración Regional (Agency for Development and Regional Integration of Cuenca - ACUDIR). The agency was formed in the year 2007 and seeks to promote strategic alliances between prominent businesses, local government actors, and local universities for the purpose of promoting regional economic growth and targeted at raising incomes for poor local populations by integrating them in to the regional economy. ACUDIR has been successful as garnering public private partnerships in order to spark growth in various key sectors in the region. For example, with the help of Red Productiva, they were able to greatly improve productive sectors such as leather goods, textile and furniture production, and ceramic tiles. Through these experiences with identifying bottlenecks in targeted industries and bringing key actors together, they identified the potential in the Panama Hat industry of Cuenca. With ACUDIR's local expertise and ability to bring together various actors, USAID decided to direct funds under the Productive Network initiative towards to the Panama Hat industry of Cuenca.

Preliminary analysis of the Panama Hat industry in Cuenca quickly revealed an interesting value chain, consisting of a variety of actors ranging from rural farmers who cultivate the straw used in weaving the hats, to indigenous women who have been weaving hats for generations, to multi-million dollar companies who have exported finished and finished hats to Europe and the US for four generations. The baseline study revealed that the actors who benefited least in the process of production were also those who contributed the most time and specialized labor: the weavers. For years, these women have earned an average of \$3 USD for a hat that requires an average of 4 hours to create. That same hat is often sold in the US or Europe for upwards of \$50. Hats of superior quality can easily retail for hundreds of dollars. Based on the great export potential of the Panama Hats and the obvious lack of economic benefits for the

most important link in the value chain; the Panama Hat industry was an exciting opportunity to utilize market-based strategies in order to strengthen a local industry.

The goal of the program is to bring together the four top exporting companies of paja toquilla hats in the city of Cuenca and encourage them to buy hats directly from the weavers associations instead of buying through an intermediary, which adds about 10% to the price of the hat. The goal of the program is to assist the four exporting companies to access markets in the US and sell finished hats directly to retailers. In order to undertake this endeavor together, the idea is to create a new brand of hats to which they will all contribute initial investment and product supply. The idea being, that by cutting out wholesalers and intermediaries from the value chain, the exporting companies will ultimately be able to fetch a 20% higher price for the product, much of which would be directly transferred to the weavers associations.

In order to accomplish this goal, the program has focused on two key areas. First, is the process of unifying the four exporting companies under one singular brand. This has included a dialogue between companies to establish clear standards of quality of the product, a market study executed in various cities of the US to determine market demand, and dialogue about the structure of the new brand (how much will each company contribute, how will new leadership be selected, how will the new brand undertake marketing and sales of the new line of products?).

The other aspect of the program has been the process of building technical and organizational capacity amongst the weavers associations. Although the art of weaving is one that has been passed down through the generations, training the weavers to meet the difficult demands of US buyers required several months of workshops and training for the weavers. In order to attract retailers in the US, the exporting company must be able to regularly rely on a product of exquisite quality and it must be able to draw upon a significantly larger supply of the

product. Furthermore, in order to export to the US, market studies showed that larger sizes are needed, which requires re-training the weavers to change their traditional style of weaving. Lastly, in order to be competitive in a market strongly dictated by rapidly changing fashions; the weavers must be capable of adapting their weaving styles to the demands of the market.

b) Background on the Panama Hat in Ecuador

Panama Hats, locally known as Paja Toquilla Hats, have been a symbolic export from the region since the mid 1800s. The straw used to weave these intricate and light-weight hats finds its ideal growing environment in Ecuador. Beginning in the 19th century and continuing through today, the hats are woven by hand from this unique raw material by indigenous women living in small rural towns surrounding the city of Cuenca.

Historians suggest that the toquilla straw was used as a weaving material by several indigenous tribes that existed in Ecuador between 500 and 1500 AD. They refer specifically to the Mantena Confederation that consisted of the Huancavilca, Manta and Cara tribes that inhabited the area of Ecuador that is recognized as the birthplace of the weaving tradition. Many historical artifacts suggest that these tribes were skillful weavers. During the colonial era, the Spanish colonizers recognized the beautiful craft of the indigenous weavers and quickly adapted the traditional styles to suit European tastes. Indeed in the beginning eras of the Panama Hat's popularity, the majority of hats were woven in communities throughout the coastal provinces. However, as the international demand for the hats grew in popularity, the export houses of the city of Cuenca played a larger role in concentrating the manufacturing of the hats. Over the course of the 18th and 19th century, weaving skills gradually faded among coastal communities as more communities took up the skill in towns closer to the vicinity of Cuenca. The change in the location of the weaver populations was also influenced by the changes in the industries in the

coastal provinces in which the labor force became increasingly involved with industrial manufacturing and agribusiness.

The Ecuadorian Panama Hat began its journey towards fame when a hat maker from Panama participated in a worldwide fair in Paris in 1855 and displayed a hat woven from straw. The style and practicality of the light weight straw appealed to the Europeans and eventually one found its way in to the hands of the French engineer, Fernando Lesseps. When Lesseps went to Panama to begin construction on the Panama Canal, the light weight hat became a true phenomenon (Rosenholtz, 2).⁹¹ Workers in the Canal Zone found it easy to import massive amounts of the woven straw hats from Ecuador, which led to the boom in the Ecuadorian Panama hat industry. In addition, historians also suggest that even prior to the construction of the Panama Canal, the Ecuadorian hats found a burgeoning market amongst roughly 300,000 americans who migrated from the East Coast to the West Coast between 1848 and 1855 seeking to find wealth in the California Gold Rush. Many of these travelers passed through the narrow pass through Panama on their way towards California, purchasing the light weight hats along their way to protect them from the harsh tropical sun. Despite the overwhelming success that the industry experienced at this time, the sale of most hats to visitors in the Canal Zone led to today's unfortunate misnomer; the "Panama" hat. During the time period between 1850 and 1900 the Panama Hat industry, concentrated primarily in the hands of several key exporters in Cuenca played a significant role in the country's economic growth. At one point in this era, the hats were the third largest export from Ecuador behind large agricultural products like cacao and banana. Throughout the second half of the 19th century, the busiest ports in the country, the ports of

⁹¹ Rosenholtz, Harry. "El Montecristi. Es el Mejor Sombrero de Panama pero Por Cuanto Tiempo?" www.cidap.org.ec/aplicaciones/publicaciones/.../El%20Montecristi.pdf. p. 3.

Guayaquil and Bahía de Caráquez, moved massive volumes of hats off to destinations around the world (Aguilar de Tamariz 7).⁹²

The Panama Hats are recognized as one of the first large scale exports to ever reach significant levels of success from Ecuador. Moreover, the success of the hats abroad were the first instance of Cuenca's transition from a quaint colonial city with a rich tradition of high quality crafts towards the savvy city it is today. Cuenca's ability in the mid 19th century to adapt hat production from a small scale artisanal good to an industrialized product serving international demands opened a significant chapter in the path towards development that Cuenca would take in subsequent decades.

After Banana boom in 1950's, commodity prices declined severely depression the Ecuadorian economy. Production of the hats slowed down significantly in Manabi but continued in Cuenca. This is likely due to the strongly consolidated export houses that existed in Cuenca and did not exist in Manabi. It could also be due in part to the rich artisanal culture of Cuenca that continued to support the market even when the prices fell. Today, many of the same companies that exported hats to Europe and the United States over 100 years ago continue to thrive as some of the exporters of the finest Panama Hats in the world.

c) Defining the Problem: Description of the Region and Target Population

The southern province of Azuay in Ecuador is renowned for its variety of innovative development initiatives aimed at invigorating the regional economy. The capital city of Cuenca is a charming Colonial city recognized by UNESCO as a World Heritage Site. Amidst the charm of the year round mild climate, friendly culture and manicured central plaza and colonial cathedral is a rich tradition of business and intellect. Cuencanos pride themselves in investing in

⁹² Aguilar Tamariz, María Leonor. Tejiendo la Vida; Las artesanías de Paja Toquilla en el Ecuador. CIDAP, Centro Interamericano de Artesanías y Artes populares. <http://www.cidap.org.ec/>

higher education and facilitating a welcoming business environment in order to facilitate future economic growth. This attitude was evident from speaking with several business owners and observing their ability to see beyond the short term gains competing with their neighbors and willingness to engage in conversations about the possibility of collaborating with actors who have traditionally been nemeses. The spirit of innovation and genuine interest in creating a successful future for Cuenca is also evident from conversation with organizations such as INVEC, the local investment agency started through USAID assistance in 2009. INVEC is actively working to address key opportunities to attract investment to Cuenca and to the Azuay province. To do so the founders of the organization have identified areas of weakness of the business climate and are working to address particular areas. Through collaboration with ACUDIR and with the hat producers in Cuenca, they have identified many interesting opportunities to link flourishing tourism sector in the region and in the country with the Panama Hat industry. Although these initiatives fell beyond the scope of this project, they demonstrate the highly collaborative and innovative spirit that exists among the actors participating in this case study. However, Azuay is also a province characterized by high poverty rates and extremely high out-migration from the rural areas to other countries. The provincial government has provided active support to several local industries which exhibit particular potential for growth and poverty reduction impact. Cuenca is home to several nascent yet relatively successful economic clusters in the sectors of ceramics, textiles, furniture, and leather goods.

d) History of Paja Toquilla Sector in Cuenca

The capital city of the province of Azuay is Cuenca and it has long been the most important epicenter for the production and exportation of the famed Panama Hats.

The straw that the hats are made of is cultivated primarily in the mountainous regions of the coastal provinces of the country. Much of the weaving of hats is done by individuals living in isolated communities throughout the provinces of Manabí and Azuay. However, the ultimate destination for the hats has for many decades been the colonial city of Cuenca. In Cuenca, the raw hats are collected by middlemen who travel to various communities and visit small groups of weavers to purchase hats one at a time. They then bring the hats to Cuenca to bargain with the exporting companies to sell them in larger quantities. The hats then go through several transformations before they are finally in the form of the finished product and ready for export.

