Close-up

SME guide
to value chains
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SME guide to value chains
This guide offers small and medium-sized enterprises (SMEs) insights on negotiation and collaboration with lead firms in international value chains. It addresses topics such as compliance with standards and regulations, contractual relationships, production and performance management, types of upgrades and strategies to avoid ‘lock-in’.

It also highlights five company success stories, illustrating how small companies grew to become regional or global leaders. The guide is based on chapter excerpts from the 2017 edition of the SME Competitiveness Outlook – The region: A door to global trade.

Title: SME Competitiveness Outlook 2017 – Close-up: The SME guide to value chains
Publisher: International Trade Centre (ITC)
Publication date and place: December 2017, Geneva
Page count: 32
Languages: English, Spanish
ITC Document Number: CEES-17-111.E

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Acronyms

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<th>Acronym</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>GATS</td>
<td>General Agreement on Trade in Services</td>
</tr>
<tr>
<td>ISO</td>
<td>International Organization for Standardization</td>
</tr>
<tr>
<td>ITC</td>
<td>International Trade Centre</td>
</tr>
<tr>
<td>MENA</td>
<td>Middle East and North Africa</td>
</tr>
<tr>
<td>MERCOSUR</td>
<td>Common Market of the South</td>
</tr>
<tr>
<td>R&amp;D</td>
<td>Research and development</td>
</tr>
<tr>
<td>SME</td>
<td>Small and medium-sized enterprise</td>
</tr>
<tr>
<td>TISI</td>
<td>Trade and investment support institution</td>
</tr>
<tr>
<td>WTO</td>
<td>World Trade Organization</td>
</tr>
</tbody>
</table>
Small and medium-sized enterprises (SMEs) represent the backbone of every economy. They tend to make up for over 95% of all firms, but only relatively few of them are active in foreign markets. For example, in the European Union, SME exporters contribute 34% of total exports, and in ten South-East Asian countries, they account, on average, for 30% of total exports.¹

The reasons why SMEs hold back from exporting are multiple. They often do not feel confident that they have enough market-relevant information. For others, the costs to get products through the border or set up foreign distribution networks appear unsurmountable.

Some risks and costs can be reduced significantly if SMEs manage to connect to international value chains. In these cases, lead firms often provide key information related to demand and requirements. Distribution and logistics are also often facilitated by lead firms. Evidence suggests that linking up to value chains can generate significant spillover effects, notably through exposure to new management methods, new technologies and new materials.

The extent of the benefits that SMEs draw from such engagements depends largely on the relationship the SME establishes with the lead firm. The contractual side of that relationship is particularly important. For SMEs to take full advantage of market opportunities arising from international economic integration, they need to be proactive within international value chains.

This guide provides SMEs with critical information on how to best approach negotiations and collaboration with lead firms and other suppliers within international value chains.² Guidance, handbooks or frameworks on supply chain management or international expansion strategies are easily available. They tend, however, to be written from the point of view of the lead firm within supply chains.³ Guidance on internationalization strategies targeted specifically to SMEs is rare. This guide therefore fills a demanding gap.

### How to increase SME bargaining power

**The recipe:**
- Increase complexity of products or services
- Enlarge pool of buyers

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1. For example, in the European Union, SME exporters contribute 34% of total exports, and in ten South-East Asian countries, they account, on average, for 30% of total exports.

2. Guidance, handbooks or frameworks on supply chain management or international expansion strategies are easily available.

3. Guidance on internationalization strategies targeted specifically to SMEs is rare.
Successful involvement in value chains requires three critical capacities:

- an ability to identify business opportunities and market niches based on unique products and services;\(^4\)
- strong managerial and operational competencies; and
- flexibility to adapt to changing demands.

This guide provides SME suppliers with actionable advice:

- on how to get selected by buyers;
- operate successfully within international value chains; and
- upgrade or expand within these chains.

It describes what SMEs need to consider when entering value chains and the expansion options available to them, based on the governance structure of the chain they are in. A key determinant to success is the firm-level capacity of SME suppliers, which can enhance or detract bargaining power with lead firms. Attracting more buyers or accessing a spectrum of buyers gives SMEs further advantage.

**How to grow a successful business**

**Enter, operate and upgrade within value chains.**

- **Get selected by buyers**
  - Use market information to target value chains
  - Demonstrate compliance with standards/regulations

- **Operate successfully**
  - Define contractual relationships
  - Meet buyers’ needs for volume, quality, efficiency
  - Improve managerial capacities
  - Use market information to target value chains
  - Demonstrate compliance with standards/regulations

- **Upgrade or expand**
  - Analyze performance to learn and improve
  - Enhance core firm capabilities
  - Focus on the type of upgrade
  - Implement growth strategies to avoid “lock-in”

The guide also showcases five company success stories, illustrating how small SMEs grew to become regional or global leaders. These examples tell us that there is no single blueprint for success. While every success story is unique, together they demonstrate that a start-up in a developing economy can become a global lead firm.
SMEs that enter international markets through value chains often are allocated standardized business functions in the chain. These usually are at the lowest value-added point in the chain, and are not necessarily very profitable. Such positions also may not be sustainable, as newcomers can threaten these activities relatively easily. As a result, SMEs carrying out standardized business functions tend to have weak bargaining power within the chain.

SMEs can strengthen their position by thinking along the two axes in Figure 3:

1. Upgrade path: move into more complex, higher value-added business functions.
2. Increase the customer base: join more value chains at regional and/or global level or expand direct sales.

**Value chain governance matters**

Governance is about the power and ability to exert control along the chain regarding what is produced (including design and specifications); how it is produced (processes, technology, quality systems, standards); and how much and when it is produced (scheduling, logistics, etc.). Those exerting power in a value chain can be buyers or producers of final goods. In producer-led chains, the final product manufacturer has most power; in buyer-led chains, the power lies with the retailers and branded manufacturers.

For SME suppliers, the governance structure has a major role in determining the flow of knowledge and competencies that boost their own performance. As a result, governance structures are crucial to whether SMEs benefit from the value chains they are in.²

There are five types of value chain governance, as shown in Figure 1. These range from a market-driven chain to a hierarchical one.

- **Market:** This structure has the lowest power asymmetry. The supplier produces a low-skill intensive, standardized intermediate product. It sells the product to a wide range of international buyers, which have little, if any, influence over the supplier.

- **Modular:** Modular governance involves more complex business functions that can be easily codified, and therefore turned into modules. The lead firm provides the software that simplifies these otherwise complex activities for the supplier to execute.

- **Relational:** The supplier executes complex business functions that cannot be codified, creating mutual dependence between supplier and buyer. Interactions are dense, knowledge is tacit, and they exchange complex information with little codification of product specifications. Supplier capabilities usually are strong, which is necessary to execute these complex business functions.

- **Captive:** The business functions usually can be codified and thus entrusted to a low-capacity supplier. This puts the supplier in a precarious situation, as it becomes heavily dependent on the lead firm, hence the term ‘captive governance’.

