United Nations
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# South-South Ideas

## Least Developed Country Graduation: Can South-South Cooperation Have a Positive Impact on Trade and Finance?

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CENTRE FOR POLICY DIALOGUE

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**July 2021**

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# Acknowledgements

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# Abbreviation and Acronyms

| | |
|---|---|
| AAAA | Addis Ababa Action Agenda |
| ADB | Asian Development Bank |
| AfD | Alternative for Germany |
| AfT | Aid for Trade |
| AIIB | Asian Infrastructure Investment Bank |
| AoA | Agreement on Agriculture |
| APTA | Asia-Pacific Trade Agreement |
| ASEAN | Association of Southeast Asian Nations |
| BFTA | Bilateral Free Trade Agreement |
| BIMSTEC | Bay of Bengal Initiative for Multisectoral Technical and Economic Cooperation |
| BOP | Balance of Payments |
| BRICS | Brazil, Russia, India, China, and South Africa |
| CDP | Committee for Development Policy |
| CEPA | Comprehensive Economic Partnership Agreement |
| COMESA | Common Market for Eastern and Southern Africa |
| CPD | (UN) Commission on Population and Development |
| CPTPP | Comprehensive and Progressive Agreement for Trans-Pacific Partnership |
| CTH | Change of Tariff Heading |
| D8 PTA | Preferential Tariff Arrangement-Group of Eight Developing Countries |
| DAC | Development Assistance Committee |
| DFI | Development Finance Institution |
| DF-QF | Duty-Free and Quota-Free |
| DTT | Digital Terrestrial Television |
| EBA | Everything But Arms |
| ECOSOC | (UN) Economic and Social Council |
| EIF | Enhanced Integrated Framework |
| EU | European Union |
| EVI | Economic Vulnerability Index |
| FDI | Foreign Direct Investment |
| FTA | Free Trade Agreement |
| GATS | General Agreement on Trade in Services |
| GATT | General Agreement on Tariffs and Trade |
| GDP | Gross Domestic Product |
| GEF | Global Environment Facility |
| GNI | Gross National Income |
| GSP | Generalised System of Preferences |
| HAI | Human Asset Index |
| IBRD | International Bank for Reconstruction and Development |
| IDA | International Development Association (World Bank) |
| IFI | International Financial Institutions |

| | |
|---|---|
| IMF | International Monetary Fund |
| INR | Indian Rupee |
| IPOA | Istanbul Programme of Action |
| IsDB | Islamic Development Bank |
| ISM | International support measure |
| ITEC | Indian Technical and Economic Cooperation Programme |
| JICA | Japan International Cooperation Agency |
| LDCF | LDC Fund |
| LDCs | Least developed countries |
| LIC | Low Income Country |
| LLDC | Landlocked Developing Countries |
| LMIC | Lower Middle-Income Country |
| MC | Ministerial Conference |
| MFN | Most Favoured Nation |
| MSG | Melanesian Spearhead Group |
| MVA | Motor Vehicle Agreement |
| NDB | New Development Bank |
| NFIDC | Net Food Importing Developing Countries |
| NTB | Non-Tariff Barriers to trade |
| ODA | Overseas Development Assistance |
| OECD | Organisation for Economic Co-operation and Development |
| PACER | Pacific Agreement on Close Economic Relations |
| PACER Plus | Pacific Agreement on Closer Economic Relations (updated in 2020) |
| PICTA | Pacific Island Countries Trade Agreement |
| PPP | Purchasing Power Parity |
| PTA | Preferential Trading Arrangement |
| RCEP | Regional Comprehensive Economic Partnership |
| RDB | Regional Development Banks |
| RoO | Rules of Origin |
| RTA | Regional Trading Arrangement |
| S&D | Special and differential |
| S&DT | Special and differential treatment |
| SAARC | South Asian Association for Regional Cooperation |
| SADC | Southern African Development Community |
| SAFTA | South Asian Free Trade Area |
| SASEC | South Asia Sub-regional Economic Cooperation |
| SCM | Subsidies and Countervailing Measures |
| SDG | Sustainable Development Goals |
| SFW | Special Fund Window |
| SIDS | Small Island Developing States |
| SSC | South-South Cooperation |
| TA | Technical Assistance |
| TFA | Trade Facilitation Agreement |

| | |
|---|---|
| TRIMS | Trade-Related Investment Measures |
| TRIPS | Trade-Related Aspects of Intellectual Property |
| UMIC | Upper-middle-income countries |
| UN | United Nations |
| UNCTAD | United Nations Conference on Trade and Development |
| UNDESA | United Nations Department of Economic and Social Affairs |
| UNDP | United Nations Development Programme |
| UN-OHRLLS | United Nations Office of the High Representative for the Least Developed Countries, Landlocked Developing Countries and Small Island Developing States |
| UNOSSC | United Nations Office for South-South Cooperation |
| USD | United States Dollar |
| WB | World Bank |
| WDI | World Development Indicators |
| WTO | World Trade Organisation |

# Executive Summary

Twelve LDCs are set to graduate over the next few years. This study argues that despite their success in meeting the specific graduation criteria, they are still afflicted by embedded structural weaknesses, a lack of export and market diversity, supply-side constraints, weak competitive strength, fiscal-budgetary deficits and aid dependence. The cost of graduating out of the LDC group will also be high. These costs result from significant erosion of preferential market access, the loss of flexibilities enjoyed under various special and differential provisions and increased obligations and commitments as developing countries under international agreements. Middle-income graduation of many of these LDCs will have adverse implications for the terms, amount and conditions of concessional private and institutional flows. This study warns that the negative impacts of the ongoing COVID-19 pandemic will add to these challenges.

Against this backdrop, this report undertakes an in-depth examination of the potential role of South-South Cooperation (SSC) in supporting sustainable LDC graduation. Two avenues of SSC are considered: *trade-related cooperation and extended support through concessional financial flows*. It stresses that both avenues are mutually reinforcing. Analysis reveals that LDCs are increasingly integrated with the Global South through trade in goods and services, investment, Southern Regional Trading Arrangements (RTA) and financial flows from both public and private Southern providers. Southern financial institutions such as the New Development Bank (NDB) and the Asian Infrastructure Investment Bank (AIIB) have added new dimensions to these financial flows. This study argues that opportunities to leverage these connections have emerged that could help LDCs in their quest for sustainable graduation.

This study therefore puts forward a number of concrete initiatives. It provides evidence that Southern markets are key export destinations for many graduating LDCs. *Under LDC schemes Southern country preferential market access* plays an important role in enhancing competitive strengths. Many graduating LDCs are also members of Southern RTAs. This study suggests Southern providers continue to provide *preferential market access to graduating LDCs for a specific period beyond graduation*, preferably for five years. It recommends that regional RTA provisions (similar to those provided to LDCs) be calibrated to extend favourable treatment to graduated LDCs on a predictable basis. And that the *special and differential treatment* provided to LDCs under various WTO agreements and provisions are also extended to graduating LDCs for an additional period. Southern countries need to demonstrate solidarity with graduating LDCs. This paper argues that trade-related aid and concessional credit will help these countries build the supply-side capacities they need, raise export competitiveness, and build production network and value chains at a time when preferential margins will decline.

Concessional financial flows are crucial to help graduating LDCs address structural impediments and build trade and other supply capacities. This paper demonstrates that LDCs and graduating LDCs continue to suffer from a *savings-investment gap, fiscal deficit and current account and balance of payments difficulties*. However, Southern providers have emerged as important players in financial flows. This report argues that, while Southern governments, private sectors and financial institutions play an increasing role in this regard, there are opportunities to *further enhance their contribution*. It therefore recommends that Southern partners be encouraged *to voluntarily adopt a target indicator* to ensure a certain percentage of their financial flows are earmarked for LDCs and graduating LDCs. Southern financial institutions should *create a special window financing the structural transformation* of LDCs and low income countries to ensure graduation is irreversible.

Such support should also be *targeted at upgrading these countries' social sectors*. Southern partners also need to provide LDCs with *greater FDI and remittances;* as these play a critically important role in their development and sustainable graduation.

Southern partners should play their part in helping LDCs and graduating LDCs survive the pandemic, which has led to the erosion of many past gains and comfort zones enjoyed as they move towards graduation. This paper argues that such support will be very well aligned with the *spirit of the SDGs, particularly Goal 17* concerning global partnerships. This report proposes establishing *a dedicated task force under the auspices of the UNOSSC to monitor how SSC will be affected by graduation, and to recommend initiatives for more effective SSC in terms of sustainable LDC graduation*. It emphasises that in view of several important upcoming global fora, including the WTO MC 12 and the UN LDC V, *Southern providers should volunteer to enhance their support* for LDCs and graduating LDCs, in areas relating to trade and through greater concessional financial flows. They should also demonstrate solidarity with these countries so that these fora agree to a *package of ISMs* to support sustainable LDC graduation.

# 1. Introduction

The Least Developed Country (LDC) category is a Southern phenomenon: all the LDCs belong to the Global South.

According to the Nairobi Outcome Document negotiated at the UN High Level Conference on South-South Cooperation and adopted by the UN General Assembly in December 2009, all developing countries are considered part of the Global South. As cooperation among Southern countries is now gaining increasing attention, South-South Cooperation (SSC) for LDC graduation is also assuming increasing importance.[1] This discussion is now relevant as, for the first time, a significantly large number of LDCs are set to graduate. All of these LDCs belong to the South:[2] three are in South Asia, three in South-East Asia, two in Africa while the remaining four are in the Pacific Ocean.

LDC graduation involves crossing a set of selected criteria thresholds. Interestingly, the discourse on implementing measures to support graduating LDCs continues to be dominated by North-South perspectives and North-South aspects of facilitating the graduation process. However, in view of the increasing number of LDCs set to graduate, and the subsequent need to find alternative avenues to support their graduation, an exploration of the opportunities to deepen SSC for sustainable graduation is increasingly relevant and important. This study seeks to address the gap by identifying SSC measures and methods to complement and strengthen traditional North-centric international support measures (ISMs)

This study seeks to address the gap by identifying SSC measures and methods to complement and strengthen traditional North-centric international support measures (ISMs)

The Istanbul Programme of Actions for the LDCs (IPOA, 2011) set the ambitious target of halving the number of LDCs from 48 to 24 by 2020. While only five LDCs have graduated since 1971, twelve are scheduled to graduate in the next few years.[3] While this could be seen as recognition of the progress made by LDCs in recent years, these countries continue to be afflicted by persistent weakness of various dimensions. To add to these embedded challenges, graduation itself will entail newer challenges. Many eligible LDCs are constrained by structural impediments and significant developmental deficits. Their graduation will result in a large measure of preference erosion (e.g. loss of Duty-Free, Quota-Free market access), and the loss of derogation from various commitments and obligations under multilateral fora such as the WTO (e.g. concerning trade-related intellectual property rights (TRIPS), trade-related investment measures and others). According to World Bank income criteria, many graduating LDCs are also graduating from

[1] LDCs have to meet at least two of the following three graduation criteria to graduate: GNI per capita of US$1,230 (in 2018 terms); Human Assets Index (HAI) score of 66 and above; and Economic Vulnerability Index (EVI) score of 32 and below. An LDC is also eligible to graduate if its GNI per capita is double the relevant income threshold.

[2] The group of LDCs was first identified as a sub-strata among developing countries in need of special attention, in 1971. Having started as a group of 25 countries, the number currently stands at 47.

[3] The five graduated LDCs are: Republic of Botswana (1994), Republic of Cabo Verde (2007), Republic of Maldives (2011), Independent State of Samoa (2014), Republic of Equatorial Guinea (2017). The countries with confirmed graduation dates (in parenthesis) are: Republic of Vanuatu (2020), Republic of Angola (2021), Kingdom of Bhutan (2023), Democratic Republic of São Tomé and Príncipe (2024), Solomon Islands (2024).
Countries recommended for graduation by the CDP but where the decision has been deferred: Tuvalu, Republic of Kiribati.
Countries to be considered for graduation by CDP in 2021: Federal Democratic Republic of Nepal, Democratic Republic of Timor-Leste (deferred from 2018).
Countries that met the criteria for the first time in 2018: People’s Republic of Bangladesh, Lao People’s Democratic Republic, Republic of the Union of Myanmar.

Low Income Country (LIC) to Lower Middle-Income Country (LMIC) status[4] which results in increased borrowing costs and more stringent borrowing conditions. Upon graduation these countries will also need to assume various new commitments and obligations as fully fledged developing countries, as members of the WTO and other relevant global fora and regional institutions.

This study is all the more relevant as LDC economies are now increasingly integrated with those of Global South countries through various channels. Indeed, almost all of the graduating LDCs have close economic ties with Southern countries through: trade, financial flows, investment, transport and a range of other connections. Many graduating LDCs are members of regional bodies and regional trading alliances (RTAs), which include LDCs, graduating LDCs and developing countries. Some Southern developing countries, such as: China, India, South Africa and Brazil have emerged as major development partners and donors.

A rich strand of literature examines the salient features and distinctive nature of SSC and how it has contributed to the development of developing economies: in areas including: trade in goods and services, investment, aid and finance, human resources, science and technology transfer, connectivity, infrastructure development and the environment. It has assessed SSC contribution and effectiveness, and examined the issues of making SSC more meaningful. There is therefore a strong case for an in-depth exploration of how SSC could play a more meaningful role in sustainable LDC graduation. As little progress has been made at the WTO and other relevant global fora in support of graduating LDCs, and recognising the large number of LDCs becoming eligible for graduation, this exploration is both necessary and urgent.

As will be seen from the following analysis, SSC could play an important role as LDCs prepare for life after graduation. Their assistance would also be very well aligned with Goal 17 of the Sustainable Development Goals (SDGs) that mentions deepening global partnerships to help developing countries attain the Agenda 2030 for Sustainable Development goals and targets. Indeed, SDG target 17.2 urges countries to implement all development assistance commitments, and 17.11 establishes the objective of helping LDCs double their share of global exports by 2020. This backdrop is a strong reason to undertake a study that examines the options and opportunities for deeper SSC to ensure it contributes to the economic development and sustainable graduation of LDCs. SSC importance for LDC graduation is now even more significant because of the adverse implications of the ongoing pandemic for the LDC and graduating LDC economies. There is therefore a renewed need and opportunity to deepen SSC for sustainable LDC graduation.

The importance of this study is underlined by the number of forthcoming global events, at which issues relating to graduating LDCs will be discussed. The most important are the 12th WTO Ministerial meeting (MC12) to be held in June 2021 in Kazakhstan[5]; the ten-year UN LDC V Conference, scheduled for March 2021 in Qatar and the 8th Aid for Trade Review now scheduled for January 2022. The need to explore deepening SSC as a tool for sustainable LDC graduation for these events cannot be overemphasised.

Unlike the other literature, this study explores concrete SSC avenues to support sustainable LDC graduation. The overarching objective is to study how both existing and potential SSC could help graduating LDCs address the particular challenges of graduation. Specifically it aims to undertake an in-depth examination of SSC in the areas of trade cooperation and financial flows.