However, it is important to note that a substantial portion of hats are exported to wholesalers in the exterior in the “bell” form, which means that they are sold un-pressed, undied, and without final garnished like belts. Bell form hats are often sold to large brand name companies like Stetson Hats who finish them using equipment in the US or Europe and put their own brand name label on them. This is a classic example of a value chain which is increasingly dominated by global buyer firms that no longer play as strong a role in actual production but rather in the coordination and marketing of the goods.

For over four generations, the Paja Toquilla Hat industry of Ecuador has been dominated primarily by three exporting companies; Kurt Dorfzaun Hats, Omero Ortega Hats, and Serrano Hats. Each of these company spans a history of three or four generations of hat producers and exporters. The companies hold the reputation as the finest producers of Panama Hats in the country and effectively in the world. For over a century each company has jealously guarded information from one another and gone about business without any form of coordination. Yet ironically, none of these companies has ever been able to export directly to retailers in the United States or Europe due to their small production capacity in relative to the massive demand for the

hats. Interestingly, these companies have operated for generations not only within the same small colonial city, but literally within blocks of one another.

e) The Panama Hat Productive Chain

The capital city of the province of Azuay is Cuenca and it has long been the most important epicenter for the production and exportation of the famed Panama Hats. However, the hats pass hands many times before they finally reach the store front windows in the US or Europe. Panama Hats represent an example of a clearly defined value chain in which the value added to the product as it moves along the chain is substantial. From their initial cultivation to the final consumer there are between 7 – 10 separate actors whose hands they must pass through.

The straw used to weave the hats comes from a species of palm known by its scientific name as *Carludovica palmate*. Locally, this type of straw (“paja” in Spanish) is called “toquilla” which explains the local name for the hats; “sombros de paja toquilla.” The toquilla straw grows in many regions of South America ranging from Panama, spanning many regions of Colombia and down to the southern most province of Ecuador. However, the lush coastal provinces of Ecuador provides the ideal climate for optimum production of the straw. The toquilla straw grows spontaneously throughout the coastal provinces of Esmeraldas, Manabí, Santa Elena y Guayas, and also in the Amazonian jungle provinces Morona Santiago. It is cultivated primarily by small scale farmers. The palm is cultivated in humid areas and requires between 4-5 months to reach the height necessary for harvest (average of 1.5 meters, sometimes growing up to 3 meters long). The farmers harvest the straw with a simple machete then manually peel the outside layer of green exterior from each straw to reveal the strong yet soft and flexible egg white vein of the straws. This interior material is the straw that is used for hat and artisanal weaving. These strands are then placed in large 50 gallon containers of boiling water for

about an hour. Then, the straw is hung to dry in bundles known as “cogollos.” During the drying process of about one week the strands begin to curve in around themselves to form a cylindrical strand about one meter in length. The cogollos then undergo another round of soaking in boiling water and drying. At that point the bundles of long fibers are ready to be sold to the weavers. The whole process is almost entirely manual and done by individual farmers. Although the scope of the project with USAID did not address the toquilla producers and how they could be better incorporated in to the value chain; it warrants to mention that any future programs should certainly take in to consideration the role of the raw input suppliers and the backwards linkages of the weavers to these suppliers (Rosenholtz 3).⁹³

When the straw is ready it is often bought by an intermediary who collects the straw from the region, transports it to towns near Cuenca, and then resells it to the weavers. Occasionally the straw producers are able to travel to the communities of weavers outside of Cuenca to sell their product. The weavers typically travel to a neighboring towns or buy the straw from the vendors for an average of \$3 per “cogollo,” which is a long bundle of raw straw used to weave the hats.

Weavers in this region are almost exclusively adult women ranging from young mothers to senior citizens. The project worked primarily in two communities near the town of Chordeleg, which is on the outskirts of Cuenca. In these communities the project works with two weavers associations by the names of Cañari and Delegsol. They are traditionally Quechua speaking indigenous communities. The women then bring the straw to their homes to weave the hats. Depending on the quality of the hat and the experience of the weaver, the production of each one requires 1-3 “cogollos” of straw and requires from 3-8 hours of work. Each week the women travel to a neighboring town, such as the town of Chordeleg in this case. They bring the hats they

⁹³ Rosenholtz, Harry. “El Montecristi: Es el Mejor Sombrero de Panama pero Por Cuanto Tiempo?” www.cidap.org.ec/aplicaciones/publicacione.../El%20Montecristi.pdf. p. 3.

have woven for the week and negotiate a price with an intermediary who buys from all of the weavers in the region. On average the weavers receive on average \$4 per hat. The intermediary who usually has access to some sort of transport vehicle typically travels to communities throughout the region buying hats. He then transports this stock of hats to Cuenca. Traditionally the intermediary sells the hats at an elevated price to the exporting companies. In the past they have been able to negotiate between exporters and extract prices from 50%-75% higher than what they paid the weavers. The exporting companies then buy the hats based on the current needs for quality, size, etc. All of the transactions to this point are characterized by an extremely informal and relatively subjective system of assigning a grade of quality to each hat and then negotiating a price. Traditionally, hats are divided into only three categories of quality: normal, fino (fine), super fino and (extra fine). This somewhat arbitrary assessment of quality and associated price has left much room for manipulation and exploitation from all actors involved.

Once the exporting company is in possession of the unfinished hats they then send them out to specialized artisans who “asocar” the hats. To “asocar” the hats means to delicately yet firmly pull the remaining straws protruding from the brim of the hat. This process tightens the final row of weaving to prevent it from unraveling. It is a process that can only be done by hand and by skilled artisans. The companies pay only a marginal stipend to these artisans; usually about \$.50 per hat. The hats are then returned to the factories of the exporters and then undergo a long process of bleaching the hats (some are left their natural color). After an average of 15 days of soaking to obtain a crisp white color (they can also be dyed a wide variety of colors, but white is the classic color of the traditional Panama Hat), they are then sent out of the factory yet again. The next step is known as the “compuesto” process. This is the process of stacking several hats then ironing them with a traditional carbon burning iron. This procedure gives the hats extra

shine shiny and forms them in to the basic campana (bell) shape. In this stage of the process they are sent to another kind of special artisan, different from the artisan weavers. It is usually a skill occupied by men only. In Spanish these artisans are called “maestros compositores.” After ironing the hats they place them on a stand and hit the brims with a heavy mallet – this process gives the hats extra pliability. The artisans who complete this process are also paid only nominal wages. Upon their return to the factory, the hats are then pressed in to shape. The final stage is to add final touches such as bands and labels. These last two stages are done in the factory.

Upon completion of the hats the exporting companies, specifically those who are highlighted in this study, then sell the hats based on specific orders to a variety of buyers. Some of the companies sell the majority of their products unpressed and undyed to large wholesalers in the US who then finish the hats using equipment in the US. Some of the companies specialize in selling finished hats to retailers in Europe who typically ask for highly specialized styles and in smaller quantities. Others sell finished hats to wholesalers in the US. Finished hats sold to wholesalers are usually sold for around \$10 per unit. The ultimate retail price for such hats is typically around \$40. These numbers can differ greatly depending on quality.

As one can see from even the most superficial glance at the value chain of the Paja Toquilla Hat industry, there are glaring inequalities between the benefits received by actors along each link of the chain. Essentially, the most labor intensive stage of the process, the weaving is valued 400% less than the price of the final product.

f) USAID Red Productiva/ Productive Network

When the United States Agency for International Development began its initiative to give support to regionally based industries with potential to access value added markets, strengthen productive relationships along the value chain, and ultimately benefit the poor, who are typically

found on the lowest rungs of the productive process; the Panama Hat Industry of Cuenca stood out as an obvious opportunity. In 2007 USAID began its “Red Productiva” or, Productive Network, program in Ecuador. The program works to facilitate private development on a national and regional level. Through the implementing actor, Carana Corporation which is a U.S.-based consulting firm, they have provided technical assistance to nine different local industries throughout the country of Ecuador. By examining and mapping the value chains of each sector they have worked in, the program identifies constraints in the value chain and then designs strategic interventions in order to create an integrated, efficient, and equitable local industry. The methodology used for these projects is centered on the involvement of an anchor firm which exhibits pre-existing or promising potential in their respective export markets. An anchor firm is typically a business situated towards the end of the productive chain, which is to say that they are typically one of the end buyers of the product before it is passed on to the final consumer. These anchor firms usually control a large portion of the local market. In many cases, the quantity and quality standards that the firms demand set the standards for the input market on a regional or even national level. In many developing countries, most of these firms are often limited in their ability to expand due to the limitations of the suppliers and their ability to produce large quantities which consistently meet stringent quality demands in order to access larger export markets.

The Productive Network program identifies bottlenecks in the value chain that are adversely affecting anchor firms’ ability to grow. The objective of these interventions is to generate greater growth potential throughout the industry and generate work which in turn increases household income for small producers. In order to do so, Red Productiva provides technical assistance and training, some equipment, management training, and financial

management training to MSMEs (Micro Small and Medium Enterprises) which serve as providers of services or inputs to the anchor firms.⁹⁴ In the past three years, Red Productiva has provided assistance in various to various burgeoning industries in Ecuador. For example, the program worked with one of the largest national producers of milk and dairy products, Toni, to help small dairy farmers in the northern region of the country meet the sanitation and quality standards of the company. By helping to strengthen the dairy associations and convincing Toni to pay an improved price for the milk, the farmers were able to increase their incomes by selling to a much larger and higher paying buyer. The project was also able to accomplish similar objectives in the industries of ceramic tiles, leather and textile manufacturing, and hot peppers (ají). By many accounts, the Red Productiva was able to accomplish a great deal and was able to identify the crucial connection between enabling economic growth and strengthening small producers in a particular industry. However, as is the case with almost any development project, the reality of the actors on the ground is always slightly more complicated than the “success stories” published on the website would suggest.

g) Program Explanation

In the case of the Paja Toquilla project, the objective was to provide support for the creation of an economic cluster amongst the most influential exporting firms in Cuenca. The project aimed to produce finished hats of superior quality that would be marketed under a unified brand, but with input and subsequent benefits for each of the anchor firms. The goal was to bring the four firms together to jointly develop new products and to jointly create market strategies for the new brand of hats. Ultimately, the project sought to bring better prices paid to the weavers by facilitating direct relationships between the associations of weavers and the exporting companies; cutting out the extra costs generated by the intermediaries. The program objectives

⁹⁴ <http://www.redproductiva.org/content/view/21/16/lang,spanish/>

also state the intention to improve links between associations of weavers. It warrants mentioning that the program also included a component that involved a design competition with students from the University of Azuay to design a more ergonomic chair for the weavers. The winning design was manufactured by the wooden furniture company that was also working with Red Productiva and ACUDIR and awarded to the leaders of the various weavers associations where the project was engaged. This aspect of the project was innovative and addressed the unfortunate fact that many women weavers had developed back problems due to the position that they traditionally assume to weave the hats. However, due to the fact that the component was not directly related to the matters of social capital or local economic development, it has not been highlighted in this study.