- **Hierarchy:** A lead firm might fully absorb the supplier via vertical integration if the supplier’s capabilities are relatively weak and the ability to codify the business functions is low.
FIGURE 1 Five types of value chain governance

<table>
<thead>
<tr>
<th>Governance type</th>
<th>Complexity of transactions</th>
<th>Ability to codify transactions</th>
<th>Capabilities in the supply-base</th>
<th>Degree of explicit coordination and power asymmetry</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market</td>
<td>Low</td>
<td>High</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>Modular</td>
<td>High</td>
<td>High</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Relational</td>
<td>High</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Captive</td>
<td>High</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Hierarchy</td>
<td>High</td>
<td></td>
<td></td>
<td>High</td>
</tr>
</tbody>
</table>

Note: *Suppliers are frequently SMEs.

FIGURE 2 Captive governance in countries with low Human Development Index


FIGURE 3 Bargaining power of SMEs within international value chains

Note: Market, modular, relational, captive and hierarchical are types of value chain governance.
Source: ITC.
Modular governance and relational governance structures are likely to be most promising to suppliers. For suppliers to have these types of relationships with lead firms, there are two conditions:

- Suppliers must fulfill relatively complex business functions.
- Suppliers must have relatively high capacities.

Avoiding capture

Being dependent on one or few buyers weakens a supplier’s negotiating position, particularly for prices and purchase conditions, such as lead times and quality specifications. Nearly a quarter of suppliers depend on their main buyer to purchase more than half of their production⁶ (Figure 2), according to data from a global survey of suppliers to value chains.

Captive governance occurs more frequently in developing than in developed countries. In countries with a high Human Development Index, only 20% of suppliers have a high risk of dependency, compared with 54% in countries with a low Human Development Index.

Increasing SME bargaining power

SMEs are likely to have a stronger bargaining position when they offer complex business functions and have a large number of buyers. Figure 3 reflects this, situating the five types of value chain governance around two axes representing complexity of business functions, the number of buyers and their type.

Market governance structures involve many buyers and the captive and hierarchical structures just one buyer. Hierarchical and relational governance structures are marked by relatively high complexity of business functions.

Figure 3 shows that suppliers can increase bargaining power by moving up the value chain and increasing the customer base. Indeed, it is likely that the only firms operating in the top right area of Figure 3 are large, international lead firms.
This guide is for SMEs interested in entering international value chains and for enterprises already inside value chains aiming to upgrade and improve their performance. The intent is to present the value chain business model as a means for boosting competitiveness, profitability and long-term sustainability of firms. The guide explores a wide range of factors SMEs can consider when entering, operating and upgrading in regional or global value chains.

SMEs have significant impact on the performance of the value chains they are part of. Often they supply commodities and low-cost labour in developing and emerging economies, and are innovators and technology specialists in developed economies. There are extensive empirical studies of the global agricultural, apparel, and electronics industries that document the participation of developing and emerging economy SMEs in value chains. Examples of SMEs in developed countries, meanwhile, include the advanced skills contributed by machinery suppliers in Germany and Switzerland.

Furthermore, SME suppliers have a direct and significant impact on the quality, cost and lead time of new products and technologies needed to meet new market demands.

### Entering regional or global value chains

Lead firms pick suppliers based on quality, flexibility, delivery, service and other factors. Lowest cost is not the overriding consideration of global buyers when selecting suppliers. Buyers look first for quality, followed by delivery, price/cost, manufacturing capability, service, management, technology, research and development, finance, flexibility, reputation, relationship, risk, and safety and environment. The trend among buyers is towards fewer partnerships with long-term, reliable suppliers.

Countries, regions and towns can attract global companies if they show they have a critical mass of competitive suppliers. The search for suppliers may be global, but buyers often prefer suppliers in the same region. There are similarities in culture, language and legal systems, as well as geographical proximity.

### Setting objectives

Negotiation between a developing country SME and a global lead firm at first may seem akin to talks between David and Goliath. SMEs do well to enter such discussions proactively and with a clear idea of what they want to achieve.

An important consideration at this stage is which type of value chains to target. SMEs may consider it easier to enter into regional value chains than global ones, depending on internal factors, such as capacity and product attributes, and external factors, such as a supportive regulatory and institutional landscape. Regional value chains can be a quicker and cost-efficient entry point and may serve as a learning platform.

It is also vital to know if the lead firm is a buyer (retailers, branded manufacturers) or a producer (final-product manufacturer). This can affect the availability and type of upgrading opportunities. For example, buyer-driven chains can provide opportunities for product and process upgrading, as their core competence lies with marketing and branding. In contrast, producer-driven chains have less incentive to upgrade suppliers, as the lead firm’s competencies are in technology and the production process.

Once they set their objectives, SMEs can consider preparing a strategic plan. Strategic planning is a multi-step process to identify the activities and resources needed to implement the strategy. It helps provide direction and set priorities, and serves as the basis for developing an operational plan.
Being attractive to lead firms

The patterns of value chain governance by lead firms are based on:
- Complexity of business functions;
- The degree to which information can be codified;
- The degree to which suppliers are capable and reliable.12

To gain access to a value chain, suppliers increasingly must signal whether their operation and production systems meet internationally recognized or private standards. Standardized processes and outputs reduce complexity and increase efficiency within the chain. They help signal capability and reliability of suppliers.

Meeting standards associated with the lead firm improves the information flow on the quality of the firm's inputs, processes, products and services. This increases the probability of being selected by lead firms. A variety of internationally recognized standards and certificates help ease access to international value chains. Adhering to such standards is often a worthwhile investment for SMEs.

Investors and lead firms are also interested in assessing the financial stability of suppliers before entering into commercial relationships. They therefore seek to gather and monitor key financial information on suppliers and contractors, such as revenue, financial references, continuity plans and third-party ratings. Willingness and ability of suppliers to disclose such information – if possible using standardized reporting methods – helps to gain access to value chains.

Complying with standards and regulations

It is impossible to overstate the importance of quality and compatibility when trading in subcomponents. Lead firms impose standards on their suppliers to ensure compatibility between products and processes throughout their value chains. Meeting these standards is critical for participation in international value chains, and improves firm-level value. Studies show that firms adopting ISO 9000 certification tend to benefit from quality effectiveness, increased efficiency and increased operational control.14

Standards also serve to satisfy high final customer requirements, especially regarding environmental and social impact.15 The emphasis on sustainable and responsible value chains has led to a rise in the use of voluntary standards.16

Major global brands have integrated their sustainable sourcing commitments into their corporate strategies. Mars Incorporated, for instance, aims to certify all its cocoa as sustainably produced by 2020;17 Unilever expects to source all its agricultural raw materials sustainably by 2020;18 and IKEA intends to source all its wood, paper and cardboard from more sustainable sources by 2020.19

Standards and regulations, however, tend to increase fixed and marginal trade and production costs. To comply, companies often must invest in new technology and production and logistical processes. Costs also occur at the certification stage, when firms have to prove that they have implemented a standard or a regulation.20 Meeting many different standards and regulations can increase production and trade costs.