4 The World Bank's 2019 income categories (GNI per capita according to the atlas method,) are: LICs (below US$ 1035), LMICs (between US$ 1036 and 4045), UMICs (between US$ 4046 and 12535), Developed Countries (above US$ 12536).

5 MC12 was to be held on 8-12 June 2020 but was deferred because of the pandemic.

## Objective, Methodology and Limitations

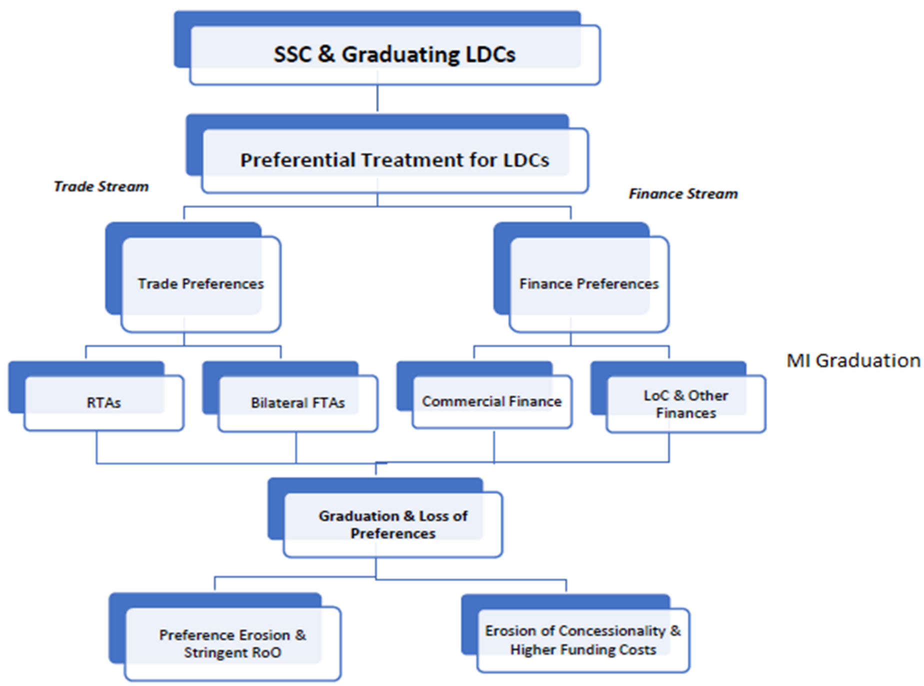
The preceding discussion establishes that, we need to bring SSC into the graduation discourse, to design support measures with momentum, and towards sustainable graduation. Potential avenues include: trade, financial flows, human resource development, establishing multi-modal connectivity, investment cooperation, technology transfer, supply-side capacity building support and others. Areas likely to be most relevant and impactful were selected for in-depth analysis because this study focuses on the implications of graduation from an SSC perspective. The criteria that informed this selection were: (a) relevance and implications of LDC graduation in SSC and (b) whether SSC could play an important role in helping graduating LDCs address post-graduation challenges. These considerations led to the selection of trade and financial flows, as shown in Figure 1. The aforementioned close link between trade and financial flows and their synergistic role in deepening SSC in other areas is another reason for this choice. Subsequent discussions will reveal that this selection is well grounded. It is a study limitation but this is also justified in view of the time constraints and resource limitation.

Areas likely to be most relevant and impactful were selected for in-depth analysis because this study focuses on the implications of graduation from an SSC perspective.

This study is based on an extensive review of the relevant literature, supported by evidence generated from appropriate datasets. Where needed, insights were gleaned from consultations with experts and webinars on the challenges of LDC graduation and impact of Covid-19. The inclusion of Finance Stream is also justified by the aforementioned second graduation from Low to Lower-Middle Income Country. This second graduation has implications for financial flows and their terms and conditions, which need to be acknowledged in the discussion of LDC graduation challenges.

This paper's discussion of the ways and means of deepening SSC in the context of LDC graduation is divided into two parts: Part A focuses on trade and market access issues while Part B deals with financial flows.

**Figure 1.1:** *SSC and LDC Graduation Impact*



The rejection of monoeconomics by the practitioners of SSC opens up the need for a new paradigm for its assessment.

Part A: Facilitating LDC Graduation by Deepening SSC in Areas Relating to Trade has three sections. Section 1 presents some of the key features of graduating LDCs and the vulnerabilities afflicting these countries, the state of trade flows and market access scenario and the likely implications of LDC graduation for those countries' trade performance. Section 2 examines graduating LDCs trade flows and trade relationships with Southern countries, and their membership of regional trading arrangements, to analyse how graduation will affect the terms of these relationships. Section 3 explores potential avenues of trade-related cooperation by adopting and deepening current SSC relationships and suggests new measures to support graduating LDCs. Addressing trade-related challenges is closely entwined with financial, particularly concessional financial, flows within SSC. Part B: Facilitating LDC Graduation by Deepening Development Finance-Related SSC, is divided into three sections. Section 4 analyses the structural vulnerabilities of graduating LDCs and their need for external finance – both public and private. Section 5 investigates the importance of financial flows from Southern bilateral providers and multilateral institutions, as well as remittances and foreign direct investments (FDI) from the South to the LDCs and graduating LDCs. The following section (Section 6) reviews bilateral and multilateral flows from Southern sources in the context of Covid-19. Section 7 wraps up the discussion with some forward-looking recommendations.

# 2. PART A: Facilitating LDC Graduation by Deepening SSC in Areas Relating to Trade

## Section 1: Structural Constraints, Trade Flows and Implications of LDC Graduation

Although they are set to graduate, graduating LDCs are still afflicted by significant structural constraints and weaknesses. Supply-side constraints have particularly adverse implications for post-graduation trade and competitive strength. The economies of graduating LDCs are critically dependent on trade. Graduation will entail a significant erosion of preferential trade and the loss of LDC-specific flexibilities, which will have an adverse impact on trade performance in regional and global markets. If graduation is to be sustainable, trade-related support needs to be extended through targeted initiatives to help address adverse impacts.

### 1.1 Structural constraints and the challenges of emerging scenarios

There is no denying that LDC graduation speaks of commendable success in terms of macro-economic performance, standards of living and a number of other key socio-economic indicators. But if we examine the three graduation criteria: Gross National Income per capita (GNI per capita), Human Asset Index (HAI) and Economic Vulnerability Index (EVI) we cannot fail to appreciate that these factors are necessary but not sufficient for sustainable development. The indicators and their sub-indices do not necessarily testify to graduating LDCs structural transformation, which is key to sustainable development.[6]

**Table 1.1:** *Productive Capacities Index (0= lowest, 1= highest)*

| Graduating LDCs | Productive Capacities Index | Structural Transformation | Transport | ICT | Energy | Private Sector Development |
|---|---|---|---|---|---|---|
| **Bhutan** | 0.78 | 0.57 | 1.00 | 0.52 | 0.92 | 0.89 |
| **Nepal** | 0.70 | 0.73 | 0.96 | 0.30 | 0.60 | 0.94 |
| **São Tomé and Príncipe** | 0.63 | 0.42 | 1.00 | 0.54 | 0.63 | 0.55 |
| **Tuvalu** | 0.52 | 0.14 | n/a | 0.69 | 0.74 | n/a |
| **Lao PDR** | 0.51 | 0.60 | 0.24 | 0.42 | 0.52 | 0.75 |
| **Kiribati** | 0.49 | 0.30 | n/a | 0.32 | 0.51 | 0.81 |
| **Angola** | 0.44 | 0.32 | 0.18 | 0.35 | 0.64 | 0.68 |
| **Bangladesh** | 0.44 | 0.68 | 0.17 | 0.25 | 0.26 | 0.85 |
| **Vanuatu** | 0.44 | 0.24 | 0.42 | 0.32 | 0.30 | 0.89 |
| **Myanmar** | 0.35 | 0.68 | 0.21 | 0.04 | 0.48 | n/a |
| **Solomon Islands** | 0.34 | 0.36 | 0.04 | 0.26 | 0.17 | 0.88 |
| **Timor-Leste** | 0.28 | 0.18 | n/a | 0.19 | 0.22 | 0.54 |

Note: ICT=Information and Communications Technology; n/a = not available. Source: UNCTAD (2016).

[6] To be considered for graduation, an LDC either needs to reach the graduation thresholds in two of three indicators (GNI per capita of US$1230 calculated according to the atlas method (2018), HAI of 66 and above and EVI of 32 and below) or reach double the income threshold. An LDC has to maintain these figures over two successive triennial reviews to be recommended for graduation by the CDP to the ECOSOC and for the UNGA to endorse the recommendation.

As Table 1.1 shows, most of the graduating LDCs suffer from various structural weaknesses (as shown in the productive capacities index). Close examination of graduating LDC profiles illustrates the range of vulnerabilities afflicting these countries. Box 1.1 summarises these. The diversity of constraints afflicting the twelve graduating LDCs is impressive: being landlocked (Bhutan, Nepal, Lao PDR); low EVI (all but Bangladesh), over-dependence on a particular export (e.g. for Bangladesh, apparel; for Angola, fuel); small island countries highly vulnerable to climate change and natural disasters (such as the four pacific islands). It is therefore not surprising that many LDCs set to graduate have requested deferment (as Box 1.1 reveals, these number exactly half of the current graduating LDCs).[7]

**Box 1.1:** *Graduation Diversities and Embedded Vulnerabilities*

- Landlocked LDCs (e.g. Nepal, Bhutan, Lao PDR)
- LDCs eligible by meeting income only criteria (e.g. Angola; Timor-Leste)
- LDC graduating without meeting the income criteria (Nepal)
- LDC graduating having met all three criteria (Bangladesh)
- LDCs eligible by meeting two out of three criteria (e.g. Lao PDR; Bhutan; Myanmar)
- WTO-Acceding LDCs (e.g. Lao PDR, Timor-Leste, Bhutan)
- Not WTO members (Kiribati and Tuvalu)
- SID-LDCs (e.g. São Tomé and Príncipe, Kiribati, Solomon Island, Vanuatu, Tuvalu, Timor-Leste)
- Graduating LDCs undergoing dual graduation – LDC and middle-income graduation (all barring Nepal)
- EVIs of graduating LDCs tend to be volatile – even when HAI and per capita GNI were rising steadily, EVIs showed considerable volatility (e.g. São Tomé and Príncipe, Solomon Island, Tuvalu)
- Graduating LDCs with debt-distress (according to the IMF: Lao PDR: High Debt Risk, Timor-Leste and Bhutan: Moderate Risk)
- World Bank Harmonised List of Fragile States: over half the LDCs are projected to remain fragile states in 2024
- Half of the graduating LDCs previously requested graduation deferment (Angola, Tuvalu, Vanuatu, Nepal, Timor-Leste and Bhutan)

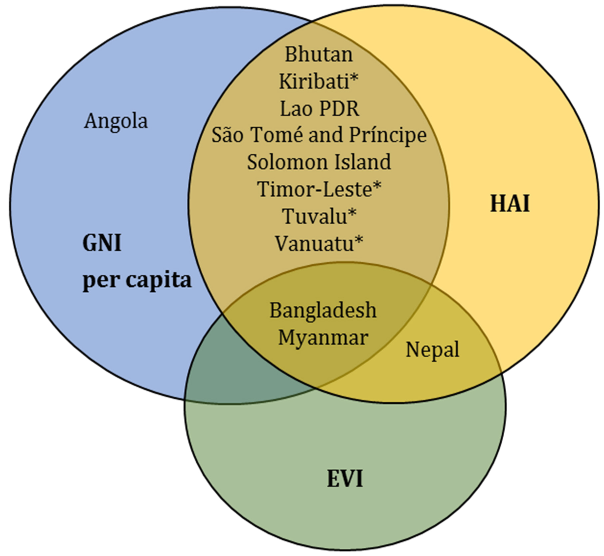
Source: Rahman and Bhattacharya (2020), WTO (2020b), World Bank (n.d.).

Even in terms of the graduation criteria, most of the twelve graduating LDCs have either only met two of the three criteria, or have graduated under the income only criteria. Figure 1.1 shows this clearly: only Bangladesh and Myanmar crossed the graduation thresholds in all three criteria.[8]

[7] The average time taken to graduate by the five graduated LDCs, (following the year when they were first slated for graduation after having met the graduation criteria,) is 9.2 years. The stipulated time is 6 years given the requirement for positive recommendation at two subsequent triennial reviews.

[8] Myanmar squeezed through with a 31.7 EVI score (the cut-off threshold is 32.0 or below).

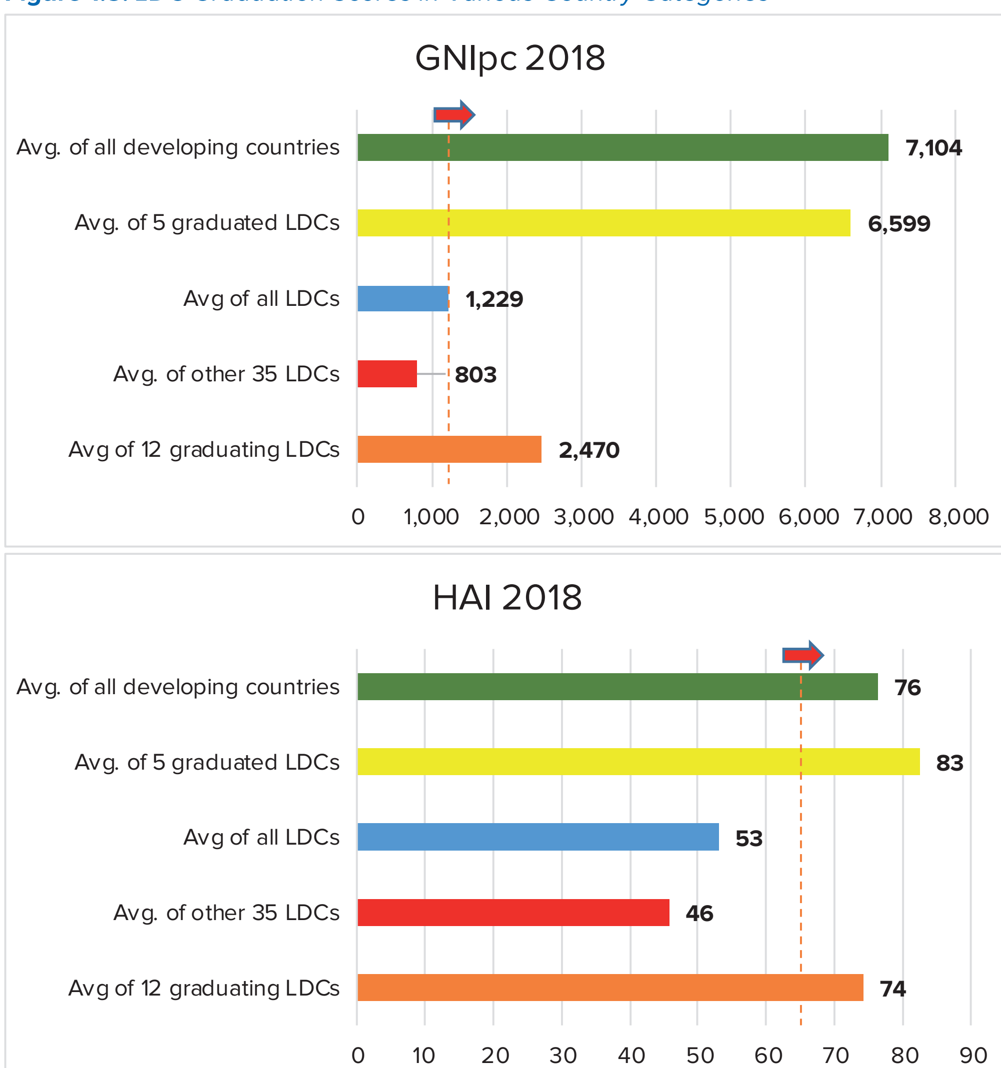
**Figure 1.2:** *The Graduation Criteria Passed by Graduating LDCs*