The beneficiaries of the program are ultimately three weavers associations and 4 exporting companies (i.e anchor firms). All are located in or around the city of Cuenca.

The project components include:

1. Improvement of the quality of the products produced by the weavers;
2. Improvement of the working conditions for the weavers;
3. Strengthening of the weavers associations;
4. Improvement of the design, finishing, and quality of the hats;
5. Access to new national and international markets.

Based on these objectives and components, USAID's desired ultimate results include:

- a. Increase the number of weavers by 225 persons;
- b. Increased incomes for the weavers;
- c. Creation of one new weavers association in the town of Delegsol;
- d. Improved quality of hats, improved designs and finishings of the hats;
- e. Increased benefits for the entire value chain;
- f. Increased export of the hats;
- g. Creation of a new ergonomic weaving chair for the weavers.⁹⁵

In the following pages, I will draw upon these objectives as laid out by USAID in the analysis of the role of social capital. By breaking down the many aspects of social capital, I will

⁹⁵ <http://www.redproductiva.org/content/view/21/16/lang,spanish/>

be able to see precisely in what way it did or did not play a role in this program's ability to meet its objectives. Specifically, the analysis focuses on the objectives related to improving the production of the cluster and how social capital plays a role.

Explanation of the Actors

h) The Panama Hat Exporters

The Ecuadorian Panama Hat industry consists of dozens of producers and exporters. However, the most prominent actors are centralized among four firms which constitute the largest and oldest Panama Hat exporting companies in the country, and in the world for that matter. These four exporters make up the cluster which was the focus of intervention in USAID's project.

i) Serrano Hats

Serrano Hats was founded by Miguel Crespo in 1905 who began by exporting hats to Panama during the construction of the Panama Canal. The company grew considerably at the turn of the century due to an economic boom in the city of Cuenca. At that time, the Paja Toquilla Hat industry was at the center of the boom. In the 1950's the company acquired another company and acquired its current name, Serrano Hats. At the end of the 1980's the company began to shift production from unfinished to finished hats. Today, 90% of production is dedicated to finished hats and 95% of total production is exported abroad. Their primary buyers are small retailers in Europe who request small and varied orders. The current CEO of the company, Fernando Moreno, has been the catalyst of the cluster program. His collaboration with the USAID program greatly influenced the decision of the other exporters to get involved with the project.

ii) Homero Ortgea

Homero Ortega Hats is one of the oldest exporters in Cuenca. It is a family run company spanning three generations. The company was originally established in 1898 by Aurelio Ortega. In 1972 the company was officially incorporated and has steadily grown its product line and market access ever since. At the moment the company has 50 employees. Currently they specialize in the export of finished hats to over 28 countries. Before the formation of the cluster, the company operated by receiving an order from a wholesaler or a small retailer from abroad. Based on that order they place an order with the intermediaries to collect hats from the weavers according the specifications of the order. Generally speaking, the lead exporters highlighted in this study had the capacity to fill orders for between 1000-2000 finished hats. Retail markers in the US typically place orders for a minimum of 10,000 hats at a time. European retailers on the other hand tend to place much smaller orders for finished hats. When the project first began, none of the exporters possessed the capacity to fulfill such large orders. Once the hats are collected from the weavers the intermediaries deliver them to the company and engaged in a traditionally combative and problematic negotiation process.

iii) Kurt Dorfzaun

Kurt Dorfzaun Hats began in 1939 and was officially founded in 1942 by a German immigrant who bore the company its namesake. The business started originally in Colombia but later moved to Ecuador. The company primarily exports unfinished “bell” hats to wholesalers in the US and to a lesser extent to Italy and Germany. The company prides itself on being a supplier to some of the most recognized hat brands in the world such as Stetson Hats. Like the other exporters, Dorfzaun Hats worked for generations in complete isolation from the other exporters, despite their geographic location literally within blocks of one another.

iv) Bernal Hats

Bernal Hats is the fourth company included in the cluster project, but is actually a much smaller company. The company was included in the cluster project to ensure the participation of a smaller company and because Bernal Hats has previous experience exporting unfinished US Hats to the US market, which could be of help in the formation of the new brand.

i) The Weavers

The weavers of the hats are almost universally women who inhabit rural communities throughout the provinces of Azuay and Manabí. In the case of the four exporting firms examined in this case, all of their hats are made produced in a handful of indigenous communities within an hour of Cuenca. The Red Productiva project focused specifically on two communities of weavers. These associations are called Cañari and Delegsol. Despite the fact that there are dozens of communities of weavers in the region, the project chose to work specifically with these communities due to the fact that there were pre established weavers associations. These associations consist of about 20 women, mostly indigenous, who have been weaving paja toquilla hats for generations. At the time of observation it was difficult to determine the exact number of members in the association due to the fact that it was a nascent organization and there was still an inconsistent level of participation. The weaver associations serve as a local organization where the women come together to weave and most importantly, to aggregate their hats to be sold in large quantity. By doing so, they are often able to negotiate a better price from the intermediaries who come to the communities to buy the hats (and then resell them to the exporting companies). In the case of the association of Delegsol, the weavers association did not exist prior to the introduction of the USAID project in the community. In the case of Cañari, the organization was established in 1991. The associations are run by an elected president and an

elected council of 2-3 “vocales” or committee members. For the purpose of this investigation, the focus was primarily on the association located in the small township of Delegsol.

Throughout the life of the USAID project, the weavers were incorporated in to the new system of working directly with the exporting companies. The most crucial aspect of the project was to assist the weavers in learning how to produce hats that met the standards and the quality demands of the US markets. European and other Latin American markets traditionally order smaller sized hats and are somewhat tolerant of small imperfections in the hats. The American market, however, poses new challenges for the industry. The weavers must learn to weave hats virtually devoid of any imperfections- which means learning how to weave with clean hands and learning to select unflawed straw to weave with. The US standards also require the women to learn to weave a larger sized hat. Additionally, the new markets set forth rigid standards for product uniformity. Therefore the weavers are learning to precisely calculate the number of rows woven in to each hat to ensure they are of uniform size and quality. Technical assistance is provided to the weavers associations for a period of 6 months to learn how to comply to the new norms. The Cuenca-based consulting firm, Ságitta, is the company hired by USAID to conduct the weekly sessions with the weavers. While Ságitta provides the business-oriented training to ensure that the hats meet market standards; CIDAP provides the technical training on the actual art of weaving. Through USAID funding, the weavers have been provided with rulers and wooden head models to assist in measuring and maintaining consist sizing. However, at the time of the study, the weavers were still in the initial process of getting accustomed to the new norms.

At the time the study was conducted, one of the biggest threats to the weavers associations was the diminishing number of young people interested in learning the trade. Traditionally, the intensive labor required to weave the hats and the very low monetary

compensation has deterred young people from an interest in carrying on this unique tradition. The USAID project decided to address this issue directly by convincing the exporting firms to increase the price they would pay the weavers prior to the establishment of the new brand. This involved an initial investment on the part of the buyers to incentive the weavers to learn the new modes of production and to attract more people to learn the skills of weaving. Given that the new unified brand, Alfaro Hats, was not scheduled to begin exporting and thus generating new revenue for at least several months; this was a demonstration of good faith from the buyers to the suppliers. It was an important move in creating the first step towards fostering trusting relationships between the buyers and the suppliers and deterring suspicion of the weavers that they were position for a potentially exploitative buyer-supplier relationship. Prior to the creation of the cluster the weavers of Delegsol would receive an average of \$4.5 per hat of third tier quality. With the investment of the buyers, they now \$4.8 per hat. Weavers now receive up to \$5.5 for a top tier hat whereas they used to receive \$4.5. This price is expected to rise by \$1-2 more after the cluster begins to export.

As a result of the training assistance and price incentives, interviews with the buyer firms and with Ságitta confirmed that the quality of the hats had distinctively improved since the initiation of the project. The next step in advancing the project plan is to significantly increase the quantity of production. This will be done by enlisting the weavers of the association to reach out to other women in the community who know how to weave and encouraging them to take an active role in the weavers association. They must also train the new members of the association on how to weave according to the new standards. This step in the project is crucial because Alfaro Hats ability to access US retail markets hinges on their ability to consistently fill the larger quantity of orders. This means that the weavers must incorporate more members to the

organization and must maintain a steady member base in order to sustain larger output over time. Interviews with the association president and with the weaving technical expert from CIDAP suggested that weavers associations tend to wax and wane over the years. If inconsistent participation continues, the buyers may face a serious input supply problem.

j) Ságitta Consulting

Ultimately, the funds provided by USAID to involve the consulting firm, Ságitta, were the most effective aspect of the project. Ultimately, Ságitta was the key actor in bringing the exporters together to discuss the prospect of forming a unified brand. They were also the key player in providing training assistance to the weavers on how to weave in accordance with market demands and norms. They were successful at not only convincing the exporters to talk, but at facilitating the entire process of designing a new product line, conducting a market study, and helping the exporters develop a production system for the new brand that would be beneficial to all actors involved. They were also successful at selecting the weavers associations that would be included in the project and connecting them directly to the buyers who previously only bought through intermediaries. Ságitta played the key role in creating weak ties between all of the actors involved. In the case of the exporting firms, Ságitta also helped the initially weak ties between companies develop in to trusting, tightly coupled relationships; despite generations of rivalry and isolation. The trust developed between these actors allowed them to pursue a new strategy for strategic functional upgrading.