SME managers need to compare the costs of complying with international standards with that of serving regional markets, which often have less stringent requirements.21 SMEs can initially enter into the regional market to gain economies of scale and learning, adopting stringent international standards at a later stage.22

Fuelling the entrepreneurial spirit

Entrepreneurship is crucial to maximize comparative advantages of operating on a small scale, such as the flexibility to adapt to changing market demands. The ability to discover, enact, evaluate and exploit opportunities across national borders forms the basis of a firm's value chain integration strategy.24

Entrepreneurial qualities of SME managers are critical to a firm's internationalization, particularly in the early phases.25 Once an SME starts to interact with lead buyers, it gains more knowledge and expertise, and the characteristics of the enterprise itself become vital.

The capacity of SMEs to innovate is increasingly important to lead buyers. At the firm level, there is a strong relationship between exporting and innovation.26 Recent research finds that entrepreneurial small firms make key contributions to innovative activity and technological change, despite low spending on research and development by SMEs, especially when innovation is measured more holistically, and not only by R&D spending. Innovation does not only occur in product development and design, but also in processes.

SMEs tend to have an innovative advantage, as their size reduces bureaucracy and increases the ability to adapt to new technologies.28 To improve innovation, SME managers need to view the process of transforming ideas into commercial outputs as an integrated flow – similar to Michael Porter's value chain for transforming raw materials into finished goods.30
Operating successfully within value chains

SME involvement in value chains usually entails greater demands on managerial and operational resources and capacity. This includes building and retaining relationships with partners, meeting product requirements, undertaking purchasing and supply functions, managing logistics and monitoring business performance.

**Negotiations to build business relationships**

The first stage in developing a business relationship often involves negotiation. Key points about such negotiations include:

- **Win-win vs. win-lose negotiations**: Adopt a constructive, realistic approach, seeking agreements acceptable to both sides.

- **What to negotiate**: Negotiation on buying and selling usually includes specifications, quality assurance, quantities, prices and discounts, delivery and payment conditions and required support services. Negotiating a longer-term business relationship may involve long-term supply guarantees and price adjustments. For partner relationships, matters may include setting common business objectives, establishing modes of cooperation, sharing information and joint problem solving.

- **Have a good BATNA, or ‘best alternative to a negotiated agreement’**: This means having an acceptable backup option, should discussions fail. By understanding the worst-case scenario, one can negotiate with greater confidence and clarity.

Negotiations entail a series of stages for both buyers and suppliers (Figures 4 and 5).

To plan and prepare for negotiation:
- Understand market conditions
- Understand the other side
- Set negotiating objectives
- Determine negotiation variables (specifications, price, delivery schedule, transport and packaging, sharing of information, etc.)
- Set targets for each variable
- Identify negotiable zones
- Differentiate positions and interests
- Develop negotiation strategy.

Negotiation meetings follow several stages. The sequence may vary, and backtracking may also occur.

Differences in language, norms and values have a major impact on the success or failure of negotiations. At the regional level, these differences can be minimized. For instance, one study shows that African culture promotes the principle of reciprocity, consultation and consensus. Another study shows that in the case of Arab States, negotiators place emphasis on building relationships and use referent power, based on the ability of the leader to influence a follower. (Referent power is one of five types of power: coercive, reward-based, legitimate, referent and expert.)

**Contractual relationships**

The contract signed between a supplier and a buyer is key to whether or not the SME succeeds. The more comprehensive the contract, the more stable the context in which suppliers operate. First, the contract should be in writing. Second, it should go beyond basic terms and conditions (type of product, volume, price, delivery dates etc.) to include additional terms, such as specifications regarding who is responsible for the costs incurred when there are changes in the orders. Model contracts (Box 1) can give SMEs an idea of the level of detail they may seek in contracts with foreign parties.

The type of contract chosen depends on the nature of the contractual relationship envisaged. This can range from a one-off purchasing contract to a joint venture, with several options in between. From an SME supplier’s perspective, it is not necessarily desirable to be at either end of the band of contractual relationships (Figure 6). While spot purchasing and call-off contracts offer little or no stability to SME suppliers, joint ventures can risk their autonomy.
BOX 1: Model contracts for SMEs

Many small companies engaged in international trade lack access to the contract forms needed to protect their firms. ITC, working with leading legal experts, has developed generic contract templates that incorporate internationally recognized standards and laws for most small business situations.

The contract templates provide practical ways to secure international business for small firms. They bridge legal and cultural traditions by harmonizing recurring legal provisions common to most international contracts. The templates are for main trade activities, including the sale of goods, distribution, services and joint ventures. They were originally published in ITC’s 2010 book Model Contracts for Small Firms: Legal Guidance for Doing International Business, based on a worldwide survey of institutions representing SMEs. The model contracts are:

- **ITC model contract for an international contractual alliance**: A framework for an alliance or collaboration between parties.
- **ITC model contract for an international corporate joint venture**: A framework for a joint venture between two parties to establish a jointly owned company.
- **ITC model contract for the international commercial sale of goods**: An agreement for the sale of manufactured goods between a seller and a buyer. It contains specifications and explanations on issues such as lack of conformity and limitation of the seller’s liability.
- **ITC model contract for the international long-term supply of goods**: An agreement for the long-term supply of manufactured goods between a supplier and a customer.
- **ITC model contract for the international manufacture agreement**: An agreement under which the client wants the manufacturer to design, manufacture and deliver certain goods, which the client intends to integrate into its own final products or its services.
- **ITC model contract for the international distribution of goods**: An agreement for the distribution of manufactured goods, between a supplier and a distributor, whether or not the supplier is the manufacturer of the goods.
- **ITC model contract for an international commercial agency**: An agreement under which a commercial agent negotiates the sale or purchase of goods on behalf of another entity.
- **ITC model contract for the international supply of services**: An agreement under which a service provider offers certain services to a client.

Companies using these model contracts are strongly recommended to seek legal advice whenever they can, due to the wide range of options, trade practices and legal uncertainties that stem from any international transaction.

More information on ITC’s support to SMEs to enter into international contracts is available at www.intracen.org/itc/exporters/model-contracts

*Source: ITC.*

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**FIGURE 6** The continuum of contractual relationships

<table>
<thead>
<tr>
<th>Spot purchase</th>
<th>Regular trading</th>
<th>Call-off contracts</th>
<th>Fixed contracts</th>
<th>Partnerships</th>
<th>Joint ventures</th>
<th>Internal provision</th>
</tr>
</thead>
</table>

*Source: ITC (2013).*
Spot purchasing: This is where the buyer simply selects the best deal possible at the time of purchase. The focus is typically on price, and no relationship develops between the parties. This approach often covers one-off requirements of standardized high-value business functions where the cost of switching suppliers is low.