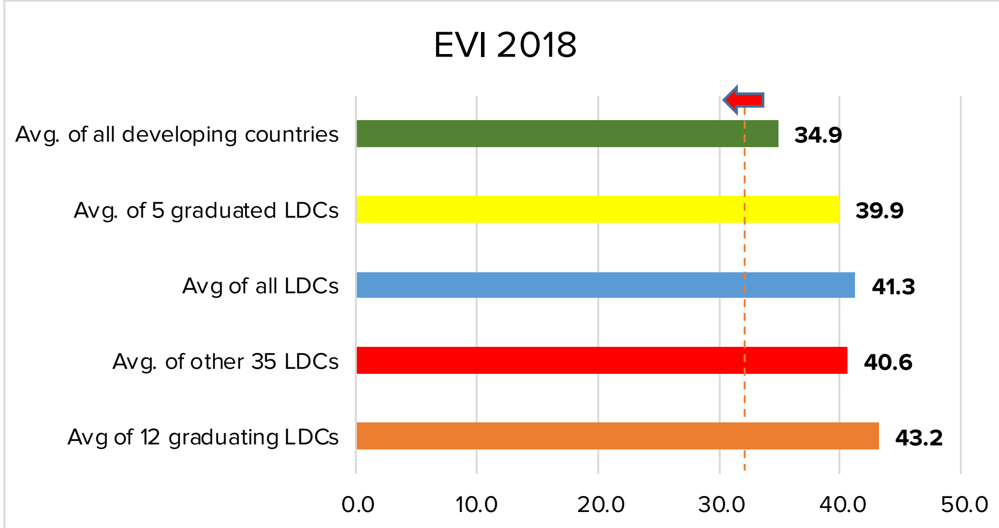



Note: *Graduating LDCs that also achieved the income only criteria (GNI per capita: equal to or greater than $2,460)
Source: UNESCAP (2020).

Interestingly, Figure 1.2 below shows that the 12 graduating LDCs underperform in terms of EVI, not only when compared to the average for developing countries and the 5 graduated LDCs but also when compared to the average of the 35 non-graduating LDCs.

**Figure 1.3:** *LDC Graduation Scores in Various Country Categories*






Source: Authors' estimation based on CDP 2018 triennial review data.

One of the reasons why such a large number of LDCs have become eligible for graduation is that the thresholds for two criteria: HAI and EVI, were set at 66 and above and 32 and below respectively in 2012.[9] Important progress has unquestionably been made in terms of attaining the target of halving the number of LDCs by 2020 set out in the 2011 Istanbul Programme of Action (IPoA).[10] However, many graduating LDCs are still challenged by pervasive weaknesses in important areas, which have not gone away just because these countries were able to meet two or three graduation criteria, or the income only criteria. Many graduating LDCs are also moving from LIC to LMIC status, which has implications for their financing terms and interest rates. Finally, graduation will be taking place in the context of the pandemic and against the backdrop of a looming global recession. This will further accentuate the difficulties faced by graduating LDCs and has added new challenges on many fronts. The need to find new cooperation methods and to support graduating LDCs is therefore now even more urgent.

## 1.2 Graduating LDC Trade Exposure

LDC economies have become increasingly integrated with the global economy, particularly through trade. Indeed, trade plays an increasingly important role in these countries' economies, in terms of employment, income, forex reserves, exchange rate management, resource mobilisation, macro-economic management and growth.

[9] Previously these indices were variable numbers, fixed periodically based on LDCs relative progress in the sub-indices.
[10] At the time, the number of LDCs was 48.

**Table 1.2:** *Graduating LDC Trade Profile in 2018*

| Graduating LDCs | Location | Population (million) | Exports (million $) | Imports (million $) | GDP (million $) | Trade openness (%) |
|---|---|---|---|---|---|---|
| **Angola** | **Africa** | 30.81 | 42,022.0 | 16,385.6 | 112,064 | 52.1 |
| **São Tomé and Príncipe** | | 0.21 | 12.7 | 155.3 | 450 | 37.3 |
| **Bangladesh** | **South Asia** | 161.38 | 45,515.6 | 57,283.3 | 269,604 | 38.1 |
| **Bhutan** | | 0.75 | 318.6 | 814.6 | 2,723 | 41.6 |
| **Nepal** | | 28.10 | 781.1 | 12,857.9 | 27,276 | 50.0 |
| **Lao PDR** | **Southeast Asia** | 7.06 | 5,814.8 | 5,848.0 | 18,179 | 64.1 |
| **Myanmar** | | 53.71 | 16,671.6 | 19,345.5 | 70,019 | 51.4 |
| **Timor-Leste** | | 1.27 | 74.8 | 477.2 | 3,590 | 15.4 |
| **Kiribati** | **Oceania** | 0.12 | 136.2 | 100.3 | 200 | 118.4 |
| **Solomon Islands** | | 0.65 | 569.1 | 601.4 | 1,294 | 90.4 |
| **Tuvalu** | | 0.01 | 30.9 | 87.0 | 46 | 256.3 |
| **Vanuatu** | | 0.29 | 176.5 | 328.4 | 889 | 56.8 |
| **Graduating LDCs total** | | 284 | 112,124.0 | 114,284.4 | 506,334 | 44.7 |
| **LDC (47) total** | | 1,010 | 200,158.4 | 283,096.8 | 1,076,864 | 44.9 |
| ***Graduating (12) LDCs as % of LDCs (47)*** | | *28.2* | *56.0* | *40.4* | *47.0* | *n.a.* |
| **World** | | 7,631 | 19,310,111.0 | 19,680,448.8 | 85,693,322 | 45.5 |
| **LDCs (47) as % of World** | | 13.23 | 1.04 | 1.44 | 1.26 | n.a. |

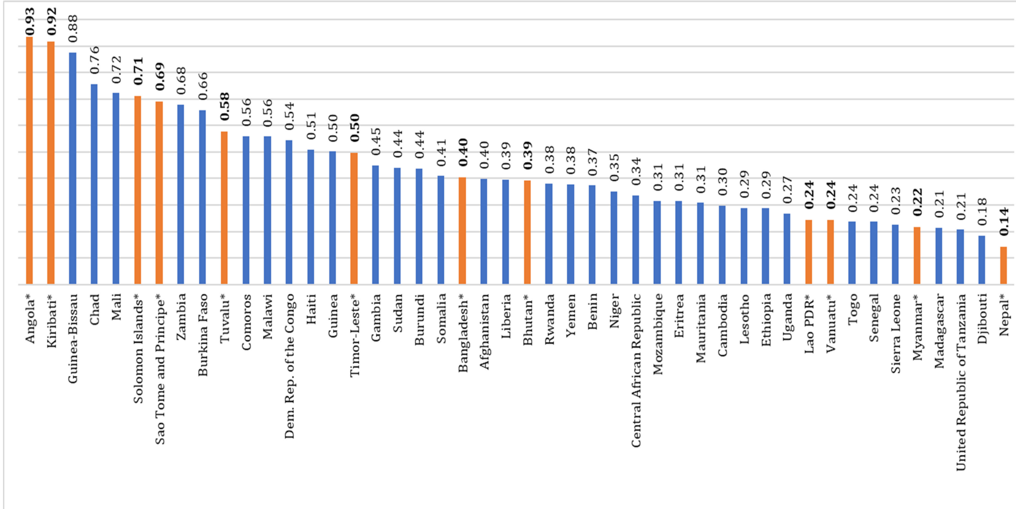
Source: Calculated from the Trade Map database.

Table 1.2 shows that graduating LDCs are very exposed to the global market through exports and imports of goods and services. Their average trade openness is 44.7 percent.[11] Indeed, if Timor-Leste (15.4 percent) is excluded, the range varies between 37.3 percent (São Tomé and Príncipe) and 256.3 percent (Tuvalu), testifying to these countries' high trade dependence. Almost all of the graduating LDCs also demonstrate high exposure in terms of export dependence (export share of GDP). These shares are particularly high in Kiribati (68.0 percent), the Solomon Islands (43.9 percent), Angola (37.5 percent) and Lao PDR (31.9 percent). As the table shows, the twelve graduating LDCs account for more than half (56.0 percent) of total LDC exports. Bangladesh (40.5 percent), Angola (37.4 percent) and Myanmar (14.9 percent) dominate their export landscape. However, the share of LDCs as a group was only about 1 percent (1.04 percent) of global goods exports ($19.31 trillion). This figure was way below the target established in the IPOA and the SDGs.[12]

[11] Trade openness is defined as the share of exports and imports as a percentage of national GDP.

[12] Both the IPOA (2011) and the SDGs (17.11) set the target of doubling LDCs' share of global trade by 2020. Their share needed to have been at least 2.0 percent by 2020 to achieve this.

**Figure 1.4:** *Product Concentration Index, 2018*




Source: Based on UNCTADstat.
Note: *Graduating LDCs are shaded in orange bars.

Figure 1.3 shows significant product concentration, and depicts the high range of indices for many graduating LDCs. It shows that Angola (0.93; Oil), Solomon Islands (0.71; Wood), São Tomé and Príncipe (0.69; Cocoa), Timor Leste (0.50; Crude Petroleum) and Bangladesh (0.40; Apparel) all have highly concentrated export baskets, which makes them very vulnerable to highly volatile global market prices and demand fluctuations.

Graduating LDCs' share of the global exports of commercial services was 0.22 percent while their share within the LDC cohort was 31.0 percent.[13] Here the picture is dominated by a few graduating LDCs (Myanmar with 40.9 percent of the group share, Bangladesh with 24.0 percent and Nepal with 14.3 percent) (WTO-EIF, 2020). Their predominant services are travel, transport and other commercial services. Remittances are also an important non-commercial services export for some graduating LDCs.[14] In this context, the most notable graduating LDCs are: Nepal (equivalent to 27.3 percent of GDP), Kiribati (10.9 percent), Tuvalu (9.7 percent), Bangladesh (5.8 percent), Myanmar (4.3 percent) and Vanuatu (3.7 percent).

Strengthening supply and competitive capacities in these areas ought to be key components in these LDCs' strategies for sustainable graduation. This issue is also important because most graduating LDCs maintain significant trade deficits. As Table 1.2 reveals, all of the graduating LDCs except Angola have a negative trade balance. Hence, the ability to maintain export competitivity and gain purchasing power through enhanced exports must be seen as critical.

The trade profiles presented above demonstrate that trade plays a crucially important role in graduating LDC economies. The following sub-section analyses what LDC graduation will entail for these countries' trade interests.

[13] The joint share of all LDCs combined was 0.47 percent.
[14] Global remittances reached $53.4 billion in 2019. However, global flows are projected to decline by 19.7 percent in 2020 according to the World Bank.

## 1.3 Graduation and trade implications

This section examines how LDC graduation is going to affect their trade interests.

LDCs receive various trade-related benefits from LDC-specific measures with significant positive implications for trade performance and competitiveness. These benefits originate at various levels: (a) through bilateral trade-related initiatives; (b) through membership of various RTAs and (c) through various measures for LDC members at global level in the WTO.[15] Graduated LDCs will enjoy trade-related benefits as developing countries upon their graduation. However, the depth and coverage of these privileges are far shallower and narrower than those in place for the LDCs. This is made clear in Box 1.2 and Box 1.3.

**Box 1.2:** *Implications of LDC Graduation*

| S&DT | LDCs | Implications of Graduation |
|---|---|---|
| Preferential market access for goods under the General Agreement on Tariffs and Trade (GATT) | Duty-Free and Quota-Free (DF-QF) market access | Will lose LDC-specific preferential market access. Will only be eligible for benefits under standard GSPs. |
| Preferential treatment for services under the General Agreement on Trade in Services (GATS) | Commitments made by developed and developing Members under the LDC Services Waiver until 2030. | No preferential treatment upon graduation. |
| Agreement on Agriculture (AoA) | LDCs and Net Food Importing Developing Countries (NFIDCs) may provide certain export subsidies until the end of 2030 (article 9.4 of the Agreement on Agriculture, Ministerial Decision of 19 December 2015 (WT/MIN(15)/45-WT/L/980, G/AG/5/Rev.10). | Provision will only be available for the NFIDCs. |
| Agreement on Subsidies and Countervailing Measures (SCM) | LDCs and other members can use export subsidies (Article 27.2 and Annex VII of the Agreement and paragraph 10.1 of the Doha Ministerial Decision on Implementation-Related Issues and Concerns (WT/MIN(01)/17)). | Only members with GNI per capita below $1,000 in constant 1990 dollars are eligible (Article 27.2 and Annex VII(b)). |
| Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) | Exempted from implementing the Agreement other than the core non-discrimination principles until 1 July 2021 (Provision of article 66.1, latest extension IP/C/64). | Will need to comply with TRIPS provisions as applicable to developing countries. |
| Transition period for pharmaceuticals in the TRIPS Agreement | Exempted from providing patent protection for pharmaceutical products until 1 January 2033 (IP/C/73 and WT/L/971). | Required to provide patent protection for pharmaceutical products. |
| Trade-Related Investment Measures (TRIMS) | LDCs can introduce new measures that deviate from their obligations, by notification. Upon acceptance, they are allowed to continue the new measure for another seven years. However, all measures must be phased out by 2020. (Annex F of the Declaration of the Sixth WTO Ministerial Conference allowed LDCs to temporarily maintain existing measures that deviated from their obligations under the TRIMs Agreement). | Will need to comply with TRIMS developing country obligations. |
| Technical Assistance (TA) provided by the WTO | TA measures and other support designed to address their specific needs. | Will not be eligible for LDC-specific TA measures. |
| TA provided by the Enhanced Integrated Framework (EIF) | The EIF is designed exclusively to support LDCs through aid and technical support. | Provision to use additional support for up to five years after graduation. |

Source: Authors, based on WTO Secretariat and UN LDC Portal information.

[15] 3 of the 12 graduating LDCs (Lao PDR, Bhutan and Timor-Leste) are in the process of WTO accession.

LDCs enjoy trade-related preferential treatment through 139 Special and Differential Treatment (S&DT) provisions for developing country members of the WTO, of which 14 are exclusively for LDCs. Box 1.2 shows that these take the form of (a) preferential goods and services market access, (b) longer transition periods to implement commitments, (c) derogation from undertaking commitments and (e) Technical Assistance, including under the WTO Enhanced Integrated Framework (EIF) initiative.