The greatest concern with the successful performance of Ságitta is concerning the sustainability of the value chain after the funding for their assistance is no longer available. When technical trainings are no longer available and there is no longer an actor facilitating the overall coordination of the chain the question begs; who will fulfill this role? Some literature

suggests that it could be filled by the new firm itself which would have to assume a larger chain governance role. Other literature suggests that the public sector should play this role.

k) Government and Non-Profit Actors

The role of the public sector in the Red Productiva project is largely symbolic. ACUDIR at first glance seems to be an interesting and innovative government agency seeking to foster public private relationships and facilitate regional economic upgrading. Interviews with the agency revealed a strong level of dedication and interest in the project. They also seemed to possess a strong knowledge of the local economic landscape that a foreign donor would not be able to possess on its own. In that sense, ACUDIR is a useful counterpart for the project. However, the day to day activity of the agency in the project is nominal. Perhaps, according to Schmitz and Knorringa's theories, the public sector is precisely that; to facilitate the bridging of relationships among economic actors and to provide a strategic macroeconomic vision. The role of ACUDIR in the project is by no means negative, but at best it is neutral. It suffices to say that the opportunities for a larger role of the public sector were not necessarily fulfilled in this project. ACUDIR was not necessarily poised to assume Sagitta's role of facilitator at the conclusion of the project namely due to a lack of industry-specific technical capacity within the agency.

l) Challenges to the Industry Prior to the Cluster

Prior to the creation of the cluster, most of the exporters faced similar challenges and threats to the long term expansion of their businesses. First and most importantly, their access to larger exports markets, specifically the United States, is marred by the quality and quantity of hats they are able to obtain from the weavers. Since the Paja Toquilla industry is in every sense a cottage industry, the most important link in the input supply chain is a hand-made good. The{ XE

"Prior to the creation of the cluster, most of the exporters faced similar challenges and threats to the long term expansion of their businesses. First and most importantly, their access to larger exports markets, specifically the United States, is marred by the quality and quantity of hats they are able to obtain from the weavers. Since the Paja Toquilla industry is in every sense a cottage industry, the most important link in the input supply chain is a hand-made good. The" } obvious implications for the exporter businesses are that the input supply (the "bell hats" or unfinished hats) are often wrought with irregularities and inconsistency. Moreover, the labor intensive and time consuming nature of the product implies a much lower output per hour and per laborer than any industrial product. These quality and quantity limitations have always been the largest barrier for the exporters to inserting themselves in the American markets which tend to demand quantities exorbitantly larger and tend to enforce extremely high standards of consistency.

Another common problem for the exporters has always been the controversial role of the intermediaries, including those who work at links further below and further above in the productive chain. The role of the intermediaries is to buy from individual weavers and sell to the companies are widely regarded as an unnecessary link in the chain that does not create any added value to the product. Traditionally, these intermediaries have been responsible for negotiating prices for each and every single hat and then transporting them from the rural areas where they are woven to Cuenca where the exporter companies are located. They often receive an average of 50% commission per hat sold to the exporters. After the hats are processed and ready for export, they are almost always sold through wholesalers in the US or Europe. This is also considered an unnecessary link in the chain that does not add value to the product. This step is required for companies who are unable to produce the quantity to meet the demand of the retail market. The wholesalers then in turn sell the hats to the retailers at 30%-40% higher than what they pay the

exporting companies. Thus, there are two distinct points in the chain in which the final price of the product is raised and the value of the product is not. According to interviews with the executives of each exporter company, these steps represent significant profit margins between the cost of the producing the hat and the final retail price that are not being translated to the actual producers of the product (be it the weavers or the export companies).

In addition to challenges with quantity, quality, and excessive steps in the productive chain; each of the exporters is restricted by limited technology and production capacity. Each of the four exporters featured in the project possesses some sort of technologically specialization, but no one of them exhibits an advanced level of production capacity or technology in all of the stages of production. For example, Homero Ortega possesses one of the most elaborate bleaching systems as well as equipment for adding finishings to the hats. On the other hand, Serrano Hats possesses a more elaborate system for pressing hats.

Lastly, one of the most pressing challenges to the exporting companies in the Panama Hat industry of Ecuador is due to rising competition worldwide. Ecuador can rightly claim that it is the only country in the world to produce the particular type of straw used for exquisite quality hats. However, in recent years straw hat industries in Brazil, Colombia, Mexico, and Peru have steadily captured more and more share of the market. While these industries are producing lower quality hats and do not therefore occupy the same market niche as the luxury Ecuadorian hats; they have exhibited more cost efficient and larger scale production capacity. Their presence in the market and their ability to produce cheaper and more consistent hats (albeit of lower quality) has had a depressing effect on prices throughout the entire industry. Another source of competition has also come from hats produced in China which utilize a synthetic, paper-based straw and are produced primarily with machinery. Again, these hats do not infringe on the luxury

level of the market, but their drastically lower prices have a de-valuing effect on the industry.

Lastly, Italian-made straw hats represent the strongest competition on the luxury end of the market. Italy's long standing history of producing high quality artisan products combined with a tenacity for accessing worldwide markets makes them a very imminent threat to the Ecuadorian industry.

m) Vision of the Cluster and Level of Commitment From Actors

Over the course of the field research conducted among various participants, it became clear that this was an interesting and unique situation in which behavior changes were observable at the early stages of the project. Through interviews with the driving actors behind the project such as the deputy chief of party of Red Productiva and the lead technical officer on the project, I learned that prior to the beginning of the program the exporters had almost no contact among one another. Marred by several generations of rivalry, the four largest exporters of the finest quality Panama Hats in the country had coexisted within blocks of one another for several generations without ever speaking to one another. When Red Productiva began, it seemed like a large feat to even suggest, no less, prompt these arch rivals to work together. However, after a few meetings between project staff and individual company executives, the many benefits of working together to reach greater scale became apparent. Within the first few months of the program, the exporters began to meet to discuss common challenges to doing business and examine ways in which each company was addressing each challenge. The exporters quickly realized that they shared in common many challenges and often felt constrained by their relatively small sizes in their ability to access larger markets. As meetings progressed, the exporters saw that the advantages of working together could potentially far outweigh the risk of sharing some trade secrets. In reality, this concern became almost obsolete as the exporters realized that each one possessed a unique market niche that did not directly compete with the others, yet they all suffered from similar problems with input supply. For example, Homero Ortega specializes primarily in finished hats and is known for producing hats responsive to the latest styles in the US and Europe. They are also strong in their ability to comply with timelines when filling orders for buyers. Kurt Dorfzan hats have reached a high quantity of production that the other producers can not yet achieve, but they primarily specialize in selling unfinished hats.

Bernal Hats, while they are the smallest producer, is the only one of the cluster that has managed to access US markets. Lastly, Serrano Hats possesses great knowledge of the niche European markets and is advancing in style and fashion innovations, but is struggling to produce the quantity that the others could. They have also been a catalytic leader pushing the image of the Panama Hat as a cultural icon of the region and of the country. Through these conversations, the exporters agreed on an area of collaboration that could substantially improve business for all four actors, without introducing more competition in to the local market. They decided that collaboration was opportune and essential for gaining access to the finished hat market in the US. In the past, none of the companies were able to achieve this due to the fact that their production was not consistently large enough to satisfy the demand for huge US wholesalers. However, if they could manage to streamline their production systems and sell the hats in bulk together, then they would be much more capable of gaining order from the large US companies such as Dorfman Pacific, HatCo Inc, Bollman Hat Company. Prior to the intervention of Red Productiva, these four companies occupied about 75% of total Panama Hat exports from Ecuador. However, their combined exports only represent 2% of the finished panama style hats that are sold in the US. This fact revealed that although the Panama Hat industry was viewed as relatively successful, their hold on the market was nominal compared to the vast potential that existed.

Over the course of the first year of the project actors such as ACUDIR and Sagitta assisted the companies in finding ways to collaborate towards the end goal of exporting to the US together. The solution that arose was the idea to create a new brand that would be comprised of inputs from each company and the profits would be divided among each company. The name chosen for the new brand was Alfaro Hats, which alludes to the Ecuadorian hero and past president, Eloy Alfaro, who is often pictured sporting a crisp white Panama Hat. With the assistance of ACUDIR as a facilitator of dialogue, the companies were able to identify common problems and common solutions to production. One of the first moves of the newly formed Alfaro Hats was to examine their up market and down market needs. They quickly launched a market study of the styles that the US buyers were looking for and created a lean but precisely targeted product line that consisted of styles originated from each of the companies. They also worked closely with Sagitta to establish direct relationships with weavers associations. They began to work through Sagitta to help weavers produce hats that met the size and style demands of the US market. For example, the study found that the US market tends to order hats in larger

sizes than the weavers were traditionally accustomed to producing. The exporters also began to examine their internal production systems which involved touring one another's factories; a monumental step in this previously highly secretive industry. They began to find compliments to one another's constraints. For example, as they began to devise plans on how to divide the production of the hats they were able to utilize the technologically advanced dyeing systems of Homero Ortega to dye the hats an array of colors, the skilled sewing team of Serrano Hats to add finishing bands, bows, labels etc.

Based on in depth interviews with the executives of each of the companies, there was ample evidence to suggest a genuine level of commitment on the part of all of the involved parties. Despite the long history of isolation between exporting companies, this Productive Network project was successful at bringing the exporters together. As a result, the level of communication and institutional willingness to collaborate for a common purpose was remarkably high.