Regular trading: In the case of repeated spot purchases from the same supplier, there can be a regular trading relationship. This is useful when a business does not know the full extent of its requirements in advance or when each of its requirements is different. The frequent interactions under regular trading contribute to mutual understanding, with suppliers giving priority to the specific buyer, and buyers treating these suppliers as preferred partners.

Call-off contracts: Also called framework agreements, blanket contracts or standing orders. The supplier provides business functions at agreed prices and within agreed timescales on an ‘as needed’ basis over an established period, such as one year. This approach saves time and effort for the buyer, allowing it to ‘call-off’ requirements directly with the supplier without the need to negotiate a deal each time.

Fixed contracts: These are similar to call-off contracts, but the buyer commits to purchasing a certain volume or value each period. Fixed contracts are best suited when requirements are frequent and volumes can be predicted in advance. This type of contract is more attractive to suppliers than a call-off contract, as it guarantees a certain quantity.

Partnerships: Partnerships involve developing a relationship of mutual interdependence based on a high degree of interaction, trust, teamwork and information sharing. Both sides invest a lot of time and effort in the relationship. The focus is usually on joint efforts to reduce total costs and improve supply chain performance, rather than on price. Partnerships are appropriate for customized high-value business functions with the aim of long-term product development.

Joint ventures: A joint venture is a separate entity formed and owned by two or more businesses. By combining technologies and other resources, it usually serves to develop and offer a specific range of specialized products that members of the joint venture cannot provide on their own. SME suppliers that own a critical technology or other component required by the lead firms are likely to be absorbed by that firm.

Internal provision: This means making rather than buying. It gives the business maximum control over supply and thus reduces its supply risk. However, developing or acquiring the required capabilities can be very costly.

Cross-border transactions are based on confidence, as delivery and payment may occur in different places. Having a better knowledge of local business law and practices can reduce uncertainties in regional value chain transactions, compared with global ones.35

As buyers move on to obtaining and selecting offers, they consider the number of suppliers to contact, the approach to use for obtaining offers and the method to evaluate them.

International contracting raises a number of significant issues, including the different social, political and economic environment faced by each firm, which applicable law to adopt and which Incoterms36 to use. It is useful to have a careful definition of the relationship, noting the overall goals, scope of the products to provide, performance measures, and a formal mechanism to resolve conflicts.37

Investing in excellence

Excellence in operational capabilities is a central element in strategies of SMEs to internationalize and become suppliers in a value chain. The six key competencies that make up successful operations management include: quality, reliability, responsiveness, agility, service to customers and cost.38
These align with ITC’s SME Competitiveness Grid, illustrated in Figure 8. The grid’s pillars of competitiveness—capacity to compete, connect and change—reflect where strengths and weaknesses of firms lie.

Transactions in global value chains normally come with quality control systems and global standards (cost, delivery, quality and just-in-time systems) that can exceed those in domestic and regional economies. Supplier quality is critical for final product quality and costs, and information from a supplier’s quality control system and performance helps buyers set the right price level.

Quality control and meeting standards are not only to signal quality when entering value chain, however. They are also central to an organization’s operational strategy. By focusing on the connection between quality and strategy, firms can make progress towards achieving buyer satisfaction.

Operational excellence also involves designing product service functions. Buyers and suppliers of manufactured products appear to agree that the quality of support services is as important as product and price issues. This involves developing standard policies and procedures for returning goods, warranty servicing, repair, upgrades and support.

**FIGURE 8** Key competencies for operational excellence

- **Quality** management systems to meet standards, product specifications, and signal value for money
- **Reliability** in delivering products to customers relying on concepts such as just-in-time and responsive supply chains
- **Responsiveness** to customers’ demands and a focus on time-based competition
- **Service to customers** such as providing information, attention, quick response to queries, support and courteous treatment
- **Operational excellence**
  - **Cost** reductions in key inputs (labour, material, etc.) to offer better prices than competitors
  - **Agility** to meet changing customer preferences, fluctuating demand and evolving business conditions. It covers volume of demand, variety of demand and innovation in demand.

**Source:** ITC.
Meeting production needs of lead buyers

Figure 9 highlights four key supplier segments depending on risk and profitability. It is followed by a list of desirable supplier characteristics for each category of business functions or items being purchased by a business. These items include goods, services and bundles of business functions.

- **Suppliers of standardized, less skill-intensive, low-cost items or business functions:** These suppliers provide a wide range of business functions over the long term. Buyers expect responsive and effective suppliers with processes that are simple, consistent and reliable. Suppliers in this category also accept purchasing cards, electronic trading, and offer consolidated monthly billing.

- **Suppliers of standardized high-value items or business functions:** Given the high spend value of these standard business functions, buyers generally seek only to ensure that the supplier has the basic capabilities and the possibility to negotiate a good deal at a lower cost.

- **Suppliers of customized low-cost items or business functions:** These business functions are critical and can immediately affect the buyer’s operations. It is important that the suppliers are fully capable in areas that pose the greatest supply risk to the business (e.g. availability, quality, rapid delivery, supply flexibility, etc.).

- **Suppliers of customized high-value items or business functions:** These are a business’s most important suppliers and key partners for the long term, as they provide items such as key components on which final products depend. The suppliers in this category are expected to be financially stable and have a sustainable market position, remaining competitive in cost and technology over the medium to long term. They also need to be particularly capable in areas that pose the highest risk to the buyer – including reducing any upstream supply risk where applicable. They should consider the products required by the buyer as their own core business.

From the supplier’s perspective, the matrix in Figure 9 highlights two possible trajectories: moving along the bottom layer from standardized to customized items and business functions (functional upgrading) or moving up to the top layer where the governance structures of value chains can be favourable to SMEs. The matrix ties in with the discussion on the relevance of ‘modular’ and ‘relational’ governance structures for SME suppliers, which are characterized by mutual supplier-buyer dependence and high supplier capabilities.

Getting products to buyers efficiently

Inventory management and efficient delivery are critical to sustaining a firm’s value chain operations. While suppliers in the chain usually are not in charge of managing relevant logistics, they are expected to adjust their own logistics to the chain’s requirements. Quality management systems are instrumental at this distribution and logistical stage. Adequate inventory records and ordering procedures, as well as timely scheduling of freight operations, help in achieving distribution objectives.

Technology plays a key role in logistics. Geographic information systems, distribution management applications and vehicle routing applications are all useful for logistics planning. The most commonly used technologies for tracking goods in the logistics pipeline are bar coding, scanning and radio frequency identification. These technologies also track vehicles, although there are vehicle-specific tracking systems based on GPS and mobile communications.

Logistical challenges for SMEs may be lower within regional value chains, due to the smaller distances and regional trade agreements that facilitate deep integration beyond market access.

Analysing performance to learn and improve

An effective measurement system enables a firm to track and control its performance in accordance with the defined strategy. It provides clarity on how effective and efficient a
firm’s activities are in a value chain, as well as the impact on profitability. Understanding how well a business is performing is fundamental to doing things right.