**Box 1.3:** *Overview of Selected S&DT for LDCs and Graduated LDCs*

| S&DT | LDCs | Graduated Countries |
|---|---|---|
| Preferential market access for goods | Duty-Free and Quota-Free (DF-QF) market access | LDC specific preferences no longer available (except the EBA for three years following graduation). GSP schemes applicable to developing countries. |
| Preferential treatment for services | Commitments made by developed and developing members under the LDC Services Waiver, until 2030. | Do not benefit from preferential services treatment |
| General transition period for TRIPS | Exempted from implementing the TRIPS Agreement (except the core non-discrimination principles) until 1 July 2021. | Required to implement the TRIPS Agreement and provide respective IP protection |
| Transition period for pharmaceuticals under the TRIPS Agreement | Exempted from providing patent protection for pharmaceutical products until 1 January 2033. | Required to provide patent protection for pharmaceutical products. |
| Flexibility to use policy instruments under the Agreement on Subsidies and Countervailing Measures (SCM) | Pursuant to Article 27.2 and Annex VII(a) of the SCM Agreement, LDCs can use export subsidies. | Export subsidies are prohibited except for LDCs, and certain other selected members. |
| TA provided by the WTO | LDCs benefit from specific courses designed for their needs. | No significant change in entitlements under the WTO TA and Training Plan. |
| TA provided by the EIF | The EIF programme helps LDCs use trade as an engine for growth and sustainable development. | Possibility of additional support for up to five years for graduated countries. |

Source: Compiled from WTO Website.

As can be seen in Box 1.3, LDC graduation will result in the loss of specific preferential treatments (beyond those provided for developing country members of the WTO). The most important are the loss of preferences and reduced flexibility concerning implementation of the various WTO Agreements. Since the WTO was established in 1995, its members have, at different times, taken a number of decisions favouring LDC goods and services, through DF-QF market access and the LDC services waiver. Bilateral and regional initiatives also include LDC-specific provisions, notified to the WTO under article XXIV of the GATT. LDCs also benefit from preferential Rules of Origin (RoO), which are more flexible than those for non-LDC members. These flexibilities are lost on LDC graduation. Graduated LDCs also lose their eligibility for transition periods when implementing the TRIPS Agreement. Here LDCs draw benefits in two ways: (a) the general transition period (until 1 July 2021) and (b) the transition period for patents, licensing and undisclosed information for the pharmaceutical sector (until 1 January, 2033). Since the relevant decisions explicitly state that the transition period will end earlier if an LDC ceases to be an LDC, graduated LDCs can no longer enjoy the attendant benefits (WTO, 2020). Graduated LDCs will also no longer be eligible for other S&D provisions implemented exclusively for the LDCs.[16]

LDC-specific Southern RTA provisions in the form of longer trade liberalisation periods, additional preferential market access, reduced number of items in the sensitive lists and

[16] Graduated LDCs do not benefit from ongoing WTO work on RoO for LDCs in line with the MC10 decision in Nairobi. This is also true of work relating to the other decisions of successive WTO Ministerials such as MC6 (Hong Kong decision on DF-QF market access for LDCs), MC7 (decision with regard to the LDC Services Waiver) and MC9 (the Bali Package).

flexible RoO, among others, will also no longer be available once an LDC graduates.[17] The following section addresses some of the important related issues from the perspective of making SSC support sustainable graduation.

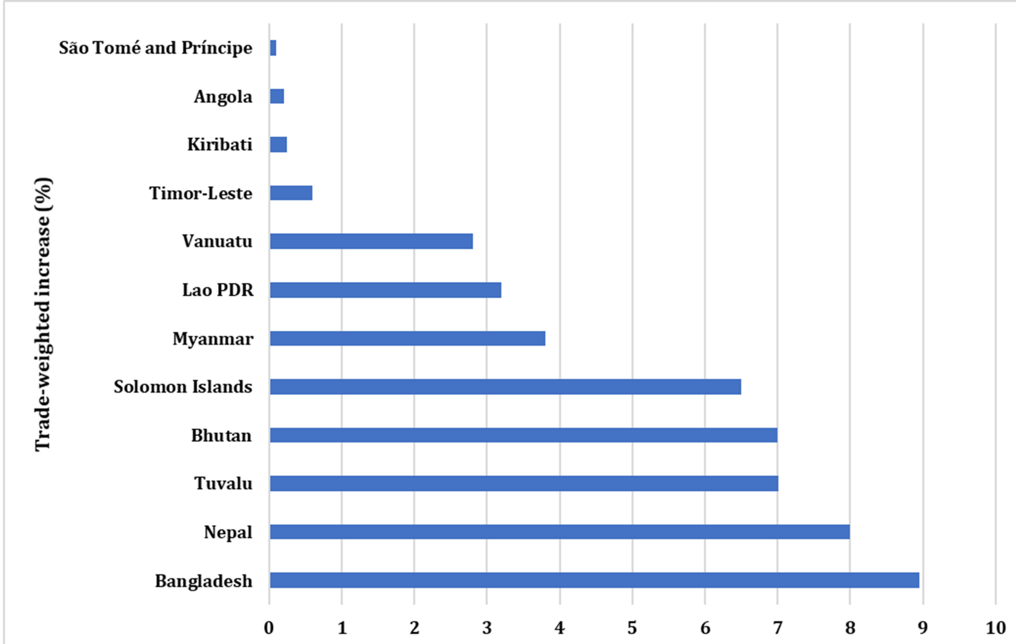
The extent to which individual LDCs are affected by the loss of LDC-specific provisions will hinge on several factors: (a) economic structure, (b) degree of openness and export dependence, (c) export composition, (d) tariff structure and Most Favoured Nation (MFN) duties on specific LDC exports including items that enjoy MFN zero duty, (e) membership of regional and bilateral RTAs and preferential treatment enjoyed as an LDC. Actual impact will also depend on the extent to which a particular graduating LDC benefits from LDC-specific preferential treatment.

Figure 5 presents WTO projections for the rises in tariff rates when a graduating LDC is no longer eligible for preferential treatment under LDC-specific schemes.[18] However, this data needs to be considered with some qualifications: (a) What percentage of the graduating LDC exports is covered by the destination country's LDC scheme? (b) What percentage of export of individual LDCs is actually able to enjoy in the form of preferential access? (c) What export share is covered by MFN duty-free? For example, in case of Bangladesh, the 9 percent tariff increase shown in Figure 5 is very relevant. About 70 percent of its exports enter various markets (e.g. EU, Canada, Japan, Australia, China, India etc.) at zero duty under LDC-specific schemes. Bangladesh does make use of its preferential treatment. So the 9 percent average tariff increase in these markets will have important export implications. On the other hand, while the projected tariff increase for Bhutan and Nepal (about 8 percent) is significant, it is not very relevant as only a low share of their exports actually enjoy LDC-specific preferential access. Most of their exports enjoy duty-free access to the crucial Indian market under bilateral free-trade agreements. In the case of the Solomon Islands where tariffs are projected to rise 6.5 percent, wood, which accounts for 70 percent of its exports, is subject to MFN zero duty.

[17] Graduated LDCs will, however, continue to enjoy flexibility from lower levels of commitments undertaken during accession, either during the Uruguay Round or at the time of accession to the WTO (e.g. lower binding coverage and lower bound tariffs).

[18] The products will either enter at MFN duty rate or under GSP schemes for developing countries.

**Figure 1.5:** *Projections on the Impact of LDC Graduation on Tariffs*




Source: Extracted from WTO_IDB database.
Note: Tariff rate changes are calculated as the difference between the best available tariff rate after graduation and tariff rate under LDC-specific preferences. Tariff increases are computed using tariff data for 2016. For trade weights, the average trade for 2016-2018 is used. Calculations assume full use of preferences

A recent study by the WTO Secretariat (WTO, 2020) estimates that if graduating LDCs are assumed to use preferential market access to the fullest extent, the additional (trade-weighted) tariffs they will face in the various preference-providing markets would be equivalent to about 4.2 percent.[19] The range of preference erosion will vary widely across the graduating LDCs, which is borne out by Figure 1.4. The depth of tariff erosion will be highest for Bangladesh and Nepal (in the range of 8-9 percent) and lowest for São Tomé and Príncipe, Angola, Kiribati and Timor Leste (0-1 percent). For example, preference erosion could reduce Bangladesh's exports by about 7-8 percent (Rahman and Bari, 2018). Loss of benefits under the WTO TRIPS and Public Health decision will also have a significant adverse impact on Bangladesh's pharmaceutical sector as the enforcement of TRIPS patent/license obligations becomes mandatory and enforceable (Rahman and Farin, 2018). The price of essential medicines will rise, with adverse implications for both producing LDCs and importing LDCs.[20]

The difficulties facing graduating LDCs are also likely to be accentuated in view of the pandemic. It has significant adverse impact on graduating LDCs' supply-side capacities, which has direct implications for employment and export earnings and indirect implications for poverty and inequality. The looming global recession is likely to aggravate the scenario and is already having a negative impact on their export performance. WTO dysfunction and the rise of mega-regionals such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and Regional Comprehensive Economic Partnership (RCEP) underscore the need for graduating LDCs to proactively find alternative avenues to facilitate market access and strengthen their development prospects post-graduation. The search for ways to deepen SSC in trade-related areas is now both relevant and important.

[19] The difference between LDC preference rate and next best rate.
[20] For example, a significant share of Bangladesh's pharmaceutical product exports is destined for Myanmar and a number of African LDCs.

A number of conclusions may be drawn from the need to explore avenues of SSC in view of LDC graduation. Firstly, LDC graduation carries significant adverse implications emanating from loss of preferential market access and loss of S&DT provisions. Secondly, while graduating LDCs are recommended for graduation on the basis of their commendable achievements in the graduation criteria, most continue to suffer from various structural weaknesses and vulnerabilities. Thirdly, the search for ways to deepen SSC as an enabler of sustainable LDC graduation has assumed heightened importance in view of the emerging global scenario. The next two sections explore possible avenues of deepening trade relationships within the ambit of SSC as key strategies that graduating LDCs need to pursue to address the attendant trade-related challenges.

## Section 2: Graduating LDC Trade Relationships with the Global South

Section 1 established the importance of trade for graduating LDC economies and examined what graduation will entail for these LDCs in some detail. In that light, this section will explore graduating LDCs' trade relationships with the Global South in more depth to discover what graduation will therefore entail. It will analyse graduating LDCs' trade flows to Global South countries, their membership of various RTAs, terms of membership and concessions, LDC-specific GSP schemes implemented by Southern providers, to find what graduation will entail in view of these. The idea is to identify ways to deepen trade-related SSC to support sustainable LDC graduation - the focus of Section 3.

### 2.1 Graduating LDCs and trade flows with Southern countries

**Table 2.1:** *LDC Graduation Changes to Market Access for South-South Trade*

| Graduating LDC | Total Export Value (2016-18 Average) | Share of Export to Southern Countries (2018) | Market Access Scenario | Impact of Graduation on South-South Trade |
|---|---|---|---|---|
| **Angola** | $40.8 billion | 83.5% | 53% exports are destined for China, 10% for India and 7% for USA. About 85% of Angola's exports (mainly fuel) are subject to MFN zero duty. It enjoys LDC-specific preferential market access on a number of other items. | Since a large part of Angola's exports are subject to MFN zero duty, its market access scenario will remain largely unchanged. A small share of export enters the Republic of Korea (RoK) under LDC schemes, which will be negatively affected by graduation. Its petroleum gas exports will face a higher tariff in RoK, which could result in export reductions of about 29%. Diamonds, (its second largest export commodity) could face a 10% tariff increase in India on graduation. |
| **Bangladesh** | $35 billion | 8% | Exports to India (3.3%) are covered by India's duty-free scheme under the South Asian Free Trade Area (SAFTA) (almost all items for LDCs). Exports to China (2%) are covered by China's LDC scheme. Exports to RoK are mostly subject to MFN duty. The share of MFN zero duty items is negligible. About 80% of its exports are to developed countries, about 65% of which are covered by LDC schemes (EU-EBA and Canada) market access to the USA (15% market share, mostly clothing) is not covered by GSP. | About 70% of Bangladesh's exports depend on LDC-specific preferences. Bangladesh will have the highest preference erosion impact will be of all graduating LDCs. However, the extent of South-South trade preference erosion will be limited because of low export exposure. Preferential export market access will no longer be available for key Southern partners as Bangladesh will no longer be eligible for LDC specific preferential access under India and China's GSP schemes. Tariffs in: India (+7%), RoK (+10%), and Turkey (+4%) are expected to rise. Market access to the EU (58%), Japan (3%) and Canada (3%), which is mostly covered by LDC GSP schemes, will be negatively affected by graduation. |

| Graduating LDC | Total Export Value (2016-18 Average) | Share of Export to Southern Countries (2018) | Market Access Scenario | Impact of Graduation on South-South Trade |
|---|---|---|---|---|
| **Bhutan** | $0.296 billion | 86.4% | Exports to India (over 80%) are covered by the Indo-Bhutan bilateral FTA. Exports to Bangladesh are by a bilateral trade agreement (a PTA is being negotiated). Bhutan is also a member of BIMSTEC-FTA. | Preferential market access to key Southern partners (about 85% of Bhutan's exports) will remain unchanged as they are covered by various bilateral arrangements or MFN duty-free. BIMSTEC FTA will also provide preferential access to regional partner markets. Only a small proportion of exports goes to developed countries. LDC-specific preference use is low. No tangible change in market access scenario is anticipated on graduation. |
| **Kiribati** | $0.154 billion | 90.5% | About 58% of exports are destined for Thailand. Its major export (93%): fish and fish products, are mostly MFN zero-duty (overall, 87% of its exports are subject to MFN zero-duty). | Only 2% of exports to preference granting members use LDC-specific preferences. Its key export: frozen fish, is MFN zero-duty in Thailand. Some RoK tariff rise (about 7-8%) is expected. Overall impact on graduation should be negligible. |
| **Lao PDR** | $5.15 billion | 88.7% | About 44% of exports go to Thailand, 28% to China, 4% to India and 1% to RoK. 45% of exports are MFN duty-free. | Only 7% of exports use LDC-specific preferences. 80% of exports to Thailand, the country's key partner, are subject to MFN zero-duty. Lao PDR also has a RTA with Thailand. It is not included in China's LDC scheme. About 30-40% of exports enter RoK under its LDC scheme, which will be negatively impacted by graduation. No tangible change is expected in market access to India. Lao PDR is not dependent on the LDC schemes of China and Thailand as it enjoys duty-free access under ASEAN-FTA. |
| **Myanmar** | $13.3 billion | 72% | Key Southern export markets are: China (27%), Thailand (20%) and India (67%). 47% of exports are subject to MFN zero duty. | No significant market access change is envisaged in key Southern markets. Tariffs on some items are expected to rise in RoK (by about 3.4%). In Thailand, China and India graduation is unlikely to change market access as the ASEAN FTA, 'ASEAN+China and ASEAN+India will continue to provide preferential treatment. As half of its important exports (apparel accounts for a quarter of its total exports) are destined for the EU, where it enjoys EBA benefits, there will be significant EU preference erosion. |
| **Nepal** | $0.830 billion | 66.0% | Exports to India represent 56% of its total exports, China 2% and Turkey 5%. About 22% of its total exports are subject to MFN zero tariff. It has a bilateral FTA with key partner India. Exports to Bangladesh are covered by bilateral agreements under SAFTA. Exports to the EU (13.3% are given preferential access (EBA) but exports to the USA (11.2%) are not. | The South-South export scenario will not change significantly on graduation. Nepal has a bilateral FTA with India granting DF access, which is expected to continue. China will remain unchanged. A BFTA with Bangladesh is on the cards. However, apparel, Nepal's major export to the EU, will lose preferential access. |
| **São Tomé and Príncipe** | $0.024 billion | 3.6% | Southern countries are not major export destinations. 90% of global exports are MFN zero duty. | The market access scenario is expected to remain more or less unchanged on graduation. Its main export: cocoa beans, is mostly MFN duty-free. |