From the perspective of the weavers, the commitment to the project seemed to run only as deep as the potential for tangible results. It suffices to say that in subsistence farming communities such as Delegsol, the flexibility of the weavers to dedicate extra time or resources to the new system of production is extremely limited. One successful aspect of the project at the time of observation was the initial investment of the exporting companies to pay the weavers up to \$.50 more per hat in exchange for increasing their quality and output. Although Serrano Hats were not yet generating increased revenue for the companies, the executives realized that the weavers could not afford to shift their modes of production without some incentive or proof of the potential benefits.

One cause for concern about the sustainability of the project derived from the strictly business outlook of some of the exporter companies. While some of the executives interviewed saw the project not only as a potentially profitable investment, but also as a socially responsible

resolution to the inadequate prices paid to the weavers; others expressed their willingness to pull out of the project if it became inconvenient to the company and expressed relatively little concern with the potential repercussions for the weavers associations. While this is an uncontrollable and inevitable variable in all market-based development efforts; it is an important reminder not to approach such projects with an overly idealistic view that the involvement of the private sector will be the ultimate resolution to development of a local economy.

n) Social Capital Analysis: Relationships Between Actors

Generally speaking, the results of the social capital measurement survey applied to the weavers association of Delegsol revealed an extremely low level of social capital. It should be noted that the association of Delegsol is a very new organization which had only been established for three months at the time the survey was applied. The association consists of approximately 20 members, all of whom are women. The members of the association have 4 children on average and in almost all cases the income from the hats is the only cash income for the household. Otherwise, they are almost exclusively subsistence farmers. There is also a high rate of out migration and a high incidence of remittance income, although the amount of money received is marginal. The study revealed that the weavers association was the only social group that the women voluntarily belonged to. Most of the survey participants said that they were also affiliated with the local water organization, but that affiliation was required by the municipality and most did not actively attend the meetings. There was no perceived benefit to actively participating with the water organization. The participants almost unanimously revealed little or no social life outside of the home; no communal festivities, celebrations of holidays or trips in groups. There was also very little mention of voluntary participation of projects which benefit

the greater good of the community. The municipality does require participation in periodic “mingas” which are groups community members called together usually to contribute manual labor to projects related to public communal infrastructure. However, non-participation in the mingas results in a fine. Only one participant stated that she regularly and voluntarily participates in projects related to the Catholic church in the community. When asked about who they perceive as available to assist them if they ever needed assistance be it financial or other all participants answered that they could call upon immediate family or neighbors. However, none of them mentioned any strong, trusting relationships with people beyond this small circle of family or close neighbors. Lastly, when asked straightforward how they perceive the level of unity among within the community all of them replied that they perceive the community to be extremely disunited. On the other hand, there was however a strong perceived benefit to being affiliated with the weavers association. All of the participants expressed interest in continuing participation in the association both for the economic benefits and for the social benefits. Several interviewees revealed that they have begun to form friendships with some of the women from the association and that they have interacted outside of association meetings with other members that they did not interact with prior to the creation of the association.

The analysis extracted from this survey is quite apparent. Delegsol exemplifies an extremely poor indigenous, Andean community in which the women must bear the greater part of the burden of managing all aspects of the household. Most women spend an average of four hours a day weaving. The rest of the day is spent cultivating crops, caring for animals and children and cooking. It comes as no great surprise that in a community with such economic constraints that the level of social interaction and cohesion is extremely low. Furthermore, communities with high out-migration typically demonstrate lower levels of social capital due to

the fact that women must assume an even greater role in all aspects of household management. The survey reveals that across the six dimensions of social capital addressed the results are generally very low. However, noting that the association was only developed several months prior to the study, there is evidence that social capital is increasing. The ability of the women to democratically elect leaders, the evidence that affiliation with the association has led to other social relationships, the perceived economic benefits of affiliation with the association and all indicators that the presence of the weavers association has the potential to facilitate the development of further social capital. If the project is implemented with this opportunity in mind, the project should take an interest in strengthening the association which is likely to have a ripple effect on the overall level of social capital across the community. These observations lead to one of the most important issues addressed in this study. The lack of social capital despite the thus far successful value chain project begs the question; what then *is* the role of social capital in value chain integration if USAID was able to implement the project in a community seemingly deprived of any real level of social capital. Furthermore, despite the admonishment of Fukuyama and Putnam that social capital cannot be created from the outside; Delegsol seems to exemplify a case in which an association has manifested in a veritable desert of social capital in response to an effort introduced by outside actors. However, this provocative contradiction is not as earth shattering as it seems upon further consideration. First of all, it is crucial to consider that the simple presence of an association does not equate to the presence of social capital. The focus rather should be on *how* to promote the creation of social capital via a local vehicle such as a producers association. In this case, the weavers association exhibits the potential for generating social capital, which could then be brokered for other forms of capital. Thus, in order to create a robust local social capacity, the project should look to strengthen aspects such as leadership,

access to information, and creation of standards and norms within the association. Furthermore, the literature on social capital suggests that all forms of capital are more likely to compound exponentially and transform in to other forms of capital – but only *after* a group is able to access *some* form of capital to begin with. Prior to the USAID project, and based on the survey results, Delegsol possessed neither economic nor social capital.

It can be argued that the strategy in this project was not to introduce social capital, but to introduce economic capital by providing the weavers with the access to markets and technical information on how to produce value added products (i.e. demand-driven styles/higher quality hats). The successful implementation of this project resulted in increased income and greater future earning potential for the weavers. These opportunities have in turn allowed the weavers to start to build social relationships in the process and incentivized them to work in collaboration with one another. Thus, the analysis suggests that the standard literature which suggests that social capital can lead to economic capital should be seen from a new proverbial chicken and the egg correlation. In this case, the evidence suggests that the introduction of economic capital has alternatively promoted the growth of social capital.

However, the observations of social capital in this study cannot be summarized solely through analysis of the weavers associations. Indeed, the other half of the equation is exporting companies and the relationships between the weavers and the exporters.

As alluded to in previous pages of this study; the four exporting companies operated in virtual vacuums of isolation from one another prior to the introduction of the USAID project. After just 7 months of meetings the cluster had reached a remarkable level of inter firm trust and cooperation. Through open discussion, the firms quickly realized that they faced similar restrains to upgrading. Many of these constraints were surrounding limitations to production due to

limited physical capital (bleaching, pressing, finishing equipment) or limited access to input goods (raw woven hats from the weavers). The idea to create a new brand of hats which would consist of products produced by all four firms resulted from the need to collaborate in order to access larger markets that were out of reach as individual firms. This case provides a classic example of what Hubert referred to as collaboration that leads to innovation. Interestingly, as the months progressed and the firms continued to meet and discuss in detail the role of each firm in the production of the new brand, Alfaro Hats, the level of trust continued to grow. In the process, each firm learned from his colleague new tips and information about the production process and about nuances of the markets they work in; thus proving the theories that strong relationships among economic actors lead to greater access to information. However, an interesting observation of this process is concerning the fact that the four men behind the formation of Alfaro Hats occupied a very advantageous socio-economic strata. Thus, while we cannot deny the fact that social capital was strengthened as a result of this project; we must recognize that the social capital formed was based upon an ample stock of pre-existing physical and human capital. As educated and successful business owners, their ability to broker capital from one form to another is significantly higher than the weavers who must form social capital spontaneously.

Another interesting critique of the high level of bonding capital among the exporters is surrounding their prospects for fostering bridging capital. Humphrey and Schmitz suggest that trust is most likely to emerge among groups of similar socio-economic actors. This holds very true for the level of trust that has been established among the exporters. However, they also go on to say that in the modern globalized context, such relationships among similar actors are losing relevance. Relationships based on functionality and processes are increasingly more important than those based on a common identity. USAID played the key role in initiating the

relationship between the exporters and the weavers associations. However, the nature of this relationship remains weak. Only time will tell if the exporters will be able to recognize this new trend and invest time and effort in fostering a tightly coupled relationship with the weavers. By investing in strong ties with the weavers the exporters will mitigate the risk of the weavers losing interest or feeling exploited. The weavers would likewise benefit from greater opportunities for upgrading if they were able to emerge from a captive network relationship to a balanced network relationship.

VI. LED Analysis

Based on the research and best practices suggested in the literature review, this project exhibits various characteristics of a value chain project worthy of further analysis. Based on observations in the field and through the many interviews conducted with various actors, the project exemplifies an innovative approach to bring actors together for the first time who traditionally considered one another competitors. The level of success at inspiring collaboration was undoubtedly impressive. The initiative to create an entirely new brand to which each exporting company would contribute equally is an innovative approach to sharing risk as well as widening the opportunity for scaling up and accessing larger export markets. The project proposes a model that comprehensively reflects the research on utilizing geographic proximity of actors in a given industry to enhance coordination and facilitate scaling up efforts.

Observing the project in implementation reveals a few apparent risks or challenges that loom on the horizon as the project moves toward its goal of increasing product quantity and quality in order to access value added markets and ultimately pay better prices to the actors at the bottom of the value chain. When the project began, the buyer-supplier relationship clearly fell in to Humphrey and Schmitz's classification of "market based." Transactions were made at arms

length and on ad-hoc schedules. Like the classic definition of a market based relationship, transactions were made in cash and only upon examination and delivery of the good. Weavers often sold through intermediaries, thus a trusting relationship between the buyer and supplier was literally non-existent. Prior to the project, the weavers had very limited knowledge of international market demands and buyers had no ability to guarantee that they could meet such demands.

