

# Upgrading in Global Value Chains: Lessons from Latin American Clusters

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**Summary.** — It has been shown that clustering helps local enterprises in industrial districts overcome growth constraints and compete in distant markets in advanced and less developed countries. Nevertheless, recent contributions have stressed that more attention needs to be paid to external linkages and to the role played by global buyers to foster upgrading at cluster levels. In this study, we contribute to this debate focusing on the analysis of the relationships existing between clustering, global value chains, upgrading, and sectoral patterns of innovation in Latin America. We find that sectoral specificities matter and influence the mode and the extent of upgrading in clusters integrated in global value chains.

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## 1. INTRODUCTION

The aim of this paper is to explore how small- and medium-sized Latin American enterprises (SMEs) may participate in global markets in a way that provides for sustainable growth. This may be defined as the “high road” to competitiveness, contrasting with the “low road,” typical of firms from developing countries, which often compete by squeezing wages and profit margins rather than by improving productivity, wages, and profits. The key difference between the high and the low road to competitiveness is often explained by the different capabilities of firms to “*upgrade*.” In this paper, upgrading refers to the capacity of a firm to innovate to increase the value added of its products and processes (Humphrey & Schmitz, 2002a; Kaplinsky & Readman, 2001; Porter, 1990).

Capitalizing on one of the most productive areas of the recent literature on SMEs, we restrict our field of research to *small enterprises located in clusters*. There is now a wealth of empirical evidence (Humphrey, 1995; Nadvi & Schmitz, 1999; Rabellotti, 1997) showing that small firms in clusters, both in developed and developing countries, are able to overcome some of the major constraints they usually face: lack of specialized skills, difficult access to technology, inputs, market, information, credit, and external services.

Nevertheless, the literature on clusters, mainly focused on the *local* sources of competitiveness coming from intracluster vertical and horizontal relationships generating “collective efficiency” (Schmitz, 1995), has often neglected the increasing importance of *external* linkages. Due to recent changes in production systems, distribution channels, and financial markets, and to the spread of information technologies, enterprises and clusters are increasingly integrated in value chains that often operate across many different countries. The literature on *global* value chains (GVCs) (Gereffi, 1999; Gereffi & Kaplinsky, 2001) calls attention to the opportunities for local producers to learn from the global leaders of the chains that may be buyers or producers. The internal governance of the value chain has an important effect on the scope of local firms’ upgrading (Humphrey & Schmitz, 2000).

Indeed, extensive evidence on Latin America reveals that both the local and the global dimensions matter, and firms often participate in clusters as well as in value chains (Pietrobelli

& Rabellotti, 2004). Both forms of organization offer opportunities to foster competitiveness via learning and upgrading. However, they also have remarkable drawbacks, as, for instance, upgrading may be limited in some forms of value chains, and clusters with little developed external economies and joint actions may have no influence on competitiveness.

Moreover, both strands of literature were conceived and developed to overcome the sectoral dimension in the analysis of industrial organization and dynamism. On the one hand, studies on clusters, focusing on agglomerations of firms specializing in different stages of the *fil-ière*, moved beyond the traditional units of analysis of industrial economics: the firm and the sector. On the other hand, according to the value chain literature, firms from different sectors may all participate in the same value chain (Gereffi, 1994). Nevertheless, SMEs located in clusters and involved in value chains, may undertake a process of upgrading in order to increase and improve their participation in the global economy, especially as the industrial sector plays a role and affects the upgrading prospects of SMEs.

The contribution this paper makes is by taking into account all of these dimensions together. Thus, within this general theoretical background, this study aims to investigate the hypothesis that *enterprise upgrading is simultaneously affected by firm-specific efforts and actions, and by the environment in which firms operate*. The latter is crucially shaped by three characteristics: (i) the collective efficiency of the cluster in which SMEs operate, (ii) the pattern of governance of the value chain in which SMEs participate, and (iii) the peculiar features that characterize learning and innovation patterns in specific sectors.

The structure of the paper is the following: in Section 2, we briefly review the concepts of clustering and value chains, and focus on their overlaps and complementarities. Section 3 first discusses the notion of SMEs’ upgrading and then introduces a categorization of groups of sectors, based on the notions underlying the Pavitt taxonomy, and applied to the present economic reality of Latin America. Section 4 reports the original empirical evidence on a large sample of Latin American clusters, and shows that the sectoral dimension matters to explain why clustering and participating in global value chains offer different opportunities for upgrading in different groups of sectors. Section 5 summarizes and concludes.

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