| Graduating LDC | Total Export Value (2016-18 Average) | Share of Export to Southern Countries (2018) | Market Access Scenario | Impact of Graduation on South-South Trade |
|---|---|---|---|---|
| **Solomon Islands** | $0.845 billion | 84.6% | China (62%), India (8%) and Thailand (2%) are major Southern destinations. Major export: wood (70%), is mostly MFN zero-duty. | The Solomon Islands does not receive LDC-specific preferences in its key Chinese market. SPARTECA preferential treatment will continue on graduation. The market access scenario for South-South trade is therefore likely to remain unchanged. |
| **Timor-Leste** | $0.110 billion | 74.4% | Major Southern partners include: Thailand (34%) and China (2%). Most exports (95%) are MFN duty free (including petroleum - 70% of its total exports). | Timor-Leste is a beneficiary of RoK and China LDC schemes, which it will lose on graduation. But, since most exports are MFN duty-free, its market access scenario is not expected to change significantly on graduation. |
| **Tuvalu** | $0.060 billion | 90.2% | Thailand (75% of total trade) is the key Southern trading partner. About 25% of exports are MFN duty-free. | Tuvalu does not use LDC schemes in preference granting markets. The average tariff applied is projected to remain unchanged after graduation, implying no tangible change in market access.. |
| **Vanuatu** | $0.299 billion | 54.2% | Major Southern destinations include RoK (6%), Thailand (5%) Turkey (4%) and China (4%). Vanuatu enjoys preferential access under the China and RoK LDC schemes. About 30% of its exports are MFN duty-free. | Tariffs will increase 3-7% in China and RoK on graduation. It will continue to enjoy preferential market access under PACER and PICTA. Some adverse market access impact is expected on graduation. |

Source: Author's assessment based on WTO (2020b), Trade map database, and EPB (2020).

Note: Share of South-South exports of graduating LDCs' total exports: 55.1%.
Share of South-South exports of LDCs total exports: 57.8%.
Share of South-South exports of total global exports: 46.4%.

An analysis of graduating LDCs' direction of trade flows indicates that over half of their exports are destined for the Global South (55.1 percent in 2018). This figure is similar for all LDCs combined (57.8 percent) and the non-graduating LDCs alone (60.8 percent). For imports these three figures are respectively: 82.4 percent, 79.4 percent and 77.6 percent, which shows the higher LDC and graduating LDC concentration of imports from the Global South. As Table 2.1 shows, these shares vary across the individual graduating LDCs. For example, the respective shares of exports to the Global South were significantly high in: Kiribati (90.5 percent), Lao PDR (88.7 percent), Bhutan (86.4 percent) and Angola (83.5 percent). However the corresponding shares were relatively low for São Tomé and Príncipe (3.6 percent) and Bangladesh (8 percent).[21] Vanuatu (54.2 percent) and Nepal (66.3 percent) were somewhere in the middle. Bangladesh is unusual among the graduating LDCs in that the Northern EU (59 percent) and USA (14.0 percent) markets together account for almost three-quarters of total exports. São Tomé and Príncipe has a similar Northern market concentration: EU countries accounted for 95 percent of the country's exports. Interestingly, 83.5 percent of Bangladesh's imports originate in the Global South. As the table shows, the only country with less than half of its imports originating in the Global South is São Tomé and Príncipe (38.8 percent). The Global South therefore accounts for a significantly high share (about 70 percent,) of the 12 graduating LDCs' trade flows (export plus import).[22]

[21] If Bangladesh is excluded; the Global South share of total graduating LDC imports is in the range of 70 percent.

[22] Table 3 also reveals most graduating LDCs' single item dependence. Their degree of export concentration is generally high, indicating vulnerability: Bangladesh on clothing (84 percent), Angola on petroleum (83.5 percent), Bhutan on electricity (86.4 percent). (Comtrade data).

As Table 2.1 shows, China is a key trading partner for many graduating LDCs. China alone accounted for more than a-fifth of total LDC trade; and it's respective shares of exports and imports were 23 percent and 21 percent. India, Thailand, Vietnam and the Philippines are also important export destinations for some graduating LDCs. In terms of imports, India (10 percent) and Singapore (6 percent) are the two most important Southern trading partners besides China.

An analysis of various graduating LDCs' trade flows with Southern partners reveals interesting features. In South Asia, all three graduating LDCs have a close trading relationship with India (Bangladesh to a lesser extent). Of these three graduating LDCs, Bhutan has the highest South Asian trade share: over four-fifths of the country's 2018-19 trade was intra-regional. About 88.8 percent of Bhutan's exports and 80 percent of its imports are South Asian. India is by far the dominant trading partner, accounting for 81 percent of Bhutan's total exports. Bhutan's key export: electricity, accounted for one-third of its total exports and is entirely destined for the Indian market. Bangladesh and Nepal account for 6.4 percent and 2.9 percent of Bhutan's exports respectively. Hong Kong (5.8 percent) and China (3.8 percent) are important Southern non-South Asian markets for Bhutan. In terms of imports, India is Bhutan's key partner, accounting for about four-fifths of the country's total imports. China (6 percent), Republic of Korea (3.4 percent), Thailand (2.6 percent) and Singapore (2.6 percent) are the other regional sources.

Regional trade is also dominant for Nepal, with South Asia accounting for about 66.2 percent of the country's total exports and about 48.5 percent of its total imports. Here again, India was the dominant trade partner, accounting for about half of Nepal's exports (56. percent), while Turkey (5.6 percent) was the other notable Southern export destination.

Of the three South Asian graduating LDCs, Bangladesh had the lowest regional exposure: about 3.5 percent of the country's total exports and 17.5 percent of its total imports were from South Asia. Predictably, India has the lion's share of Bangladesh's regional trade: about 88.6 percent of regional exports and 90.8 percent of regional imports. Pakistan is Bangladesh's other notable trading partner in South Asia at 3.2 percent exports and 8.0 percent imports. The Association of Southeast Asian Nations (ASEAN) market accounted for only 1.7 percent of Bangladesh's total exports.[23] However, Bangladesh has significant imports from non-South Asian regions in the Global South. In 2018, China represented about 30 percent of the country's total imports and was its most important import partner. Other important import sources include: India (15.7 percent), Singapore (6.1 percent), Malaysia (3.9 percent) and Indonesia (3.5 percent).[24]

The largest of the three Southeastern graduating LDCs: Myanmar, has strong regional trade, dominated by China, which represents one-third of the country's global trade share. In 2019, Myanmar's top export destination was China (33.3 percent), followed by Thailand (18.0 percent), India (3.4 percent), Hong Kong (3.4 percent), Singapore (2.9 percent) and Republic of Korea (2.7 percent). China is also the preeminent import source (32.2 percent), followed by Singapore (19.2 percent), Thailand (13.5 percent), India (5.2 percent), Indonesia (4.8 percent), Vietnam (3.1 percent) and RoK (2.3 percent).

Regional countries have the lion's share of Lao PDR's trade. Its major export destinations are China (36.1 percent) and Thailand (31.3 percent). The country's major sources of imports are Thailand (61.8 percent), China (18.2 percent) and Vietnam (10.1 percent). Regional markets also dominate Timor-Leste's trade. Singapore is the most important destination for exports (60.6 percent), followed by Indonesia (5.5 percent) and China

23 ASEAN countries accounted for 5.8 percent of Bangladesh's total non-RMG exports.

24 Both China and India have seen rapid rises in their share of Bangladesh's total imports in recent years. This trend is also true for most graduating LDCs.

(4.2 percent). Key import countries are: Indonesia (40.2 percent), China (28.3 percent), Singapore (7.7 percent) and Thailand (7.0 percent).

A number of graduating LDCs are very vulnerable to commodity price fluctuations.

Among Africa's graduating LDCs, intra-Africa exports accounted for only 5 percent of Angola's, global exports and 12 percent of its total imports. However, Angola has strong trading relationships with non-African Southern countries. Major Southern export destinations are: China (55 percent), India (9.5 percent) and UAE (5.3 percent). China (15.9 percent), Singapore (12.4 percent) and Togo (6.1 percent) are key import sources. São Tomé and Príncipe, (13.0 percent) is the major Southern export destination for the other African graduating LDCs,, while Angola (20.2 percent), China (6.6. percent) and Malaysia (1.9 percent) are the key Southern import sources. In the Pacific region, Southern flows dominate graduating LDC Kiribati's trade to its key export destinations: Thailand (63.8 percent), Mexico (15.5 percent), Philippines (6.2 percent) and RoK (2.8 percent). While its major import sources were: Fiji (20.1 percent), China (20 percent) and RoK (14.6 percent). Tuvalu's major export destinations were: Thailand (59.5 percent), Philippines (18.7 percent) and Nigeria (1.7 percent) while Fiji (42.4 percent) and China (25.5 percent) were its major sources of imports.

A number of graduating LDCs are very vulnerable to commodity price fluctuations. Angola is a relevant example. Its economy is significantly affected by the current oil price dip, while it is slated for graduation in 2021. The same is true for Timor-Leste.

The above analysis helps draw a number of important insights. Firstly, graduating LDCs have strong trade relationships with the Global South.[25] Secondly, Asia is important in terms of LDC trade flows, with rising shares in China, India and Thailand. Thirdly, while the six Asian graduating LDCs have strong ties within the Asian region, the six graduating LDCs from Africa and the Pacific region do not. These LDCs tend to trade more with Asian countries. Even in Angola, by far the largest graduating LDC in the Africa-Asia Pacific region, trade flows to Africa represented less than 7 percent of total trade. Fourthly, and importantly from the perspective of deepening SSC, large shares of Southern trade flows are covered by the various Southern RTAs of which the graduating LDCs are members. This will now be examined in more detail.

## 2.2 Graduating LDCs and Southern RTAs

The preceding section revealed graduating LDCs' strong trade relationships with the Global South in significant trade flows, in particular with South and South-East Asian countries. As noted earlier, about 55.1 percent of total graduating LDC exports were destined for Global South markets, whereas the share was as high as 82.4 percent for imports. The rise of China, India and Thailand, as both export destinations and import sources, is becoming increasingly prominent. This section explores the role of Southern Bilateral Free Trade Agreements (BFTAs) and RTAs, and examines the extent to which LDC-specific preferential market access schemes by Southern partners like China, India and Brazil are important.

A review of the relevant literature shows that graduating LDCs enjoy preferential market access to Southern trading partners through three routes: (a) as members of RTAs; (b) as part of bilateral trading arrangements and (c) as beneficiaries of Southern countries' LDC-specific preferential market access schemes.

Graduating LDCs enjoy various specific trade-related RTA and BFTA benefits. These take the form of (a) non/less than-reciprocal preferential treatment; (b) preferential market access; (c) preferential RoO; (d) flexible trade liberalisation commitments; (e) more import

[25] Except for export relationships in case of Bangladesh (where Northern markets such as US, EU and Canada are predominant), and São Tomé and Príncipe (where most exports go to the EU)

items included in LDC sensitive lists and fewer items on the sensitive lists of developing country partners and (f) special treatment and flexibilities in terms of compliance requirements and obligations. Graduating LDCs enjoy non-reciprocal preferential market access as beneficiaries of their Southern partners' LDC-specific preferential market access schemes, mainly in the form of duty-free (or less than MFN duty) market access and favourable RoO.[26] The trade liberalisation plan allows for slower trade opening by these countries. They are also allowed to keep a larger number of items on their sensitive list to protect domestic industries. Some RTAs have special schemes to compensate for revenue losses arising from the implementation of trade liberalisation schemes.

[26] In terms of both domestic value addition and regional cumulation and change of tariff heading (CTH) requirements.

**Box 2.1:** *Graduating LDCs in RTAs and BFTAs*

| Graduating Asian LDCs | Ratified and in Operation | Proposed/ Under Study |
|---|---|---|
| Bangladesh (*South Asia*) | APTA (1976)<br>D8 PTA (2011)<br>SAFTA (2006)<br>*Not yet in effect:* Trade Preferential System of the Organization of the Islamic Conference (2014)<br>*Negotiations launched:* Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC-FTA, 2014). Negotiations on goods trade completed; discussion on trade in services being confirmed. | Bangladesh-Bhutan PTA (2019)<br>Bangladesh-Nepal FTA (2020)*<br>Bangladesh-Indonesia FTA (2020)*<br>Bangladesh-Brazil FTA (2018)<br>Bangladesh-India FTA (2018)<br>Bangladesh-People's Republic of China FTA (2016)<br>Bangladesh-Sri Lanka FTA (2016)<br>Bangladesh-Thailand FTA (2020)<br>Bangladesh-Turkey FTA (2012)<br>Bangladesh-Pakistan FTA (2003) |
| Bhutan (*South Asia*) | Bhutan-India Trade Agreement (2006)<br>SAFTA (2006)<br>*Negotiations launched:* BIMSTEC-FTA (2014). Negotiations on trade in goods completed; discussion as regards trade in services confirming | Bangladesh-Bhutan PTA (2019) |
| Nepal *(South Asia)* | Indo-Nepal Treaty of Trade (2002)<br>SAFTA (2006)<br>*Negotiations launched:* BIMSTEC-FTA (2014). Negotiations on goods trade completed; services trade discussions being confirmed. | Nepal-Pakistan Free Trade Agreement (2009)<br>Nepal-People's Republic of China Free Trade Agreement (2016) |
| Lao PDR *(Southeast Asia)* | ASEAN FTA (1993)<br>ASEAN-Australia and New Zealand FTA (2010)<br>ASEAN-Hong Kong, China FTA (2019)<br>ASEAN-India Comprehensive Economic Cooperation Agreement (2010)<br>ASEAN-Japan Comprehensive Economic Partnership (2008)<br>ASEAN-People's Republic of China Comprehensive Economic Cooperation Agreement (2005)<br>ASEAN-Republic of Korea Comprehensive Economic Cooperation Agreement (2007)<br>APTA (1976)<br>Laos-Thailand Preferential Trading Arrangement (1991)<br>*Negotiations launched:* RCEP (2013). A 15-country FTA has been agreed.[27] Negotiations on goods trade completed; discussions on services trade being confirmed. | ASEAN-Canada FTA (2017)<br>ASEAN-EU FTA (2015)<br>ASEAN-Eurasian Economic Union FTA (2016)<br>ASEAN-Pakistan FTA (2009)<br>Comprehensive Economic Partnership for East Asia (CEPEA/ASEAN+6) (2005)<br>East Asia FTA (ASEAN+3) (2004) |