With the introduction of the USAID program many of these issues have been addressed. The buyers and suppliers have now established a direct relationship and can probably be classified as a captive network: an economic relationship in which the lead firm sets the parameters under which others in the chain operate. In addition, the weavers seem to have reached a new level of process upgrading which allows them to transform inputs and outputs more efficiently by introducing new market norms for weaving which fetch a higher market price. The exporters also shifted along the upgrading scale from product and process upgrading to functional upgrading, which now allows them to acquire a new function in the chain; that of retail exporter to the US. The initial investment of the exporters to pay more for the hats bought directly from the weavers association should be noted as a commendable first step in building a trusting relationship and reducing the sense of vulnerability of the weavers.

However, the next steps beyond these initial advances seem more complicated. Indeed, a look in to the future of the chain is not as bright as the recent history. The prospects for further relationship evolution and chain upgrading are not necessarily equal for all of the actors involved. Namely, the project appears to lack built in mechanisms for promoting learning and the capacity to innovate amongst the suppliers (weavers). The nature of the buyer-supplier relationship seems entrenched in a quasi-hierarchical or captive network framework. While the

exporting companies have been able to foster a balanced network type relationship, resulting in the pooling of resources to conduct market studies and identify the specific demands of the latest fashions in the US; the local weavers remain completely at the will of the demands of the exporting companies. While it may not be realistic to suggest that the weavers could eventually reach a level of upgrading that rivals the role of the exporters, the project does not account for even a gradual process of upgrading capacity building amongst the weavers. A more critical look at this situation may reveal that while the project demonstrates a strong likelihood of improving the incomes of the weavers, it is not necessarily empowering them to acquire greater authority or autonomy in the industry. In other words, the prospects for further product or even functional upgrading are bleak.

In cases where social capital is strong, making the leap from producer to innovator is usually an organic and self-evolving process. This is because groups with high social capital are more likely to possess aspects like “weak ties” which link them to other resources of information and eventually lead to other economic opportunities. For example, if the weavers association did possess a strong level of social capital, their participation in the project could theoretically be a stepping stone towards their branching out on their own to establish ties with other hat processors and exporters in the country. They would be able to draw upon weak ties to establish relationships in which they were able to play a stronger role in the negotiation of prices of inputs and prices received for the hats. They would also be more likely to draw upon weak ties to gain more market information which would enable them to adapt their designs to the changes in fashion/market demands. However, based on observations, the reality is that the project does not provide any such social capital building outlet which empowers the weavers to take a more proactive role in the value chain. The project does not promote weavers to interact with other

weavers associations in the region, nor does it provide any portals through which the weavers could gain access to new market information, nor does it teach the weavers skills in organizational leadership or negotiation skills. It could be easily argued that these activities simply were not a part of the “scope of work” of the project and that weaver empowerment was not an objective of the project. However, if the goal is ultimately to stimulate sustainable local economic development through integration in to the global value chain; then local ownership and capacity building which demonstrates how the work of a weaver is a part of the larger chain is an integral aspect of ensuring the sustainability of the endeavor. In addition, the project did not exhibit a systematic way of ensuring that technical capacity and quality control was institutionalized. The local consulting firm, Ságitta, as well as the technical expert in weaving from CIDAP (Centro Interamericano de Artesanis y Artes Populares) provided invaluable training to the weavers about standardization of hat production, but there was no observable guarantee that these standards would be carried out in the long run as associations change leadership and members of the association come and go. This observation was made at the beginning of the part of the program that sought to train trainers who could pass on the information to fellow weavers.

This aspect of the program was intended to contribute to the sustainability of sharing of technical information among weavers but the activities missed one crucial link. The program does not address how to maintain a sustainable flow of information between the exporters and the weavers. This is precisely the role of a business development service provider or a university would play in a more advanced industry. For example, Peter Knorringa’s case study on the ceramic tile industry in Brazil addresses the important role of the universities in ensuring changes in market demand to various actors along the value chain. At the time of

implementation, Sagitta and CIDAP played an important role in facilitating communication and continually advancing technical assistance to the weavers which enabled them to learn about the clients' needs and gain the skills to adapt their product accordingly. However, at the time of observation, Red Productiva was directly funding both actors to participate in the program. The exporters had begun to communicate directly with the weavers, but it was unclear how the exporters would communicate market needs to all of the weavers in the future in a cost-effective, not overly time consuming manner. The distribution of models to use for uniform hat sizing and of rulers for uniform size of rows of weaving was a positive step towards institutionalizing the new production norms, but in order to ensure long term sustainability, after the technical experts are no longer present at each association meeting; there needs to exist a further step in centralizing information on technical production standards. For example the exporters could consider funding, in conjunction with contribution from various weavers associations in the region, a technical information center. This center could function as a clearinghouse for housing information on norms, standards, trends, and market information relating to all aspects of the value chain. Based on examples of other economic clusters, such centers of information are usually housed within universities. In the case of the *paja toquilla* industry, CIDAP and ACUDIR could conceivably play a long term role in fulfilling this function. However, at this time, it is not ideal to see a crucial link in the flow of market information that appears to be unsustainably dependent on donor funding.

The ability of the weavers to take ownership of quality and quantity of production is not only a threat to the empowerment of the local weavers, but poses a long term challenge for the interests of the exporting companies. If the quality and quantity of the product deteriorates after the help of the USAID funded technical assistance is gone, the exporters will not be able to meet

the demands of the foreign markets. It is in the interest of the exporters to have a consistent source of weavers able to produce large quantities of high quality hats without the continuous need for oversight or intervention from the exporters. Thus, the link between building local social capacity and the sustainability of the overall effort at integrating the value chain grow increasingly apparent.

VII. Project Analysis

Throughout the author's conversations with various actors who have been involved with the Panama Hat industry for many years, the question was posed several times about the validity of the value chain and anchor firm methodology. Some informants, such as the technical expert from CIDAP who had worked closely with hundreds of weavers for many years expressed a concern with pushing the weavers associations to behave like businesses. He suggested that many artisanal sectors have remained artisanal due precisely to the fact that these products originate from unique cultures that have been isolated from the mainstream economy. By encouraging the artisans to adopt a more business minded approach to their product, one runs the risk of losing the unique quality of an artisanal good. However, successful artisan projects around the world would likely argue that channeling sales of products through more lucrative channels is not fundamentally contradictory to preserving a local culture. Additionally, the value chain methodology seeks to allow producers to focus as much as possible on the production of their product by linking them with other actors along the chain who take on the responsibility of further processing and marketing. Based on the analysis of this case, it seems that the weakness of the association in its ability to meet market demands is not due to a lack of business capability, but much more related to their weak associative and organizational capabilities to

orchestrate unified production of scale. This is much more related to the lack of social capital amongst the weavers than to an imposition of a foreign system.

Other critiques of the anchor firm model suggest the opposite extreme. Several programs in the past through different donors saw any actors that stood between the weavers and the end consumers as unnecessary “middlemen.” Previous programs attempted to provide weavers with the ability to create finished hats which would allow them to sell directly to consumers. However, these experiences quickly revealed that selling the hats is a much larger challenge to assume than simply obtaining the materials to add ribbons and a hat press.

After becoming intricately acquainted with the Red Productiva program, it seems like the level of social and human capital is low enough to justify working through an anchor firm. In addition, one must take in to account the ultimate program goal which was to create exponential regional growth, which is often much more effective when done through a large economic actor whose success is likely to have a ripple effect on the entire local economy. This type of program objective more than justifies the decision of the project to work through exporters rather than attempting to help the weavers become exporters themselves.

This type of local economic development methodology is sometimes criticized by observers claiming that it is unjust for the final retailer or even the exporters to receive a high profit margin than the weavers who unarguably dedicate much more intensive labor to the production of the final product. This is an argument that is made repeatedly by outside observers on development programs in almost any country and in dozens of industries. The reaction to this criticism has prompted some development programs to attempt a different methodology which focuses more on strengthening producers associations such that they are capable of not only producing the raw product, but also capable of processing and marketing the final good. This methodology seeks to

help local producers capture a much larger market segment and therefore theoretically also capturing much larger profit margins. However, in cases where the associations are weak and possesses little or no knowledge about the market beyond their current position; the time and investment required to reach the end goal is substantial. Such an approach would require many years and millions of dollars to help the association morph in to a fully function exporting organization. The risks associated with this kind of investment are also very high. In the dynamic international economy of today, the nuances of consumer demands change daily, the price of labor and inputs are constantly adjusting and the political economy of many countries, particularly in Ecuador is increasingly unstable. In this environment, economic actors need to be nimble and flexible. This is extremely difficult for an organization that invests significant time and effort in to growing to be large enough to assume many roles along one single production chain rather than specializing in one particular role and learning how to adapt it to various subsectors. For example, this could be said of the coffee sector in Colombia which has been remarkably late in joining the organic movement due to the Coffee Federation's deep involvement for over 50 years in the entire chain of production in the regular coffee sector. Thus, when approached with the question of how to utilize donor funds in a way that will disperse the assistance to as many beneficiaries as possible and spark exponential growth in a sector, the decision to work through an anchor firm is logical. The weakness of this methodology is the risk of losing opportunities for functional upgrading for producers, but this weakness can and should be addressed in program design. In the opinion of this author, the weaknesses of the anchor firm methodology are still far fewer than of the methodology which seeks to combine steps in the value chain.

VIII. Return to Cuenca Ten Months Later

Ten months after the initial conclusion of this study, the author had an unforeseen opportunity to return to Cuenca to meet with some of the exporting companies. Although on this occasion the author was not in the seat of student researcher, but rather as a development professional preparing for a potential USAID project that would continue the efforts of Red Productiva. This fortuitous opportunity allowed the author to discuss with Fernando Moreno and with the team at Red Productiva in Quito about the current status of the cluster development efforts among the hat exporters.

The conversations revealed that the exporters were successful in organizing their production systems such that the production of Alfaro Hats complemented the strengths and weaknesses of each company. They also achieved a system in which each company was comfortable with the gains received in comparison to the level of effort and resources they were willing to provide. This synergy of production is an important accomplishment in the development of an economic cluster. The exporters also managed to update the market study of the US and adapt the styles of hats to the style and regional trends of various consumers in the US. This demonstrated ability to assess and adapt to changes in demand is also a significant milestone.