The performance management process starts with identifying the most appropriate performance indicators. This is followed by collecting internal baseline and external benchmark data relevant to these indicators. Time-bound performance targets for the selected indicators can then be set, and an action plan developed for achieving these targets. Performance against the targets must be measured during, and at the end of, the action plan.

This process needs to be repeated continuously. Performance measurement frameworks can help SME managers to improve their visibility among value chain partners and explain the basis of decisions.45

In assessing their performance in value chains, SME suppliers should focus on the six key competencies mentioned earlier: quality, reliability, responsiveness, agility, service to customers and cost (Figure 8). The results help identify what to improve and reduce the chances of being replaced by other competitive suppliers. Depending on how feedback systems are used, an incentive system can influence the development of new capabilities – through organizational learning, or by reconfiguring existing capabilities.46

**Upgrading in value chains**

When SMEs enter value chains, they often are lower-tier suppliers. But this position tends to be precarious, as other suppliers can easily replace the original supplier by offering comparative advantages, such as lower costs. The challenge for SMEs is to move up by increasing their value content or by attracting more buyers or value chains.

**Types of upgrades**

Value chains open new doors to suppliers for the transfer of knowledge and technology, which stimulate innovation and lead to upgrading.47 Enterprises can consider upgrading in various ways, for example by entering higher unit value market niches or new sectors, or by undertaking new productive functions. There are four main types of upgrading through value chains:

- **Process upgrades** bring better or more innovative production methods, for more efficient conversion of inputs into outputs.
- **Product upgrades** involve producing better or higher quality products.

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**FIGURE 10** The performance management process


**FIGURE 11** Types of upgrades in value chains

Source: Avendaño, Daude, & Perea (2013).
Functional upgrades enable firms to move from low value-added business functions, such as assembly or extraction of minerals, to higher value-added activities, such as marketing or R&D.48

Chain upgrades allow firms to tap into value chains with more value added as a whole – moving from a textile chain to an electronics chain, for example. This usually happens at country level, in conjunction with policy decisions to channel competitiveness to different sectors of the economy. For example, such chain upgrading is thought to have been key in Chinese Taipei’s development path.49 SMEs can benefit if such a chain upgrade occurs in their country.

Innovation is crucial for upgrading. Such innovation does not necessarily mean a breakthrough creating an entirely new product or process. Instead, it involves marginal, evolutionary improvements of products and processes that are new to the firm, allowing it to keep up with changing international market requirements.

Value chains offer especially favourable conditions for product and process upgrades. The international buyer has an incentive to stimulate suppliers’ production and delivery methods, as well as product quality. It is more complicated for firms to upgrade functionally. The lead firm has little incentive to assist its suppliers, as such upgrades can be a threat to the buyer’s activities.50

When SMEs operate in several value chains with different buyers simultaneously, they can use the profits and the skills learned from one value chain for other markets. The lead firm or first-tier supplier in the first chain may only support or allow less threatening product and process upgrading, but in other markets buyers expect the firm to have its own designs or market its own products, leading to functional upgrading.51

Strategies to avoid ‘lock-in’

As SMEs consider their options to upgrade and reposition their firm within value chains, they face the potentially serious problem of a ‘lock-in’ situation. In such an instance, firms find that a large part of their output is going to one, or a small number, of customers, and they become specialized in one particular activity, usually production. They either do not develop design or marketing capabilities, or allow such capabilities to atrophy because of the strength of the relationship with the lead buyer. Below are some strategies to help SME managers tackle lock-in and achieve upgrading.52

Diversify into new markets

Market diversification is an opportunity for SME suppliers to produce for diverse buyers and markets, or even for more than one cluster. Trade intelligence and participation in trade fairs can help enterprises reach new markets. When dominant firms in the cluster are particularly dependent on a few large customers and reluctant to diversify, diversification efforts can be directed towards smaller firms, which frequently produce for different markets.

While diversifying entails a greater level of uncertainty, by investing in firm-level competencies, SME managers can be better prepared and ensure that decisions are well informed. Moreover, they can be in a position to apply the knowledge and capabilities acquired in one market to new markets and customers.

Align with corporate social responsibility

Most regional or global buyers face increasing pressure to maintain appropriate levels of social, environmental and ethical standards in addition to producing quality products. As a result, more and more buyers are emphasizing green and ethical purchasing. Green purchasing involves applying environmental considerations, such as reducing waste, re-using, recycling, protecting biodiversity and using environmentally sustainable materials and energy sources. Ethical purchasing involves treating suppliers fairly and responsibly, buying only from fair and responsible suppliers, and avoiding any illicit or dishonest practices in the purchase process.

SMEs can build their potential to upgrade by applying sustainable development principles where relevant in their business activities and meeting the quality requirements, ISO benchmarks and codes of conduct of buyers.

Use acquired knowledge

‘Learning by exporting’ is a well-known phenomenon,53 with the performance of firms improving after they enter export markets. Firms learn from contact with new markets, and joining value chains can magnify the impact if there are significant information flows between producers and buyers. However, the full advantages depend on the knowledge being used effectively. When firms, or groups of firms, sell to different markets they can leverage the knowledge gained in one market to support upgrading in another.
Considerations for services exporters

Many of the points above are relevant for both goods producers and service providers. It is hard to be prescriptive about strategies for services firms to join regional and international value chains, because there is little analytical material to draw on.

Some services sector characteristics affect the options and strategies open to service suppliers, particularly SMES, and suggest areas where support could be beneficial.

A paradox of cross-border trade in services is that explicit policy barriers are often low, but trade costs are very high – higher than for goods. This is an overall comparison of services to goods, and the situation may be different when analysing specific services sectors. For example, computer services have seen significant decreases in trade costs over recent years, due to the spread of internet connectivity. In theory, reaching international customers can be done through a website that is relatively simple and inexpensive to establish, using widely available technologies. This is beyond the reach of the smallest SMEs in low income countries, but could be feasible for many medium-sized firms in those countries, and a wider variety of SMEs in middle income countries.

About a third of small services firms used a website to communicate with customers – a higher share than for manufacturers, according to World Bank Enterprise Surveys. For medium-sized firms, the proportion is closer to 60%. This suggests that services firms in developing countries are adopting digital technologies to connect with foreign customers.

It is not enough to simply establish an online presence and set up a payment system. A much more active approach is necessary to reach foreign customers. A major issue for all service providers, and particularly SMES, is tailoring services to meet the purchaser’s needs.

Even when services firms are creative and offer diversified portfolios, in their early stages of development, it may appear to outsiders that they only perform a narrow range of business functions geared to the local market. This diminishes their attractiveness as international partners. The costs of obtaining the information about services markets, such as demand and requirements, are substantial, and there is a role for trade and investment support institutions (TISIs) in bridging this gap.

Another key difference between service and goods providers relates to the various modes of supply for international trade in services. These modes are defined under the General Agreement on Trade in Services (GATS), and include supplying services across borders (Mode 1) and having a commercial presence in another country (Mode 3).

