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Cluster Development Strategy in the Philippines

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Introduction

Clusters are geographic concentrations of interconnected companies in a particular field, with upstream links that include suppliers of inputs and services, downstream entities such as customers and marketing outlets, and horizontal links among enterprises with similar technology and inputs, or complementary products. They may also include support institutions such as universities and research centers, standards-setting government agencies and trade associations, among others.[2]

The Philippine Experience

The Philippine government has two major parallel programs for industrial policy: formation of industrial zones and industry clustering.[3] While both programs seek to promote exports, regional and national economic development, and support regional dispersal of industries, they differ in nature. Industrial zones or parks encourage exporting firms, regardless of market orientation, with incentives and measures that attract foreign investments. These industrial parks are managed by the Philippine Economic Zone Authority (PEZA). Industry clustering, on the other hand, is more than a concentration of firms in the same sector or in the same location; it encourages collaboration among enterprises and promotes "the synergistic relationship between these firms and other enterprises, the government and supporting institutions."[4]

Industry cluster strategy occupies an important role in the government's development plans. In the Philippine Development Plan (PDP) for 2011-2016, further development of industry clusters is included in the ten-point agenda, specifically, to increase productivity and efficiency of the industry and services sectors to enable them to contribute more to economic growth and employment. Potential industry clusters that may be considered as priority areas are identified for each region annually. Priority areas are reviewed regularly to take into account changes in the global market. At present, industry clustering is actively promoted by the National Cluster Management Team (NCMT) of the Export Development Council with the support of the Department of Trade and Industry (DTI). The NCMT monitors the performance and identifies the needs of the national priority clusters, and aims to coordinate programs of various government agencies to match the needs of the clusters.[5]

Benefits of clusters

The nature of interconnectedness enables firms within the cluster to be more productive and competitive. Firms can have access to stable sources of inputs, and market and technical information. The linkages facilitate dealings and lower transactions costs. Although the linked enterprises may be competitors, they are better able to deal with common problems, such as tax issues, for example, collectively. The complementarities within a cluster may increase the success of the entire cluster—this is more evident in a tourism cluster where the efficiency of shopping outlets, restaurants and hotels, and tourist attractions enhance the quality of the whole cluster.[6]

[1] Bank Officer V, Center for Monetary and Financial Policy
[2] Porter 1998.
[3] PIDS 2008.
[4] PIDS 2008.
[5] Reyes-Macasaquit 2008.
[6] Porter 1998.

As a development strategy, industry clustering can be effective because it takes a holistic view of the supply chain from providers of raw materials on one end to users on the other end. The support structure promotes innovation and the transfer and adoption of new technologies either through demonstration effect or through links with research organizations and the academe. Also, an industry cluster is a greater attraction to foreign investments than a single firm.[7] Moreover, clusters may also be able to have not only greater access to financial sources but more favorable terms with the financial sector as well, by leveraging on the number of group members and resources. Finance companies, in turn, may design financial products and services suited for clusters.[8] Indeed, clusters, by their multi-enterprise linkage feature, magnify the beneficial growth impacts of development initiatives compared to initiatives involving individual firms. As such, cluster-based approaches have been prominent in development strategies of national and local governments, and competitive initiatives of international organizations and donor agencies.

For example, the Japan International Cooperation Agency (JICA) had a successful joint undertaking with DTI—the Davao Industry Cluster Capacity Enhancement Project (DICCEP) is a recipient of the 2010 NEDA Good Practice Award[9]—that will be expanded nationwide[10] as the National Industry Cluster Capacity Enhancement Project (NICCEP). Also the Korea International Cooperation Agency (KOICA) completed a feasibility study on the establishment of multi-industry clusters in three pilot provinces: Isabela, Quirino and Misamis Oriental.[11]

Promoting exports and MSMEs

The shift of the government's export promotion program to the clustering approach was presented in the 1999-2001 Philippine Export Development Plan (PEDP).[12,13] Previously, the focus of assistance was on specific sectors with export potential. With the cluster approach, assistance is provided on the basis of the common priority needs of the cluster. The PEDP for 2002-2004 emphasized coordination among various sectors by defining the roles of relevant government agencies in the implementation of the clustering strategy and highlighting the involvement of the private sector.[14]

Factors for successful clusters

Like any other enterprise, firms within clusters experience operational and market constraints and limitations. Yet in the same way that the multi-firm nature of clusters enhances its benefits, so does it magnify problems and weaknesses. Some of the more common challenges[15] to clusters are weak infrastructure support, high cost of utilities, and unmanageable and costly procedures of doing business. For clusters that are in the rural areas there is limited availability of skilled labor mainly due to migration and low level of technological capability. For industry clusters comprising of MSMEs, prevalent problems are access to finance and market information, and low productivity and competitiveness due to limited resources.[16] Oftentimes, MSMEs lack acceptable collateral and credit history to establish credit worthiness.