On the supply side, i.e. the weavers, the prognosis was not so encouraging. It seems that the weavers have been unable to reach the quantity that the exporters require to meet the demands of the US market. Moreno affirmed that they could easily obtain this supply by buying through middle men, but that would defeat the mission of the project which was to provide higher prices directly to the weavers. In speaking with project staff at Red Productiva, I learned that the project was able to attract another group of weavers to participate in the project that was

initially uninterested. Apparently the increased success of the weavers that were participating in the project was sufficiently convincing to the weavers in the neighboring community to entice them to strengthen their association and sell directly to the exporters. According to the social capital analysis, this event suggests that the economic incentive to participate in the project inspired the weavers association of the neighboring community to work together in order to improve the quality and consistency of their product so that it could be sold to the cluster. Thus, we observe another instance in which the social capital was not necessarily strong prior to the introduction of another kind of capital. Representatives of Red Productiva claimed credit for inspiring the generation of greater social capital by introducing a new economic opportunity and concluded that it was a significant success of the project.

However, conversations with Fernando Moreno reveal another side to the story. Despite the projects' success at attracting more weavers to work with the cluster, the businesses are still far from satisfied with the quantity and quality of the hats being produced. This suggests that despite the assistance from Sagitta and CIDAP, the weavers have been unable create a strong association capable to enforcing quality control standards amongst their own members. Without having the opportunity to visit the weavers again it is difficult to say why they have not been successful in producing to the standards that the market demands despite considerable technical training. Perhaps it is because the weavers are unable to dedicate sufficient time to weaving amidst their other daily obligations. Perhaps the association has been unable to retain membership and therefore has seen a decrease in production and/or must dedicate time and resources to training new members. Perhaps there has been a change in leadership in the association which has not been replaced, leaving the weavers without clear direction. Regardless of the specifics of the situation (although it would be very useful to know more), one can

conclude that the weavers associations continue to lack the organizational capacity to orchestrate consistent production amongst their members. In this particular case, the weaving skills amongst the members are already well entrenched. What is clearly lacking is the ability of the weavers to apply these skills in a way that addresses the demands of the buyers, which ultimately comes down to a question of associative capabilities. Without the ability to dive further in to the particulars of the current situation of the weavers, one can still conclude that this is an aspect of the Red Productiva program that was demonstrably weak. In an effort to extract lessons and incorporate the theories discussed above, one can conclude that importance of understanding the level of social capital prior to engaging in such a project is crucial. Had the program done a social capital assessment such as the one conducted in this study, the current problems with associative capabilities among the weavers would have been easily foreseen. In heeding Coleman and Fukuyama's admonishment to practitioners who attempt to draw upon or create social capital where it does not exist, the Red Productiva program made an erroneous assumption that by creating a weavers association, they would be creating the social capital needed to sustain a long term relationship with the exporters. The program clearly did not consider the necessary elements of social capital that Coleman considers fundamental such as trust, channels of communication and norms among a group. As the survey revealed, the weavers possessed none of these at the beginning of the program. Thus we can conclude that the program expected the weavers association to form bridging and bonding linking with other actors along the value chain, but failed to account for lack of fundamental building blocks of social capital within the group.

Another conclusion that resulted from conversations with the cluster exporters ten months later was with regards to the forward linkages in the value chain. By focusing so much

on the US market, Moreno suggested the cluster has surpassed opportunities for Alfaro hats to grow as a national brand. He asserts that there is still a huge unmet demand for fine Panama Hats within Ecuador. Specifically, he refers to the promising relationship between tourism and the hats. As tourism to all part of Ecuador grows exponentially every year and as the profile of the tourists grows, the national economy has observed that tourists are spending more money per person than ever before. Thus, as the high end tourists that previously only visited the Galapagos are now venturing to other sites on the mainland, the opportunity to sell fine goods to them has greatly expanded. Moreno revealed that among the artisanal shops in the major hotels in Ecuador, or artisanal/tourism shops in Quito, Guayaquil and on the Galapagos there are very few high quality Panama Hats available to sell to tourists. Moreno suggested that this forthcoming market should be a focus of Alfaro hats but to date, the cluster has only concerned itself with the far more ambitious, perhaps overly ambitious, goal of exporting to the US. However, as an objective observer, it should be noted that my informant on this subject now holds a relatively prestigious political position and is openly affiliated with the current government of Ecuador. That suggests that the informant's views are very much in line with the current political economic push towards keeping as much economic activity within Ecuador's borders and is less enthusiastic about opportunities for economic expansion through interaction with foreign markets.

IX. Conclusions

Ultimately, the case of the Panama Hat industry reveals several fascinating conclusions about the role of social capital in a value chain strengthening project. The literature on social capital clearly lauds the presence of intangible things like embedded and autonomous relationships, communal norms and sanctions, trust, and bridging and bonding ties as paramount

to a deposit of wealth waiting to be exploited. The academic rationale behind theories on local economic development that speak of the opportunities for poverty reduction through integration into the global economy also pay acute attention to the importance of trust and social relationships in the modern global marketplace. However, both academic worlds, despite the rarity of their encounters with one another, make thorough caveats to the possibility of negative and exclusionary repercussions of strong social relationships in the economic development context. Such relationships often lead to elitism, exclusion, and patterns of being trapped within one social paradigm without the ability to reach beyond.

In the case of the Panama Hat value chain, the evidence suggests a well executed methodology that follows the text book advice on value chain integration to a tee. The USAID project was extremely effective at identifying bottlenecks in the chain and making strategic human and physical capital investments in order to overcome these hurdles. Instead of trying to compensate for the private sector, which too many donors have mistakenly done in the past, the project successfully facilitated relationships between key players and effectively brokered these relationships so that the sum of the parts of the local Panama hat industry amounted to something much greater than when the project began. The project accounts for the importance of social relationships in building value chains by helping the exporters to develop strong levels of bonding among one another. They also introduce the weavers to key external or weak ties that allow them to interact directly with the exporters. Ultimately, the project succeeded in strengthening relationships along the chain enough such that the ultimate goal of raising income for the weavers was accomplished.

Despite these advances, analysis of the social relations brings to light some serious concerns about the sustainability as well as the ultimate empowering qualities of the project. A

closer analysis of the project reveals that opportunities for learning and process upgrading for the weavers are significantly lower than they are for the exporting companies. The observation begs the question: what is the definition within the development community of “integration.” If the definition is placated by simple process upgrading and a nominal increase in income; then the project was a success. If the definition of “integration” is meant to imply more complex process and functional upgrading and an implied improvement in supplier empowerment and independence; then the project has missed its mark by a long shot.

This analysis is not meant as a criticism of this particular project, but rather as a much needed revelation of the deceptively complex reality of value chain programs. We see that actors that are already socially and economically endowed with capital are very well poised to benefit from the role of an outside actor which fosters new social relationships (as in the case of the exporters). However, for the actors that initially possess little or no capital of either the social, human, or physical form, then the role of a “relationship broker” may be of little use because they are less capable of utilizing these new relationships to their advantage. The evidence suggests that the intervention chosen by the outside actor should be adapted to the specific needs of the beneficiaries. Populations which possess a lower level of social capital may need higher levels of human or capital investment in order to strengthen the levels of social capital. As the project invested in the human and physical capital in the form of models and technical training, then the strength of the weavers associations showed signs of growth and stabilization. In the case of the exporters, the physical and human capital was already present and thus the projects’ investment in social capital (by facilitating relationships) was a very effective investment. Ultimately, the research reveals that a pre-existing stock of social capital is not necessarily the egg that comes before the chicken when it comes to jump starting market based development

programs. It seems that all forms of capital are equally crucial to the development process and that it is the responsibility of practitioners which kind of capital investment will yield other forms. The prospects for poverty reduction through value chain integration remain extremely encouraging. It is the hope of the author that with a more in-depth understanding of the social realities behind market transactions which programs such as the USAID Red Productive project will continue to improve.

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Annex I

Cuestionario para las asociaciones de tejedoras de paja toquilla

Datos básicos:

1. ¿Por cuanto tiempo ha pertenecido a este grupo de tejedores?¿:_____
2. ¿Cuales son los fuentes de ingreso más importantes para su familia?_____
3. Cuantos hijos/hijas tiene:_____
4. Estado civil:
 - a. Casadab
 - b. Soltera
 - c. Viuda
5. Ingresos promedio de su hogar por mes:_____
6. Ingreso promedio por mes de tejer:_____
7. Como se utiliza los ingresos de tejer los sombreros:
 - a. educación para los hijos
 - b. comida
 - c. transporte
 - d. ropa
 - e. cosas para la casa
 - f. otra _____

1. Grupos y redes

Hay Miembros de su hogar que pertenecen a algún grupo? Cuales Grupos:

	Nombre del grupo	Miembro de la familia	Nivel de participación (escala 1-5)
Grupo o cooperativa decampesinos / pescadores			
Otro grupo de producción			
Asociación Comercial o de comerciantes			
Asociación de profesionales			
Gremio o sindicato			
Comité del barrio/ parroquia			
Grupo religioso			
Grupo político			
Asociación o grupo cultural (músico/ baila)			
Grupo de créditos, fianzas, ahorros			

Grupo de educaron (por ejemplo grupo de padres y profesores)			
Grupo de salud			
Grupo de manejo de agua/riego			
Grupo deportivo			
Grupo de jóvenes			
ONG/Fundación			

2. De todos los grupos a los que pertenecen los miembros de su hogar, nombre el más importantes para su hogar.

3. ¿Cuántos días de trabajo dio su hogar a este grupo el año pasado? _____

4. ¿Cuál es el principal beneficio que se obtiene al unirse a este grupo?