Conventional theory suggests that SMEs usually export via Mode 1, whereas larger, more productive firms can bear the additional costs associated with trade via Mode 3. In services, however, relatively few developing country firms

### BOX 2: Characteristics of trade in services

**Situational:** Exporting services involves providing solutions to customer problems across borders. This requires firm-level capacities to build effective customer relationships, recognize emerging opportunities and respond rapidly with new solutions.

**Client-driven:** Service exporters tend to have relationships with individual clients, rather than with geographic markets.

**Relationship-based:** Clients often require a long-term relationship. Given that service exports are not tangible products and cannot be quality controlled on the spot, durable relationships require building mutual trust between service buyers and sellers.

**Project-based:** Services are usually part of a broader offering that goes beyond the service product being exported. For example, a piece of exported software is usually not a purpose in itself, but rather a means for achieving the client’s end purpose.

**Innovation-dependent:** Each service export project tends to require a nuanced service offering. This means services exporters are rarely able to find new export markets without innovating.

**People-driven:** Service exports projects require a team of talented and creative people.

sell through a commercial presence abroad, even within their own region. When it does occur, it is most often firms from large, emerging markets.

As a result, Mode 1 trade is particularly important for SMEs, suggesting that digital strategies are key to their ability to join regional and international value chains. Unlike in goods markets, where online platforms can reduce trade costs substantially, the need to custom-tailor services means that there is no ready equivalent to eBay for service providers. Instead, the strategy for reaching potential customers has to be more sophisticated, increasing the need for TISIs and development partners to assist firms in this process.

Research by ITC summarized in Box 2 highlights the distinctive characteristics of services trade. From the SME perspective, there are significant barriers to reaching international clients, even those in neighbouring countries. Two of the most important factors in services trade are the need for innovation and human capital, which are linked.

There is little systematic data on innovation by services firms in developing countries. However, World Bank Enterprise Survey data for India, which has seen impressive performance by services exporters in business process outsourcing and software, provide some insight.

The surveys identify firms that have engaged in recent process innovation. While the rate of process innovation for manufacturers is 46%, for services firms it is 55%. The data also identify improvements in management and company systems, with similar results: 43% for manufacturers, and 47% for services firms. This suggests that innovative activity is more prevalent among services firms than manufacturers, although generalizing such a conclusion requires data for more countries.

If this is the case, strategies for success in services exports should emphasize innovation, both in production processes and management and company systems. Mobilizing resources to help firms work on these areas could contribute greatly to promoting engagement in regional and international value chains.

Finally, trade in services plays a vital role in the functioning of international value chains. Traded services are commonly used as inputs into the production of other goods and services, which means that the sector is already important to regional and international value chains. For SME service providers to gain a greater share of this business, they must work closely with TISIs and development partners. The services economy is key for development over the medium to long term, and further engagement with regional and international value chains can help boost productivity and drive higher incomes.
SMEs take a variety of paths to international success. When small or medium-sized, firms tend to operate in just a few markets, or provide inputs for regional or global lead firms based in their home country.

For some SMEs, however, the road to success involves growing in size and taking a lead role within international value chains. The following examples highlight such firms, examining the steps these companies took and the role of regional integration and regional policies in their success.

The five companies covered have become regional or global leaders in their line of business. They come from different regions and sectors, including processed food and ecotourism, and have reached varying degrees of internationalization. Some capitalized on their home region; others used it as a springboard to expand globally. Governments’ regional policies often played a role in their success. Other factors included company attitudes towards quality control and international standards.

The five examples highlighted here illustrate that blueprints for success do not exist and that every success story is unique. But they also show that it is possible for a start-up in a developing economy to become a global lead firm.
Wilderness Safaris:
From safari camp to regional ecotourism operator

*Wilderness Safaris* is one of Africa’s prominent safari brands, headquartered in Botswana. Established over 30 years ago, it operates camps and lodges, and offers a wide range of safari experiences in Botswana, Kenya, Namibia, Rwanda, Seychelles, South Africa, Zambia and Zimbabwe. Providing private access to 2.5 million hectares (over six million acres) of wilderness, the company has over 40 exclusive camps and lodges.56

The regional success of Wilderness Safaris hinges on a supportive policy environment and a robust business model centred on ‘4Cs - Commerce, Conservation, Community and Culture.’ 57 The company has improved its competitiveness through upgrading. It has diversified its services to include those with higher value added and complexity, increasing its bargaining power.

**From safari to stock exchange**

Wildlife enthusiasts founded Wilderness Safaris in Botswana in 1983 as a mobile safari operator owning one safari camp and one jeep. The company gradually expanded in the region and extended its services from safari camps and lodges to light air travel and destination management. It was listed on the Botswana Stock Exchange in 2010.

In the early 1980s, Botswana was little known as a safari destination. Wilderness Safaris set up its first safari camp in Maun in the country’s northern region, tapping into undiscovered natural parks and resources. Subsequently, the company purchased more equipment and employed specialized guides. By the 1990s, Wilderness Safari had become a well-known mobile camping safari company and had begun to build a few permanent camps. In 1991, Wilderness Safaris expanded by starting a new service, Wilderness Air, offering scheduled transfers between Wilderness camps.

The company’s growth trajectory entailed vertical integration across four types of business areas: safari consulting (tour operation and destination management); transfers and touring (by air and road), camp, lodge and safari exploration operations; and finance and asset management.58

Wilderness Safaris has expanded in sub-Saharan Africa, where regional tourism is increasingly popular. In Botswana, Namibia, Rwanda, Zambia and Zimbabwe, an average of 80% of tourists are from African countries.59

**Supportive policies: Land use, standards**

One key behind the success of Wilderness Safaris is policy support to access land. In the 1990s, Botswana’s government reviewed land use in the Okavango, and areas outside the national parks became available for tender. This marked a big change in the safari business in Botswana, allowing Wilderness to develop and grow. There were similar developments in other countries – Namibia and Zimbabwe developed lodge and camp circuits, allowing the company to alter its business emphasis.

There has also been an interplay between Wilderness Safaris’ operations and the national policy framework and legislation, with the company in some instances helping to guide the development of national standards.

**Business values: Conservation and community engagement**

Conservation of natural attractions and the involvement of local communities are central to running a safari company. Wilderness Safaris evaluates destinations based on ‘4C’s: Conservation, Commerce, Community and Culture’. If these four goals cannot be fully pursued, the company may opt for alternative locations.

Since its inception, Wilderness Safaris has involved communities in ownership and operation of concessions. The company pioneered joint ventures with local communities, and its business model successfully integrates environmental, economic and social dimensions.
Wilderness Safaris has an impressive record of accomplishment in providing local economic benefits to communities through employment, procurement and joint ventures.60 The model developed between Wilderness Safaris Namibia and the people of the Damaraland area sets new industry standards. The success of this project led the Namibian government to declare the area a Conservancy (an area designated to conserve and protect natural resources), and Damaraland Camp won the international ‘Tourism for Tomorrow’ award in 2005.61
**Grupo ARCOR:**
From candy maker to Multilatina

**Grupo ARCOR** is an example of Latin America’s version of multinational corporations. Known as ‘Multilatinas’, these companies start in one Latin American country and spread throughout the region, first increasing their sales outside their home market (the trade expansion phase) and then acquiring strategic assets abroad (the investment phase).