Studies identify important factors that characterize successful clusters. A qualified work force is important for the quality and sustainability of clusters. Similarly, access to financial institutions provides stable source of resources. A link to a center or institute of research development assures the application or adoption of the latest technology and

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7 PDP 2011-2016

8 Nadifi, Samy. "Cluster Finance: The Missing Cluster Competitiveness Discipline."

9 Sun Star Davao. "DICCEP bags national award." 5 January 2011.

10 Manila Bulletin. "JICA to expand projects." 10 January, 2011.

11 Olchondra 2011.

12 International Trade Centre. "Country perspectives," International Trade Forum, Issue 4/1999.

13 Former DOST Secretary Ceferino Follosco has been referred to as the primary advocate of industry cluster strategy, pushing for the strategy's inclusion in the government's development program. (The Philippine Star "Industry clustering adopted as core strategy.") Secretary Follosco is currently adviser to the National Cluster Management Team.

14 Reyes-Macasaquit 2008.

15 PIDS 2008.

16 PDP 2011-2016.

promotes innovation, and, subsequently, competitiveness. To maximize efficiency of the cluster, there has to be a strong link of cooperation among enterprises within the cluster, and of support from institutions outside the cluster. Within the cluster, enterprises must have commitment to devote time and resources, and willingness and trust to act collectively.[17] Clusters are also greatly supported and sustained by facilitating entities or, in general, "institutions for collaboration." These consist of trade associations, standard setting agencies, non-governmental organizations, and technology centers, for example, that provide connections to market players, and correct for market and public failures, among others.[18]

Cluster interventions

While traditional development policies respond to the needs of specific firms or industries, cluster interventions take a holistic view of the cluster. Government initiatives should involve coordinated interventions to provide an integrated response to the needs of industry clusters.

The public sector's main role in clusters is as a facilitator that brings the different entities together and not as a leader. Clusters should be led by the private sector; thus, public-private partnerships (PPP) may be an efficient strategy. Also, the formation of clusters should not be driven by government initiatives but should be a result of market developments and incentives.[19]

Financing clusters

As a basic example of how clusters facilitate financing, an International Food Policy Research Institute (IFPRI) report[20] on cluster-based industrial development in China gives an account of a cashmere sweater cluster where enterprises can get trade credits from upstream and downstream firms in addition to informal financing from friends and relatives. The practice mitigates entry barriers by lowering initial capital investment.

In general, clusters may source their funds from the private sector (commercial banks), public sector (government investments) or through specialized government banking such as development banks), external sources (foreign direct investments or donor agencies) or from themselves (equity financing or voluntary contributions).[21]

In a parallel program that is consistent with cluster initiatives, the Philippine Development Plan 2011-2016 espouses financial inclusion as a key feature of the development plan for the financial sector. Specifically to address MSMEs' lack of access to finance, the plan recommends the use of microfinance and the government's collaboration with microfinance institutions. Moreover, there are complementary programs such as the Credit Surety Fund (CSF) program initiated by the Bangko Sentral ng Pilipinas. The CSF is a fund created from contributions by well-capitalized and well-managed cooperatives with an equivalent contribution from the provincial government.[22] It is designed to serve as a substitute for collateral and is appropriate to the nature of clusters (interrelated businesses).

There are other solutions designed for clusters—development of bank credit assessment models that consider cluster firms to be less risky compared to stand alone firms, and the selection of cluster enterprises of one partner bank that would house all of their accounts to allow to negotiate collectively for more favorable loan terms.[23]

Finally, there are caveats to providing funds to cluster firms. Funds should not benefit one or a few of the companies within the cluster, nor should funds replace the costs that are normally borne by the private sector. Essentially, too much funding is a disincentive for the private sector to put up its own resources, and would, consequently, weaken initiative and reduced local ownership.[24]

[17] USAID 2003.
[18] Ketels and Memedovic 2008.
[19] The World Bank. Local Economic Development.
[20] Jianqing Ruan and Xiaobo Zhang 2008.
[21] The World Bank 2009.
[22] Credit Surety Fund Primer. Bangko Sentral ng Pilipinas.
[23] Nadifi, Samy. "Cluster Finance: The Missing Cluster Competitiveness Discipline."
[24] USAID 2003.

Conclusion

Given the potential benefits of industry clusters, the government would do well to adequately address the needs of and provide appropriate support to these clusters. Interventions should focus on strengthening links among the cluster enterprises, thus enabling the private sector to assume greater ownership.

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