- a) Mejora la subsistencia actual de mi hogar y el acceso a servicios
- b) Es importante en casos de emergencia/ en el futuro
- c) La comunidad se ve beneficiada
- d) Diversión/ Recreación
- e) Beneficio espiritual, nivel social, auto estima
- f) Otros (especificar) _____

6. En los últimos cinco años, ¿la cantidad de miembros del grupo ha disminuido, se ha mantenido o ha aumentado?

- a) Ha disminuido
- b) Se ha mantenido
- c) Ha aumentado
- d) No sabe /no está seguro

7. ¿Cómo se seleccionan los líderes de este grupo?

8. En general, ¿el liderazgo del grupo se ejerce de manera efectiva?

a. Sí b.

No

9. ¿Este grupo trabaja o interactúa con otros grupos con objetivos similares en el vecindario / aldea?

- a) No
- b) Sí, en ocasiones
- c) Sí, con frecuencia
- d) No sabe / no está seguro

10. ¿Este grupo trabaja o interactúa con otros grupos con objetivos similares fuera del vecindario /aldea?

- a) No
- b) Sí, en ocasiones
- c) Sí, con frecuencia
- d) No sabe/ no está seguro

11. ¿Cuál es la fuente más importante de financiamiento de este grupo?

- a) Los derechos de los miembros
- b) Otras fuentes dentro de la comunidad
- c) Fuentes fuera de la comunidad
- d) No sabe/ no está seguro
- e) No corresponde

12. ¿Quién fue el fundador del grupo?

- a) El gobierno central
- b) El gobierno local
- c) El líder local
- d) Miembros de la comunidad
- e) No sabe/ no está seguro
- f) No corresponde

13. ¿Aproximadamente cuántos amigos cercanos tiene en la actualidad? Estas son personas con las que se siente cómodo, puede conversar sobre temas privados o llamar para pedir ayuda.

2. Confianza y solidaridad

14. Si repentinamente usted necesitara una pequeña cantidad de dinero ¿cuántas personas ajenas a su hogar inmediato podrían ayudarlo?

- a) Nadie
- b) Una o dos personas
- c) Tres o cuatro personas
- d) Cinco o más personas

15. El año pasado, ¿cuántas personas con algún problema personal se dirigieron a usted para pedirle ayuda? _____

16. Hablando en forma general, ¿diría usted que puede confiar en la mayoría de las personas o que no necesita ser demasiado prudente en sus tratos con otras personas?

- a) Se puede confiar en la mayoría
- b) No se puede confiar en nadie

18. Si un proyecto de la comunidad no lo beneficia directamente, pero tiene beneficios para muchas otras personas del vecindario / aldea, ¿contribuiría con tiempo o con dinero al proyecto?

Tiempo:

- a) No contribuiría con tiempo
- b) Contribuiría con tiempo

Dinero:

- a) Contribuiría con dinero
- b) No contribuiría con dinero

3. Acción colectiva y cooperación

19. El año pasado, ¿trabajó usted con otras personas de su vecindario / aldea para hacer algo por el beneficio de la comunidad?

- a) Sí
- b) No

20. ¿Cuáles fueron las tres actividades principales el año pasado? ¿La participación fue voluntaria u obligatoria?

1. _____ Voluntaria / Obligatoria

2. _____ Voluntaria / Obligatoria

3. _____ Voluntaria / Obligatoria

21. En resumen, ¿cuántas veces en el año pasado usted o alguien de su hogar participó en actividades de la comunidad? _____

22. ¿Si hubiera un problema con el suministro de agua en esta comunidad, ¿qué probabilidades hay de que las personas cooperen para tratar de resolver el problema?

- a) Muchas
- b) Algunas
- c) Ni muchas ni pocas
- d) Pocas
- e) Muy pocas

23. Supongamos que algo muy desafortunado le sucede a alguien del vecindario / aldea, como una enfermedad grave o la muerte de uno de los padres. ¿Qué probabilidades hay de que algunas personas en la comunidad se organicen para ayudarlo?

- a) Muchas
- b) Algunas
- c) Ni muchas ni pocas
- d) Pocas

e) Muy pocas

4. Información y comunicación

24. ¿Cuáles son las tres fuentes de información más importantes acerca de lo que está haciendo el gobierno (como extensión agrícola, trabajo, planificación familiar, etc.)?

- | | |
|--------------------------------------|---------------------------------|
| a) Parientes, amigos y vecinos | g) Grupos o asociaciones |
| b) Informativo de la comunidad | h) Socios de trabajo o negocios |
| c) Periódico local o de la comunidad | i) Líderes de la comunidad |
| d) Periódico nacional | j) Un funcionario del gobierno |
| e) Radio | k) Las ONG |
| f) Televisión | l) Internet |

25. ¿Cuáles son las tres fuentes de información más importantes acerca del mercado (como trabajos, precios de artículos o cosechas)?

- | | |
|--------------------------------------|---------------------------------|
| a) Parientes, amigos y vecinos | h) Socios de trabajo o negocios |
| b) Informativo de la comunidad | i) Líderes de la comunidad |
| c) Periódico local o de la comunidad | j) Un funcionario del gobierno |
| d) Periódico nacional | k) Las ONG |
| e) Radio | Internet |
| f) Televisión | |
| g) Grupos o asociaciones | |

26. ¿Cuántas veces usted ha viajado en el año pasado? _____

5. Cohesión e inclusión social

27. ¿Cómo clasificaría la unidad social dentro de este vecindario?

- a) Muy unida
- b) Unida en parte
- c) Algunas disputas y conflictos
- d) Gran tensión y conflicto
- e) Gran conflicto y violencia

28. ¿Cómo clasificaría la unidad social de este vecindario con otros vecindarios cercanos?

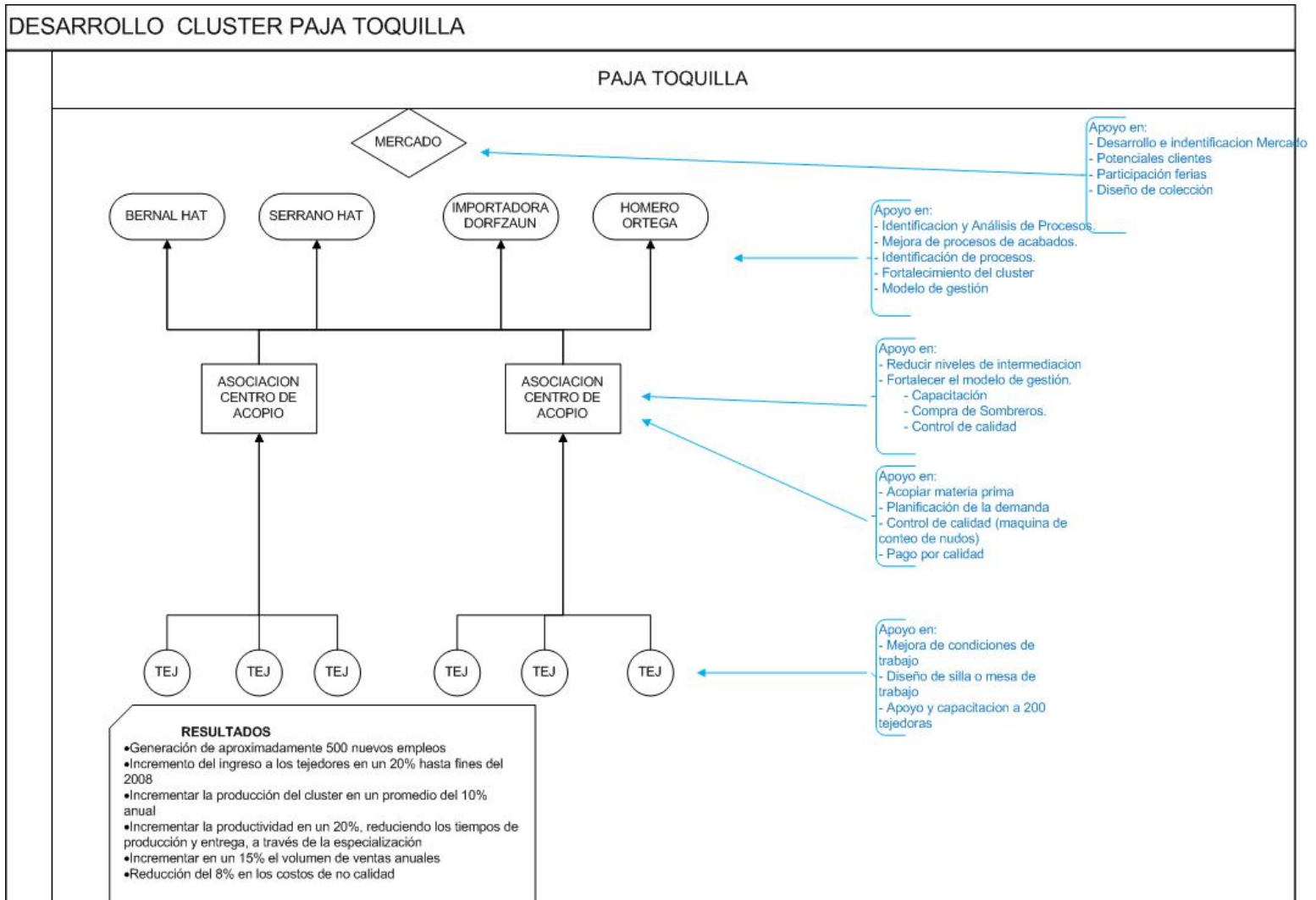
- f) Muy unida
- g) Unida en parte
- h) Algunas disputas y conflictos
- i) Gran tensión y conflicto
- j) Gran conflicto y violencia

29. En el último mes, ¿se ha reunido con personas en un lugar público para conversar, comer o beber algo?

- a) Sí ¿Cuántas veces? _____
- b) No

30. En el último mes, ¿le han visitado personas en su hogar y han ido al hogar de otras personas?
- a) Sí ¿Cuántas veces? _____
 - b) No vaya a la pregunta 5.17

⁹⁶Annex II. Value Chain Map of the Ecuadorian Paja Toquilla Hat Industry



⁹⁶ USAID Ecuador, 2009. Carana Corporation.