[27] In September 2019, the 7th RCEP Ministerial Meeting agreed to sign a 15 member free-trade area by the year 2020. The group includes two graduating South East Asian LDCs: Myanmar and Lao PDR. It also includes the other ASEAN 10 countries: Brunei, Cambodia, Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam and three other East Asian ASEAN Plus Three members: (China, Japan and Republic of Korea) as well as two members of ASEAN Plus Six (Australia and New Zealand). India has a FTA with ASEAN and did not join (however, negotiations continue).

| Graduating Asian LDCs | Ratified and in Operation | Proposed/ Under Study |
|---|---|---|
| Myanmar *(Southeast Asia)* | ASEAN FTA (1993)<br>ASEAN-Australia and New Zealand FTA (2010)<br>ASEAN-Hong Kong, China FTA (2019)<br>ASEAN-India Comprehensive Economic Cooperation Agreement (2010)<br>ASEAN-Japan Comprehensive Economic Partnership (2008)<br>ASEAN-People's Republic of China Comprehensive Economic Cooperation Agreement (2005)<br>ASEAN-Republic of Korea Comprehensive Economic Cooperation Agreement (2007)<br>*Not yet in effect:* Myanmar-US FTA (2013)<br>*Negotiations launched:* BIMSTEC-FTA (2014)<br>RCEP (2013). Negotiations on goods trade completed; discussions on services trade being confirmed. | ASEAN-Pakistan FTA (2009)<br>Comprehensive Economic Partnership for East Asia (CEPEA/ASEAN+6) (2005)<br>East Asia FTA (ASEAN+3) (2004)<br>ASEAN-Canada FTA (2017)<br>ASEAN-EU FTA (2015)<br>ASEAN-Eurasian Economic Union FTA (2016) |
| Timor-Leste *(Southeast Asia)* | *Has not signed any agreement as yet. Has applied for ASEAN membership in 2013.* | |
| Kiribati *(Asia-Pacific) and* Tuvalu *(Asia-Pacific)* | Pacific ACP-EC Economic Partnership Agreement (2014)<br>PICTA (2003)<br>South Pacific Regional Trade and Economic Cooperation Agreement (1981)<br>*Not yet in effect:* PACER Plus (2017) | |
| Solomon Islands *(Asia-Pacific) and* Vanuatu *(Asia-Pacific)* | MSG (1993)<br>Pacific ACP-EC Economic Partnership Agreement (2014)<br>PICTA (2003)<br>South Pacific Regional Trade and Economic Cooperation Agreement (1981)<br>*Not yet in effect:* PACER Plus (2017) | |
| Angola | Common Market for Eastern and Southern Africa (COMESA)<br>Southern African Development Community (SADC) | |

Source: Based on the Asia Regional Integration Center FTA database (https://aric.adb.org/database/fta).

As Box 2.1 illustrates, graduating LDCs belong to a large number of RTAs including other LDCs and Southern developing countries. Some are also members of RTAs negotiating new FTAs with other developing and developed nations (e.g. RCEP)[28] and of FTAs being negotiated with developed countries (e.g. ASEAN-Canada FTA, ASEAN-EU FTA). Angola is member of COMESA and SADC.[29] Asia-Pacific graduating LDCs are also members of a number of RTAs. A closer look at Box 2.1 reveals that many graduating LDCs have initiated bilateral negotiations with a number of other countries (both LDCs and developing countries). Bangladesh has initiated bilateral PTA/FTA discussions with 11 countries including graduating LDCs (such as Bhutan) and developing countries (such as Sri Lanka and Malaysia). However these are currently in the initial negotiation stages.

Many regional and bilateral trading arrangements use a two-tier approach for LDC and non-LDC members. Under SAFTA, (which came into force in 2006,) SAARC LDCs[30] enjoy S&D status in various forms: (a) smaller initial tariff reduction and longer implementation period under trade liberalisation programmes; (b) longer list of sensitive goods exempt from liberalisation commitments than non-LDC signatories; (c) shorter sensitive lists in partner developing countries that allow DF-QF market access for a larger number of goods; (d) less stringent RoO both for domestic value addition and regional accumulation; (e) greater flexibility in continuing with quantitative and other restrictions and in the

[28] RCEP was signed very recently, on 15 November 2020 and is expected to come into force in early 2021.

[29] Note that African countries have also decided to form a pan-African FTA involving almost all of the African countries including LDCs and graduating LDCs.

[30] SAFTA includes the three graduating LDCs (Bangladesh, Bhutan and Nepal) and Afghanistan (LDC).

application of anti-dumping and countervailing duties and safeguard measures; (f) a mechanism to compensate for loss of revenue on account of trade liberalisation.[31] India subsequently offered non-reciprocal DF-QF market access to all four LDC members. This was significant from the point of view of these countries' export interests.[32] Two South Asian graduating LDCs: Bhutan and Nepal, also have bilateral FTAs with India, under which they enjoy DF-QF market access. This is particularly important to the graduation discussion. The three graduating LDCs will cease to enjoy the benefits of India's unilateral preferential scheme under SAFTA once they leave the LDC group. However, bilateral preferential market access (offered to Nepal and Bhutan) is set to continue after graduation. Bangladesh does not have a BFTA with India, so graduation will lead to significant loss of preference. The conclusion of the BIMSTEC-FTA goods negotiations augurs well for its four graduating LDC members (Bangladesh, Nepal, Bhutan and Myanmar) as BIMSTEC-FTA also has a two tier LDC and non-LDC system.[33] BIMSTEC-FTA is important for South Asia's three graduating LDCs as it provides these countries with an opportunity to enter the ASEAN market from a position of strength.

When a graduating LDC enjoys preferential market access as part of bilateral FTA, graduation will not entail any changes

In South-East Asia, ASEAN-FTA membership allowed the two graduating LDCs (Myanmar and Lao PDR)[34] to reap significant benefits from the S&D treatment initially given to Cambodia, Myanmar, Lao PDR and Vietnam under the ASEAN Common Effective Preference Tariff (CEPT) scheme. Since 2018, most ASEAN tariffs have been reduced to zero, so preferential margins were significantly reduced. The two graduating LDCs also benefit from the six ASEAN FTAs.[35] Tariff elimination schemes under these FTAs (with tariff lines ranging from 76.6 percent for India to 93.6 percent for China) have given both graduating LDCs considerable competitive edge in terms of preferential market access to these trading partners.

The above discussion illustrates the benefits graduating LDCs can enjoy under the various RTAs and BFTAs. Where these benefits are LDC-specific (two-track), they will cease on LDC graduation. When a graduating LDC enjoys preferential market access as part of bilateral FTA (e.g. Bhutan and Nepal with India), graduation will not entail any changes (unless the terms are renegotiated). Where partner countries reduce their tariffs to zero for all member countries' exports, the additional advantage enjoyed by partner LDCs under the two-track system, is eroded. However, even in such cases partner countries may adopt more relaxed RoO or other flexibilities (e.g. SPS/TBT) for LDC members.

In line with the Hong Kong Ministerial (MC6) meeting, a number of developing countries have also expanded coverage of their dedicated LDC preferential market access schemes, to move gradually to 97 percent of the tariff lines. ,The LDC-specific schemes of China, India, Thailand and the Republic of Korea are the most important for many graduating LDCs in view of their current direction of trade (WTO, 2020). The revised Chinese scheme extending duty-free market access for LDC goods was implemented in 2017. This scheme covers 96.6 percent of tariff lines and includes most of the items exported by graduating LDCs (exclusions include chemicals, transport vehicles, paper).[36] The Indian scheme (2016) covers 94.1 percent of tariff lines (exclusions include plastics, coffee and tea, tobacco, alcoholic beverages). The Thai LDC scheme (2017) gives LDCs DF-QF market access for 78.7 percent of tariff lines (exceptions include apparel, transport

[31] While this is allowed under SAFTA, it has never been used in the history of this agreement.
[32] India's LDC DF-QF offer includes virtually all items except 25 specific categories including arms, narcotics, alcohol...
[33] Although BIMSTEC-FTA negotiations were supposed to involve both goods and services, discussions on services have not made much progress to date.
[34] Timor-Leste has applied for ASEAN membership in 2013. Although the country's Strategic Development Plan (2011-2030) states its aspiration to become an ASEAN member, little real progress appears to have been made.
[35] ASEAN-Australia, ASEAN-China, ASEAN-India ASEAN-Japan, ASEAN-Korea and ASEAN-New Zealand.
[36] A notable exception was Bangladesh, which received DF access from China for 3,095 items under the APTA. Then in June 2020, China offered DF market access for 8,256 items covering 97 percent of the tariff lines.

vehicles, iron and steel goods, electrical machinery and appliances). The Republic of Korea's LDC scheme covers 89.9 percent of tariff lines (exclusions include fish, wood products, mineral fuels, oil seeds). After graduation, LDCs will no longer be eligible for preferential access under these schemes.[37]

## 2.3 Loss of preferences and implications

The implications of graduation in terms of loss of preferences, both under global LDC schemes, and LDC schemes at regional and bilateral levels, need to be considered from several angles: the range of preferences, goods coverage, depth of preferential treatment and ability to enjoy preferences. A number of studies have shown that LDCs benefited from preferential market access schemes, although it is difficult for them to take full advantage of these benefits, for various reasons (e.g. UNESCAP (2020); WTO, 2020b). Non-tariff barriers, supply side constraints, lack of proper trade facilitation, and subsequently longer lead times, have undermined their ability to achieve the export potentials facilitated by these trading arrangements. Thus, while large shares of graduating LDC goods can enter markets taking advantage of preferential market access, the range of these products and their export value are below potential. This is where deepening SSC to build supply side export capacities comes in. Secondly, this study reveals that even when LDC-specific preferences are gone, many graduating LDCs will continue to enjoy preferential market access under bilateral arrangements, or as part of RTAs. Indeed, as a recent study (WTO, 2020) shows, an average of only 12 percent of exports enter preference–granting markets under LDC-specific schemes (across all 12 graduating LDCs). Bangladesh is unusual in comparison with the other graduating LDCs – about 70 percent of its exports use LDC-specific preferences while the comparable figures are 10-20 percent for Myanmar, Nepal and Solomon Islands, 5-10 percent for Bhutan and Lao PDR and below 5 percent for Angola, Kiribati, São Tomé and Príncipe, Timor-Leste, Tuvalu and Vanuatu (WTO, 2020).

While large shares of graduating LDC goods can enter markets taking advantage of preferential market access, the range of these products and their export value are below potential.

Except for Bangladesh, most graduating LDC goods trade occurs either through their membership of RTAs or BFTAs. Using RTAs and BFTAs to achieve sustainable graduation in view of addressing post-graduation challenges is therefore relevant. Thirdly, many graduating LDCs already actively pursue policies of regional and sub-regional integration to off-set the loss of trade preferences and as part of their sustainable graduation strategy.

This underlines the importance of deepening SSC from two perspectives: SSC can be a strategy to compensate for the loss of current preferences and SSC can be a strategy to use the preferential market access granted under RTAs and BFTAs and to build supply-side capacities through closer regional and sub-regional cooperation. This is crucial not only for increasing exports but also for the overall economic development of these countries. The next section explores some of the SSC initiatives that could be pursued in this regard.

[37] RoO for China's LDC-specific GSP scheme entails 40 percent regional value cumulation (RVC) or change of tariff heading (CTH). Under India's LDC GSP scheme, the RoO require a CTH and domestic value addition requirement of 30 percent.

## Section 3: SSC and Trade-related Support for Graduating LDCs

The LDC Report 2016 (UNCTAD, 2016) states that graduation should not be seen as: “a winning post, but rather as a milestone in a country’s long-term economic and social development. Thus, the focus should not be on graduation itself, but rather on “graduation with momentum”, which will lay the foundations for long-term development and allow potential pitfalls to be avoided far beyond the country’s exit from the LDC category.” The preceding sections have demonstrated the importance of trade for graduating LDC economies, revealed the high proportion of South-South trade by analysing South-bound trade flows and shown the important role played by regional and bilateral trading arrangements.[38] Graduated LDCs will no longer be eligible for preferential market access under the preferential schemes of Southern providers such as India, China, Thailand and South Africa. For graduating LDCs overwhelmingly dependent on non-reciprocal market access from developed countries (such as Bangladesh,) the implications of loss of preference on graduation will be highly significant. Although graduated LDCs will be eligible for preferential treatment under general GSP schemes by developed and developing countries, their breadth of coverage and depth of tariff reductions are much shallower than those for the LDCs; and the RoO are much more stringent. There will also be significant adverse implications for trade performance resulting from the loss of various S&D provisions (under TRIPS, TRIMS, AoA and other WTO Agreements).

Options for deepening (particularly South-South) trade cooperation for graduating LDCs need to be re-examined. Indeed, a number of global events including the decadal 2011 Programme of Actions for LDCs (IPOA, 2011) and the Second High level UN Conference on SSC (BAPA+40 in March 2019) have emphasised the importance of SSC in this respect. For example, IPOA underscored the importance of smooth graduation. It emphasised the need to ensure that these LDCs are able to embark on a sustainable development path, through appropriate programmes and projects, in line with their own smooth transition strategy (IPOA, 2011). The Addis Ababa Action Agenda (AAAA, 2015) highlighted the need to deepen SSC and triangular cooperation to support LDCs, LLDCs and the SIDs. Successive WTO conferences have called on members to come up with initiatives that support graduating LDCs.

A number of UN Resolutions specifically asked members to take concrete measures to support graduating LDCs. The UN Resolution that followed IPOA 2011 (UNGA 2019: A/RES/74/232), urged development partners to strengthen graduation support for smooth transition so that graduating LDCs could minimise disruptions (para 3). The 2030 Agenda for Sustainable Development emphasised that the Addis Ababa Agenda for a revitalised global partnership was an integral part of the SDGs; the AAAA in turn recognised the need to support graduating LDCs to sustain development progress towards the SDGs (AAAA, para 73). BAPA+40 reviewed current measures and identified new measures to deepen SSC, which is extremely important for the future of graduating LDCs.

As a result, the following sub-sections identify and propose trade-related measures to support graduating LDCs by deepening SSC.

[38] As WTO (2020a) informs, 74 percent of the 12 graduating LDC exports of 94.5 billion (2018) entered the export markets under some type of preferential schemes. These shares were very high for Nepal (95.2 percent) and Bhutan (94.5 percent), and significant for Angola (77.3 percent) and Bangladesh (72.6 percent). For others such as Timor-Leste, this is of low significance as its main export: crude oil, is mostly MFN zero duty.