Founded in 1951 in Argentina, Grupo ARCOR manufactures confectionery, chocolate, cookies and crackers. ARCOR has evolved from selling candy in local cities (its name combines the first letters of the city and province where it was founded, Arroyito in Córdoba) to become one of the world’s largest candy manufacturers.

As the firm expanded regionally and internationally, it benefited from regional trade agreements, such as MERCOSUR, and made foreign direct investments in its home region. The company diversified its products and vertically integrated its production process, with marketing affiliates, production plants, and distribution centres across Latin America.

**Regional road, sweet success**

ARCOR began in 1951, when Fulvio Salvador (son of Amos Pagnani, an Italian immigrant who opened a candy factory after arriving in Argentina in 1924) and a group of entrepreneurs opened its first candy factory in Arroyito. By 1958, the company was producing 60,000 kilograms of sweets sold mainly in the domestic market. During the 1980s, the firm experienced strong investment and growth, diversifying its products and sites to take advantage of industrial promotion programmes within Argentina. The company set up seven new plants in the provinces of Catamarca, Tucuman, San Juan and San Luis.  

In the 1990s, the firm expanded, with sales reaching $1.1 billion in 2000, including exports of $218 million and the company employed 12,700 people, 30% of whom were outside Argentina.

The company invested in Latin America, establishing marketing affiliates in Venezuela, as well as production plants and distribution centres in Chile and Mexico. It acquired firms and created partnerships with global companies, such as Danone, and regional firms, such as Mexico’s Bimbo. ARCOR also increased its market share in North America through agreements with firms in the United States and a new commercial affiliate in Canada.

ARCOR currently has more international markets than any other Argentinian group. Its early focus on exports helped consolidate the company’s regional and international business. Its brands are present in more than 120 countries and it has 40 industrial plants in Latin America and 11 commercial offices worldwide, including in Europe, Asia and Africa (Figure 13).

**Taking advantage of regional integration policies**

ARCOR’s international expansion was part of a strategy to integrate with neighbouring countries, which was later reinforced institutionally with the creation of the Common Market of the South (MERCOSUR) in 1991.

The company made foreign investments in Paraguay, Uruguay and Brazil. It set up Arcorpar in Paraguay to counter the advance of Brazilian companies in the Paraguayan market. It used Paraguay as a launching pad for moves into other countries when Latin American Integration Association agreements eliminated tariffs on regional exports.

In Uruguay in 1979, ARCOR formed an association with Industrias Van Dam, a local manufacturer of confectionery and chewing gum. ARCOR established itself in the Brazilian market by purchasing Nechar SA, a small confectionery manufacturer. This investment was also part of the company’s regional integration strategy in the context of various Latin American trade agreements.
**FIGURE 13 Commercial offices of ARCOR worldwide**


**Becoming a lead firm**

Success factors include vertical integration of production (Figure 93) and diversification of products and geographical markets. Some successful strategies resulted from the sector’s globalization and accumulation of experience in foreign markets. The firm moved from candy production to chocolates and candy bars, and eventually into other foods and alcohol. It also invested in agribusiness and other industries outside its core competencies, such as construction and hotels.

Integration of ARCOR’s presence in Argentina, Brazil and Chile helped the company to build a manufacturing and sales network with specialized plants and a regional vision. This enabled it to gain a strong strategic position in costs and flexibility.

**FIGURE 14 ARCOR value chain**

KÜRT Co. has grown from a small, Hungarian-owned enterprise into an international group, developing technologies and solutions for information protection, data loss prevention and data recovery.

Recognizing emerging opportunities and responding rapidly with new solutions contributed to KÜRT’s global success. The company used the European market as a stepping stone to develop and market services that were later sold globally.

**Working magic**

Founded in 1989 by the brothers János and Sándor Kürti in Budapest, Hungary, KÜRT started as a hard drive repair shop, next to a laundry service. It is now an internationally recognized data recovery and information security company, recording net profit of HUF 45 million ($163,000) on revenue of HUF 1.18 billion ($4.2 billion) in 2014. Its data recovery services began in response to a data loss incident at a major legal institution in Hungary, where the data storage unit was accidentally dropped. Today, KÜRT offers innovative solutions to help clients recover from IT disasters and to prevent disasters, abuses and system problems. The company’s information management division is a key player in the Hungarian market, having successfully completed a wide range of IT security projects. KÜRT’s incident management team provides in-house developed solutions in ethical hacking, log analysis and network investigation.

From bringing crashed servers back to life for banks, to finding evidence of criminal activity on smashed hard drives for the police, KÜRT built an international reputation for working magic on heavily damaged – soaked, broken or even burnt – hard disks. The firm was involved in the recovery of information destroyed in the September 11, 2001 attack on the World Trade Center. Although the company’s reputation has been built on data recovery, this accounts for only 30% of revenues. The remainder comes from information security services and consulting.

**Flexibility in regional growth strategies**

In early days, KÜRT sold its data recovery technology through its foreign partners and operated a data recovery network in 16 European countries, called the European Data Recovery Services (EDRS). In the early 2000s, Kürt rapidly started to lose the European market when its main competitor, Ontrack from the United States, acquired KÜRT’s 16 partners in EDRS.

With its local market saturated and the company close to bankruptcy, KÜRT set up wholly owned subsidiaries in Germany and Austria, through which the company serves the EU market. In 2006, KÜRT was recognized for outstanding growth performance and contribution to employment creation as one of ‘Europe’s 500 – Entrepreneurs for Growth.’

**Going global**

KÜRT also expanded outside its home region. The governments of Vietnam and Egypt have purchased its data recovery know-how, and clients in many countries, have used its IT security services. For example, one of Kuwait’s largest corporations, Zen, has contracted the company to review and develop its security systems. KÜRT is present in Dubai, where it is training financial institution employees on IT security. More recently, KÜRT has been planning to expand into the Chinese market, after signing a strategic partnership agreement with Invest Shenzhen, China’s first special economic zone, in 2015.

**Business assets: skills and innovation**

KÜRT’s success is tied to its ability to use a strong skill base and a long-standing reputation to grow in changing circumstances. The firm’s philosophy is ‘cultivate our skills and survive our failures’.

Kürt’s business started at a time when rules dating from the cold war under the Coordinating Committee for
Multilateral Export Controls (COCOM) resulted in a shortage of computer spare parts, making repaired storage devices a marketable product. KURT repaired all devices, initially due to physical damage and later due to IT disasters. The challenges led the company to invent new technology for information security and data recovery.