## 3.1 Adjust Southern RTAs to support LDC graduation

**Box 3.1:** *Support for Graduating LDCs in Various Trade-related Areas*

| Programme | Area of Support and Provider | Post-graduation Extension Period |
|---|---|---|
| EU's Everything but Arms scheme (EBA) | Trade related, LDC-specific, market access support from the EU | 3 years |
| Enhanced Integrated Framework (EIF) | Trade related, capacity-building, multi-donor support managed by UNOPS | 5 years |
| UN Capital Development Fund (UNCDF) | Financial support for LDCs | 3 years + 2 years on an equal cost sharing basis |
| Least Developed Countries Fund (LDCF) | Climate fund operated by the Global Environment Facility (GEF) | Projects approved before graduation funded |
| UN Technology Bank for LDCs | ICT and knowledge sharing platform | 5 years |
| International Development Law Organization (IDLO) pro-bono legal support | On-demand legal and professional assistance for LDC governments | 5 years |
| UN travel support for GA sessions | Travel support fund from UN agencies | 3 years |

Source: http://unohrlls.org/custom-content/uploads/2020/01/Solomon-Islands-Joint-Graduation-Workshop_SUMMARY.pdf

As Box 3.1 shows, several countries and international organisations have come up with a number of unilateral measures to support graduating LDCs through the WTO and as part of various UN initiatives. The EU extended EBA for three more years (WTO was notified to this effect); EIF and LDC technology transfer support have been extended 5 years.[39] Southern countries could similarly extend preferential market schemes for a specific period after graduation. This could be applied in view of the two-tier schemes in Southern RTAs and BFTAs. Southern countries with LDC-specific preferential market schemes (e.g. India, China, Thailand, Republic of Korea, South Africa) could also extend preferential treatment for graduated LDCs. RoO including regional cumulation and sensitive list items should remain unchanged, while no quotas should be imposed on preferential market access. It is interesting to note that China continued LDC-specific market access for Samoan items of export interest (agri-products), following the country's graduation in 2014. Similarly, SAFTA establishes special provision for the Maldives (Article 12), (a graduated LDC,) extending the same treatment provided to LDC members of the grouping.[40]

As Box 2.1 clearly shows, many graduating LDCs are considering signing bilateral FTAs and comprehensive economic partnership agreements with Southern partners. However, unlike the two-tier RTAs and LDC specific Southern schemes, these cooperation agreements will have a large degree of non-reciprocity. This study suggests that Southern developing country partners to such agreements, offer more than reciprocal access to graduated LDCs for a specific period of time, in terms of preferential treatment, RoO, and other trade-related provisions.[41].

## 3.2 Extend Southern solidarity to support graduation

Southern solidarity in global trade fora such as the WTO could significantly strengthen current moves supporting graduating LDCs. Graduating LDCs have asked WTO for the extension of market access and S&D provisions for a limited period. Chad floated

[39] While such measures are not enough given graduating LDC needs, they have been welcomed as concrete support for sustainable graduation. Graduating LDCs are keen to have LDC-specific market access extended by some additional years, in line with the extension offered by the EU.

[40] Maldives graduated out of the LDC group in 2011. Article 12 of SAFTA stipulates that the Maldives were to be given LDC treatment in the Agreement and any subsequent contractual undertakings.

[41] This could be in the form of flexible ADD and CVD provision enforcement for a certain period of time, by not imposing TRIPS and TRIMS plus provisions, etc.

a proposal on behalf of the LDC group, calling for reinforced measures to support sustainable LDC graduation. Their submission proposes that the upcoming MC12 decide to allow graduating LDCs to enjoy benefits accruing from all S&DT measures and the exemptions available to LDCs under various (current and future) WTO Agreements, for a specific period. Graduating LDCs are also seeking additional flexibilities in view of ongoing WTO discussions, for example, in the context of fishing subsidies and new issues such as e-commerce and MSMEs. Strong support from Southern WTO members will create momentum in ongoing discussions in Geneva. Their support could be crucial in getting the proposal on the MC12 discussion agenda. A commitment to extend LDC-specific market access from Southern providers will create a lot of synergy for a positive outcome at the upcoming Ministerial Conference.[42] As noted earlier, a number of other important events where LDC-specific issues will come up for discussion are planned for the next few years. The LDC V conference in January 2022 in Doha, Qatar could be a crucially important opportunity to steer the discussion towards ISMs for sustainable LDC graduation. Concrete trade and financial flow initiatives under the rubric of SSC, could add momentum to the discussion.

Trade-related support to help LDCs double their share of global exports is an important target to be achieved by 2020.

The 2030 Agenda considers international trade as an engine for inclusive economic growth and poverty reduction and recognises that trade makes an important contribution to sustainable development. The SDG 17 on global partnership stipulates that countries take concrete measures to support LDC development. Trade-related support to help LDCs double their share of global exports is an important target to be achieved by 2020. However, the current share of less than 1 percent is far off the target 2 percent, as preceding sections have noted. The cohort of graduating LDCs have been unable to raise their relative share of global trade in any tangible way over this period. Southern support for graduating LDC trade capacity building achieved by deepening regional and bilateral cooperation is very much in line with the spirit of the SDGs.

To support graduating LDCs, India could offer the three graduating LDC members of SAFTA an extension of the DF market access currently extended to the four LDCs. This would particularly benefit Bangladesh with which India does not have a bilateral FTA (unlike Bhutan and Nepal). In the context of the ASEAN FTA, and in view of the RCEP Agreement, partner countries could conceive concrete measures to support the sustainable graduation of Myanmar and Lao PDR. This support could be similar to that granted to the LDCs, but limited to a specific time after graduation. It could concern areas including preferential market access, removal of Non-Tariff Barriers to trade (NTBs), obligations, SPS/TBT compliance etc. Timor-Leste has been striving for ASEAN membership for several years (it first applied in 2013). ASEAN members could fast forward this process to support its sustainable graduation.

The Pacific Agreement on Closer Economic Relations (PACER) launched in 2017 and is yet another example to consider in this context. The four graduating pacific island LDCs: Kiribati, Solomon Islands, Tuvalu and Vanuatu, are signatories. The agreement covers trade in goods and services, investment, labour, Sanitary and Phytosanitary Systems (SPS) and other issues. The tariff reduction schedule is slower for the four LDC signatories, with reductions beginning in 2028, unless a country graduates earlier. In view of this, trade liberalisation and other commitments will come into force upon graduation. In consideration of their vulnerabilities, New Zealand and Australia could offer these LDCs an extension for implementation of the tariff liberalisation timeline (possibly beginning

[42] In line with the Hong Kong MC6 decision on DF-QF market access for LDC goods, the language of such a resolution could be couched along the following lines: 'developed country members and developing country members in a position to do so will extend preferential market access for graduated LDCs for 'x' years from the date of their graduation.'

from 2028 as is envisaged for the LDCs). This would particularly benefit graduating LDCs more dependent on import tariffs.

The enhancement of preferential market access and deepening of trade cooperation within Southern RTAs will help graduating countries enhance exports by raising their competitive strengths. Such support will also allow these countries to expand exports to developed Northern markets by leveraging cooperation with Southern partners.

Three of the graduating LDCs are in the process of WTO accession. They will need to negotiate various provisions (commitments and obligations) as part of their accession process.[43] Southern WTO members may also choose to demonstrate a flexible approach in negotiations with acceding graduating LDCs.

### 3.3 Steer SSC to support the structural transformation of graduating LDCs

While achieving commendable success in certain areas, graduating LDCs continue to suffer from formidable structural weaknesses in the form of weak industrialisation, low productivity and a lack of economic diversification. In view of the challenges of the post-graduation trading scenario, they will need to significantly raise their supply-side capacities, labour and capital productivity, and competitive strength to be able to compete in regional and global markets. SSC could be an important tool for expanding these countries' capacities in each of these areas. Exports to regional and other Southern markets tend to be more sophisticated than to developed markets, providing greater scope for growth and structural transformation (UNCTAD, 2016). Many graduating LDCs are pursuing various initiatives that are critically important to strengthening the comparative trade-related advantages of graduating LDCs, and will help these countries to translate those comparative advantages into competitive strengths. In South Asia, the Bangladesh-Bhutan-India-Nepal Motor Vehicle Agreement (BBIN-MVA) is a pertinent example that could play a highly positive role in enhancing the three graduating LDCs' intra-regional and sub-regional trade.

Flows of primary commodities continue to be an important segment of South-South trade.

In South-East Asia, Greater Mekong Subregional (GMS) cooperation is another relevant example. The SASEC connectivity, Belt and Road Initiative (BRI) and associated corridors could also prove important for creating new trade-related opportunities for graduating LDCs, in reducing lead times for goods exports, in the export of (transport-related) services, in attracting investment and by way of establishing production networks and value chains. It is critically important to steer this in a way that promotes the diversification of graduating LDC export portfolios. Flows of primary commodities continue to be an important segment of South-South trade. However, competitive advantages built on value-adding investment in backward and forward connections are critically important for sustainable graduation. The successful triangulation of trade, transport and investment is therefore crucial. Greater flows of finished goods will be needed to make South-South cooperation work for both the structural transformation of graduating LDC economies and their export and market diversification. These initiatives should help create the supply-side capacities necessary for structural transformation, competitivity and export and market diversification, which are of crucial importance for sustainable graduation. Terms of credit (interest rates, maturity periods, grace periods) and various investment agreement provisions (domestic sourcing requirements and technology transfer provisions, local employment ratio etc.) can be arranged to service the priorities and needs of graduating LDCs. Such support will not only foster regional integration, it will also help graduating LDCs by ensuring global integration from a position of strength.

[43] The Chinese scheme for the acceding LDCs could serve as a good example for other advanced developing countries.

As part of the graduation process UNCTAD is asked to perform a vulnerability audit of graduating LDCs to support their smooth graduation and graduation with momentum. Following graduation, monitoring is undertaken to assess the implementation of a smooth transition strategy designed by graduating LDCs themselves. Various UN and other international organisation resolutions/decisions talk of extending the necessary support to graduating LDCs. Relevant Southern players could design support measures as part of the South's contribution. Opportunities to leverage SSC and perform triangular cooperation need to be actively explored to strengthen this. These could be an important way to scale up successful policies, share best practices, encourage knowledge flows and knowledge sharing, incentivise knowledge transfer and enhance the transformative changes needed by graduating LDC economies. Many platforms are geared to support the LDCs, through various forms of SSC. This study suggests that, in view of the large number of LDCs graduating in the next few years, the support granted to LDCs should be extended to graduating LDCs on a defined scale and scope, and for a predictable period following graduation.

## 3.4 The pandemic as a trigger to support graduating LDCs

The pandemic has important implications on three fronts: (a) sustainable graduation; (b) South-South economic cooperation and (c) making South-South cooperation work for sustainable graduation.

All projections indicate that Covid-19 will have severe implications that will accentuate the vulnerabilities afflicting developing countries in general, and graduating LDCs in particular. For graduating LDCs, this will not only be felt in terms of the three graduation criteria as these countries move towards their respective deadlines for leaving the group, but also in the negative impact on their sustainable graduation (Bhattacharya and Islam, 2020).

The pandemic is already producing reduced income levels, accentuated human hardships and increased economic vulnerabilities.[44] Global growth projections have been revised downward and investment flows are also projected to be low.[45] The developed countries (key markets for a number of graduating LDCs,) have already entered into a recession with adverse implications for exports from graduating LDCs. By all estimates, economic recovery will be a tortuous journey and the pandemic will leave a negative footprint on the long-term prospects of economic growth in low-income countries and graduating LDCs. The need for deeper SSC to help graduating LDCs in their post-COVID recovery and sustainable graduation, has assumed renewed urgency. As LDCs are also important markets for Southern developing countries, such support has a strong economic motive.

As the WTO reports, many countries, including Global South nations, have resorted to protectionist measures to safeguard their trade interests. Export and import restrictions are both at play. Health and food related restrictions feature prominently among the 59 restrictive trade measures. Southern G20 members (half the number),[46] should provide

[44] For example, 2020 growth projections for Bangladesh have been significantly downgraded; various estimates also note that the percentage of people living below the poverty line has increased from 20 percent pre-COVID to 35 to 45 percent (CPD, 2020). Private investment and credit takeoff have also come down, inequalities (income, consumption and assets) have gone up. Additional money has to be spent on health emergencies. All this will make sustainable graduation more challenging. This narrative is a common across all the graduating LDCs.

[45] In contrast to the January 2020 forecast of +3 percent of global GDP growth, the IMF revised the April 2020 figures significantly downward to -3 percent (IMF, 2020). The World Bank projects a 5.2 percent contraction in global GDP in 2020. UNCTAD (UNCTAD, 2020) estimates that investment flows will come down by 40 percent in 2020 according to the WTO (2020a), and world trade is expected to fall by between 13 percent and 32 percent in 2020.

[46] The ten Southern G20 members are Argentina, Brazil, China, India, Indonesia, Republic of Korea, Mexico, Saudi Arabia, South Africa and Turkey.

pandemic recovery leadership. They should demonstrate that they are committed to protecting the trade-interests of low-income and graduating LDCs, and will not pursue restrictive and protectionist trade measures that harm these countries.

The extension of the WTO TRIPS waiver for LDC pharmaceutical sectors, (which allows flexibility concerning patenting and licensing requirements and compliance enforcement,) is of particular interest to graduating LDCs. These are to be effective until the end of December 2032. However, graduating LDCs will cease to benefit from this waiver as soon as graduation becomes effective. This waiver has allowed Southern LDCs and developing countries to import cheap drugs from graduating LDCs such as Bangladesh. There is a move to allow graduating LDCs to continue enjoying the benefits of this waiver until the end of the waiver period, even if an LDC graduates earlier.[47] In view of the current importance of medicine and the particular importance of the pharmaceutical sector, the need for serious, positive consideration of this proposal (which is currently being discussed in Geneva,) cannot be overemphasised. Southern G20 members should give it their fullest support.

### 3.5 Design an institutional framework to structure SSC to support graduating LDCs

While the LDCs are specifically classed as a group in connection with the work of various global and Southern platforms, there is no formal recognition for graduating LDCs as a separate category, for example in the context of the WTO. A WTO proposal to recognise SID graduating LDCs as a separate category (with a view to designing a set of targeted measures for their sustainable graduation), did not gain enough support. However there is a widespread recognition that graduating LDCs need special and targeted support, as testified by successive UN resolutions, decadal LDC support programmes, BAPA+40 resolutions, Agenda 2030 work plans, and the work of UN bodies including UNESCAP, UNCTAD, UNCDF and UNOSSC.

The LDC graduation procedure stipulates that UN-DESA propose an ex-ante impact assessment and UNCTAD prepare a vulnerability profile for the CDP after an LDC is first found eligible for graduation. The LDC concerned is also expected to prepare its own smooth transition strategy,[48] which is to be monitored for three years after graduation. The global community is expected to take targeted measures to help the graduating LDC address specific difficulties that impede its sustainable graduation. The CDP has promoted the adoption of smooth transition measures and improved assistance for graduated and graduating LDCs. EIF, the Technology Bank for LDCs, the Investment Support Programme for LDCs and UNCDF have smooth transition provisions that allow them to continue to support LDCs for a certain period of time after graduation. The UN Inter-Agency Task Force on LDC Graduation[49] is responsible for coordinating UN agencies and other international and regional organisations to jointly help graduating and graduated LDCs achieve a smooth transition.