The company has continued to develop cutting-edge products and services. These include: SeCube, to control an organization’s information security management system; the Advanced Data Assessment Toolkit (AdvDAT); the specialized analytical storage tool PetaPylon; and the log file processing and analytics toolkit LogDrill.
Hikma Pharmaceuticals and its parent, the Hikma Group, started as a small manufacturing plant in Amman, Jordan. Some 40 years later, Hikma has grown into a pharmaceutical giant in the Middle East and North Africa (MENA) region, Europe and the United States.

Initially, Hikma’s expansion was mostly in its home region, but the company later expanded to North America and Europe, mainly through acquisitions. The company focused on signalling quality and reliability by meeting standards and implementing quality management systems. Capitalizing on its US Food and Drug Administration (USFDA) approval, Hikma became the licensing partner of choice for multinational companies seeking to expand into the MENA region. Hikma also benefited from Jordan’s economic reforms, improvements to intellectual property laws and accession to the WTO’s Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

Origin, history and current situation

In 1978, Samih Darwazah established Hikma in Amman. In its early days, Hikma became a leading supplier of branded generics and in-licensed products in the Middle East and North Africa, supplying high-quality, affordable medicines. The company’s success led it to expand beyond the MENA region. In 1991, Hikma established a presence in the United States through the acquisition of West-Ward, a generic pharmaceuticals business.

The pharmaceutical industry is Jordan’s highest value-added export sector and among the front-runners in the country’s strategy of export-led economic growth. It accounted for 9.6% of Jordan’s exports in 2016. Hikma leads the sector in Jordan. Spanning 50 markets, Hikma is also one of the largest pharmaceutical manufacturers in the MENA region and a large supplier of generic drugs in the United States.

FIGURE 16  Hikma manufacturing and R&D in Middle East and North Africa, Europe, and United States

▲ 29 manufacturing plants in 11 countries  ▲ 7 R&D centres

Source: Hikma website, www.hikma.com
Hikma’s listing on the London Stock Exchange in 2005 began a new development phase, enhancing its flexibility to expand geographically and build a strong and diverse product portfolio. Hikma completed four strategic acquisitions in 2007: two in Germany, to develop its oncology medications, one in Egypt, to establish a local manufacturing plant and presence in this market, and one in Jordan, to consolidate its domestic presence and gain access to the Saudi Arabian market.

Meeting international standards
The aim of adhering to international standards led the company to consider introducing internal quality control systems from early days. The company implemented total quality management in its various processes. Hikma Pharmaceuticals Jordan has a strong quality unit, and its director reports directly to the company’s general manager. The quality unit contains five departments: quality assurance, quality control, regulatory affairs, validation and calibration and the compliance department, each run by a dedicated manager, and directly reporting to the director of the quality unit.74

Seeking and obtaining USFDA approval was a key element in Hikma’s success in entering markets beyond Jordan. In 1996, Hikma Jordan’s manufacturing site was the first Arab pharmaceutical company to obtain USFDA approval. By the late 1990s, Hikma’s innovation and presence in Europe, MENA and North America led to significant expansion of the company. Hikma’s strong market position and its attention to high quality standards made it the licensing partner of choice for multinational companies looking to expand into the MENA region.

Supportive trade
While Hikma’s early success came through the manufacturing and marketing of branded generic drugs, Jordan’s comprehensive economic reforms, accession to the WTO’s TRIPS agreement and increased intellectual property protection brought the company many new prospects. Those reforms appealed to international partners, which brought further licensing and partnership opportunities.75 By the time intellectual property laws in Jordan changed, Hikma had a proven track record of working with global licensing partners. Its USFDA approved facilities, highly skilled workforce and production capabilities made the company even more attractive to multinational partners.
From a small village extraction factory in India, Synthite Industrial Chemicals has become a world leader in the value-added spices industry, processing and supplying a wide range of spices to major food, fragrance and flavour companies in over 100 countries.

Synthite's strong commitment to innovation and technology and early adoption of global food safety directives have given the company a competitive advantage in internationalization.

Building on oleoresins

While the history of spices is deeply entwined with the history of India, the country's tryst with value-added spice extracts began in the early 1970s. Synthite Industries Ltd, the global leader in value-added spices, had a humble beginning in 1972, as an oleoresin (spice extracted in liquid form) extraction factory in the small village of Kadayiruppu, in Kerala, South India. Launched as an idea of businessman C. V. Jacob, the family business that began with 20 employees has grown across borders and now processes and supplies a wide range of spices in diverse forms – whole, powder, oil and oleoresin – to companies worldwide.

Today, Synthite leads the global oleoresin industry, with 30% of world market share. In 2010, the company set up offices in China and the United States. In 2012, Synthite entered a new growth phase, establishing its first overseas production facility, which makes Paprika Oleoresins in Xinjiang, China. Besides this foreign production facility and the overseas offices, Synthite runs its worldwide operations through representative offices (Figure 14).

The role of policy: Public investment in R&D

The oleoresin business was initially based on research by India’s Central Food Technological Research Institute in Mysuru, which had developed a method for isolating active ingredients in spices using steam distillation and solvent extraction processes. However, it took several years of additional research and development by Synthite to make the technology viable. It was another four years before the company convinced food producers that it could produce quality products on time.

Commitment to quality control, innovation, technology

Synthite was the first Indian food company to obtain an ISO 9002 certification with HACCP in 1994. Its product range of more than 500 spice offerings conforms to global food safety directives and meets the stringent quality standards of major clients, which include Nestlé. The company adopts a multi-layered quality control system that begins at the farming stage. Synthite’s production and manufacturing units are ISO 22000:2005 certified. Other quality management systems conformed to include ISO 9001:2008 and National Accreditation Board for Testing and Calibration Laboratories (NABL) Accreditation – ISO 17025:2005.

Synthite’s commitment to innovation and technology has been crucial in its success. It won India’s Spices Board award for exports excellence several times as well as National awards. The company uses technological processes such as Supercritical Fluid Extraction, Thin Film Distillation and Spinning Cone Column. These processes translate into high quality and cost effectiveness. To maintain competitiveness, Synthite employs experts with diverse skill sets, from flavour and fragrance specialists to business leaders.

Technical superiority, four decades of expertise and a commitment to maintaining product quality have contributed to making Synthite a preferred partner for some of the largest international businesses in seasoning and flavouring industry, including Givaudan, IFF, Griffith Laboratories and Kerry Group.
FIGURE 17 Synthite’s worldwide operations


2. This Guide is based on the “SME Competitiveness Outlook 2017. The region: A door to Global Trade”, analysing the role of regional trade agreements and regional value chains for SME internationalisation. It is available at www.intracen.org/SMEOutlook.


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34. Vaughan-Whitehead and Caro, Purchasing Practices and Working Conditions in Global Supply Chains: Global Survey Results.


36. Incoterms are trade terms published by the International Chamber of Commerce (ICC) that are commonly used in international and domestic trade contracts.


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49. Humphrey and Schmitz, “How Does Insertion in Global Value Chains Affect Upgrading in Industrial Clusters?”
50. Ibid.
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63. Ibid.
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