Given the large number of LDCs slated for graduation, and considering that several other LDCs will be eligible for graduation over the next decade, there is an urgent need to gear up work to support graduating and graduated LDCs. In the context of deepening SSC, much more will need to be done. Developing countries can take the lead. Their cooperation could cover the implementation of trade-focused RTAs, BFTAs and CEPA cooperation initiatives, regional and bilateral investment agreements and multi-modal

[47] Bangladesh has already made a submission to this effect, proposing that all LDCs continue to benefit from the TRIPS waiver decision until the current end-period, irrespective of whether they will graduate earlier.
[48] The graduating LDC is expected to constitute a Graduation Task Force to identify bottlenecks and constraints and to help create strategies for sustainable graduation.
[49] Chaired by the Director of the OHRLLS.

connectivity agreements. These could extend preferential treatment, enhance market access, establish a two-tier liberalisation plan, and ensure more than reciprocal treatment in various provisions, etc. A dedicated body is needed to identify concrete measures and initiatives and proactively pursue their implementation.

This study therefore proposes that UNOSSC establish a task force to examine various SSC initiatives to safeguard the interests of the graduating and graduated LDCs. This is due to the need to design a package of support, as part of SSC, for sustainable LDC graduation. The Task Force will be responsible for auditing various initiatives in trade, investment, connectivity, technology and other areas to best serve the interests of graduating and graduated LDCs.

This task force would work closely with UNOHRLLS and the UN Inter Agency Task Force on LDC graduation. Its specific responsibility will be to examine the various SSC trade and non-trade initiatives involving graduating and recently graduated LDCs. They will identify measures to help implement smooth graduation and sustainable graduation strategies. The Task Force could encourage Southern partners to help address these countries' concerns, both within SSC and in view of triangulation, and to mobilise Southern support to help implement smooth graduating LDC transition strategies. Such targeted efforts will also help address requests to defer LDC graduation, which are likely to increase given the pandemic.

While the adverse implications of the pandemic are being felt across all Southern economies, there are strong reasons and evidence to show that strategically designed and effective SSC could catalyse Southern economies towards sustainable and resilient recovery. All Southern countries stand to gain from this approach.

LDCs start their post-graduation journey with a number of embedded structural weaknesses. These are likely to be exacerbated by the loss of many trade-related preferences on graduation and also because of the pandemic. International flows, particularly in the form of concessional finance, FDI and remittances could allow graduating LDCs to build their supply-side capacities and competitive edge, which would enable them to deal with the adverse effects of graduation including those originating in the erosion of market access preferences. Financial flows, in conjunction with trade-related initiatives could be an important sustainable graduation enabler. Sections 4, 5 and 6 deal address pertinent issues in this respect.

# 3. PART B: Southern Financial Support for Graduating LDCs – Status and Opportunities

A total of 12 countries are set to graduate from the LDC Group over the next decade, so long as the COVID-19 pandemic does not have too debilitating an impact.

Due to their structural weaknesses, LDC economies are dependent (to varying degrees) on external financial flows. However, there are hardly any dedicated preferential financial arrangements for this group of countries at global level. These countries' simultaneous transition from the LIC to LMIC group also restricts their access to concessional finance. In this context, the following sections (4, 5, 6 and 7) examine the dimensions and composition of graduating LDCs' dependence on external finance (essentially public development finance). It further explores the opportunities for Southern providers to support these LDCs as they tackle strategies for smooth and sustainable graduation. Finally, this study reviews graduating LDCs' experience of Southern financial assistance from the South during the pandemic. It seeks to address one of the knowledge deficits concerning LDC and graduating LDC status and their opportunities to access Southern financial assistance.

## Section 4. Graduating LDCs' External Financial Dependence

Of the 12 graduating LDCs, two are in Africa (Angola and São Tomé and Príncipe), six are in Asia (Bangladesh, Bhutan, Lao People's Democratic Republic, Myanmar and Nepal) and four in the South Pacific (Kiribati, Solomon Islands, Tuvalu and Vanuatu). As Table 4.1 shows, in 2018 the LDC group commanded only 1.3 percent GDP, of which the 12 graduating LDCs held 47.3 percent. They represented around one percent of global merchandise and exports, of which 54.3 percent belonged to the graduating LDCs. Further, less than 1.8 percent of global FDI and little over 6 percent of global remittances were held by all the LDCs, of which respectively 12.7 percent and 57.6 percent were commanded by the graduating LDCs.

While the LDC group receives almost 30 percent of official development assistance (ODA), the 12 graduating members account for 21.5 percent of that. Curiously, the share of funds flowing to LDCs from private (international) philanthropy is comparatively lower (less than 12 percent), and these flows are even less directed at graduating LDCs (only 11 percent of the group total). Private (international) philanthropy comes in the form of a grant and plays a significant role in certain sectors (e.g. health).

*Profile and Vulnerabilities.*

Incidentally, graduating LDCs' weight in the global economy is greatly influenced by the two relatively large graduating LDCs: Angola and Bangladesh. These two countries account for almost 50 percent and in some cases more of the graduating LDCs share of the different economic indicators (see the third column of Table 4.1).

However, data on Southern shares of these funds, particularly ODA, is not readily available from existing international datasets. This paper proposes certain measures in this regard.

**Table 4.1:** *LDC and Graduating LDC Shares in 2017-2018*

| Indicator | All LDCs (percentage of world total) | 12 Graduating LDCS (percentage of all LDCs) | 10 Graduating LDCs, excl. Bangladesh and Angola (percentage of all LDCs) |
|---|---|---|---|
| **Population** | 13.5 | 28.2 | 9.1 |
| **GDP** | 1.3 | 47.3 | 11.6 |
| **Goods exports** | 1.0 | 54.3 | 12.5 |
| **FDI** | 1.8 | 12.7 | 21.6 |
| **Remittances** | 6.0 | 57.6 | 21.4 |
| **Gross ODA commitments** | 29.8 | 21.5 | 10.6 |
| **Gross ODA disbursements** | 27.4 | 17.8 | 8.5 |
| **Private philanthropy** | 11.7 | 11.0 | 4.0 |
| **Private finance mobilised by ODA (annual average over 2012–2017)** | 6.0 | 34.0 | 13.5 |

Source: Based on UNCTADSTAT, OECDSTAT, IMF, WDI (2019).

An assessment of graduating LDCs' financial needs shows that 12 of these countries have a geographical handicap.[50] Six are SIDS (Kiribati, São Tomé and Príncipe, Solomon Islands, Timor-Leste, Tuvalu and Vanuatu) and three are LLDCs (Bhutan, Nepal and Lao People's Democratic Republic). All graduating LDCs are also vulnerable to climate change (CDP 2018). Additionally, five countries: Kiribati, Myanmar, Solomon Islands, Timor-Leste and Tuvalu are defined as fragile states in the World Bank's Harmonised List of Fragile Situations (World Bank, 2018). It is important to remember that the nine graduating LDCs other than Bangladesh, Myanmar and Nepal, have not met EVI criteria.[51] There is growing concern about whether their forthcoming transition out of the LDC group will be "smooth and sustainable."

LDC graduation is also going to be a double transition, as 11 of the 12 graduating countries (except Nepal) have lost their low-income status in recent years. Ten countries have entered the LMICs group, while Tuvalu moved up to UMICs. Becoming an LMIC implies improved creditworthiness as the country graduates from International Development Association (IDA) only status to IDA or the International Bank for Reconstruction and Development (IBRD) blend, and eventually IBRD only status (World Bank, 2012). However, this also suggests that loan concessions will be more restricted for transitioning countries. Graduating from the LDC group will close concessional financing windows.

The graduating LDCs are significantly dependent on external (public and private) financial resources to sustain their investment and development activities. Estimates of these countries' financial requirements for implementing SDGs also indicate the important role attributed to external public development finance (UN, 2014). This is particularly true for financing sustainable infrastructure, which is crucial for achieving Agenda 2030 (UNCTAD, 2018; UNDP, 2020). Financial resources have played a key role in the development of LDC economies, particularly in areas associated with graduation: enhancing export competitiveness (through aid and credit for infrastructure development, and supply side capacity-building), reducing economic vulnerabilities (through aid and concessional credit to increase resilience, raise competitive strengths and diversify the production base). Remittances are important for raising per capita GNI and savings and household

[50] 17 of the 47 LDCs are LLDCs, while nine are SIDS. An overwhelming number of LDCs are also suffering the negative consequences of climate change. Over half of the LDCs are either in conflict or post-conflict countries.

[51] EVI is based on indicators of: (a) population size; (b) remoteness; (c) merchandise export concentration; (d) share of agriculture, forestry and fisheries; (e) share of population in low elevated coastal zones; (f) instability of exports of goods and services; (g) victims of natural disasters; and (h) instability of agricultural production (UN-OHRLLS, n.d.).

incomes (which in turn contributes to meeting the LDC graduation criteria). Studies also show a remarkable correspondence between LDC delivery of the SDGs and smooth graduation (Khatun et al., 2018).

Graduating LDCs' financial needs are underpinned by the structural weaknesses of their macroeconomic balances, namely their savings-investment gap, fiscal deficit and balance of payments (BoP) shortfall. The following paragraphs discuss these three dimensions.

According to Table 4.2, the average graduating LDC savings-investment gap as a share of GDP has shown an increasingly negative trend over the last decade. This indicator peaked in 2008-09, after the global economic and financial crisis, and is yet to stabilise fully. In fact, the savings-investment gap has worsened during the last couple of years (2017 and 2018), reaching (-)7 percent of GDP.

Table 4.3 reveals that the savings-investment gap is usually much higher among graduating SIDS than non-SIDS, although Bhutan has the highest saving-investment gap (18.4 percent, 2018).[52] The only graduating LDC with a national savings surplus is oil-exporting Angola.[53] In the face of modest national savings rates, SIDS' relatively higher investment rate is sustained by foreign aid.

The way in which these countries' savings gap is financed in future will have important implications for their debt (UNCTAD, 2016). For instance, much of Bhutan's public and private debt is in Indian Rupees (INR) (ADB, 2015. As the INR has depreciated against the United States Dollar (USD), borrowing is likely to become more expensive for Bhutan.

**Table 4.2:** *The Average Savings–Investment Gap of Graduating LDCs (% of GDP)*

| Country | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **All LDCs** | -5.2 | -6.1 | -5.8 | -6.4 | -7.1 | -8.0 | -6.4 | -6.5 | -6.3 | -5.5 | -6.0 |
| **Graduating LDCs (12 countries)** | -5.1 | -6.9 | -10.4 | -9.5 | -5.1 | -5.5 | -7.3 | -5.5 | -5.4 | -7.0 | -7.0 |
| **Graduating SIDS** | -17.9 | -23.9 | -27.8 | -18.0 | -10.2 | -9.0 | -13.0 | -7.6 | -5.3 | -9.0 | -8.1 |
| **Graduating Non-SIDS** | 0.0 | -0.1 | -3.4 | -6.0 | -3.1 | -4.1 | -5.0 | -4.6 | -5.4 | -6.2 | -6.5 |

Source: Based on IMF (2019).

As private investment in LDCs is constrained by a number of factors including market distortion, political instability, flawed institutions and governance, there is inevitably high reliance on external grants or ODA (UNDP and AFD, 2016). As is to be expected, ODA flows also help mobilise domestic resources when these are targeted towards strengthening the capacity of domestic institutions to broaden tax base, digitise the revenue collection system and develop the concerned human resources. Moreover, given the macroeconomic imbalances afflicting graduating LDC economies, a substantive fall in external finance may act as a shock on their economy, destabilising achievements. Graduating LDCs' macroeconomic imbalances need foreign finance as shown in their fiscal deficit and BoP shortfall. Sources of such financial inflows include bilateral Southern providers, as well as newly established financial institutions under the aegis of Southern counties.

Given low effective revenue mobilisation and the growing demand for development finance, LDC governments systematically suffered a fiscal deficit. This had to be addressed by foreign grants and domestic and external borrowing (UN LDC IV & UNOHRLLS, 2010). Table 4.3 reveals that from 2008–2018, LDCs as a group suffered from a -4.1 to -1.7 percent fiscal deficit (net government borrowing as a percentage of GDP) Graduating LDCs also generally experienced a negative fiscal balance (and actually had a higher deficit/borrowing in some years).

[52] Indian bilateral investment, which totaled $50.12 million between 2007 and 2019 (Taneja, et al. 2019), is the driving factor behind this substantial gap.

[53] Angola's FDI has been volatile and is mostly concentrated on the mineral sectors (UNCTAD, 2019). Even with more lenient investment terms, Angola is failing to lure back international investors (The Economist, 2019).

**Table 4.3:** *Graduating LDCs' Average Fiscal Deficit (Government Net Borrowing) (% of GDP)*

| Country | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **All LDCs** | -2.4 | -4.1 | -3.2 | -2.9 | -2.5 | -1.7 | -2.7 | -3.1 | -3.4 | -2.8 | -2.1 |
| **All Graduating LDCs** | -3.0 | -5.3 | -4.1 | -3.6 | -1.6 | 2.7 | 0.4 | 1.6 | -1.3 | -2.3 | -0.5 |
| **Graduating SIDS** | -4.0 | -7.5 | -7.4 | -6.5 | -2.1 | 7.3 | 2.1 | 5.3 | 0.0 | -0.5 | 2.0 |
| **Graduating Non-SIDS** | -2.1 | -3.0 | -0.8 | -0.7 | -1.1 | -2.0 | -1.3 | -2.2 | -2.7 | -4.0 | -3.0 |

Source: Based on IMF (2019).

Consideration of SIDS' and non-SIDS' average fiscal deficit figures reveals intriguing differences. Over a recent 10-year period (2008–2017), non-SIDS graduating LDCs continuously faced budget deficits, unlike their SIDS counterparts. Country-specific data reveals that SIDS experienced highly volatile revenues, which questions the robustness of this data.

Improving effective revenue mobilisation will be of primary importance to avert fiscal shock. Moreover, prudent financing has to be devised to underwrite the fiscal deficit and to avoid debt stress. Efficient use of foreign grants and concessional loans could be an essential element for this approach.

Goods exports as a share of imports declined between 2000 and 2015 for all LDCs, before starting to improve slowly. In 2015, LDCs suffered an approximately 25 percent contraction in goods exports due to drops in the price of and demand for fuels and mining products (WTO, 2016). As shown in Table 4.4, LDCs were able to cover around 70 percent of their imports by goods exports in 2018. Small island LDCs were only able to back up about 58 percent of their imports through exports. Angola, Bangladesh and Myanmar sustained their positions in the top five LDC goods traders' list from 2008 to 2018 (WTO, 2019).

The LDC group current account has been negative (as a percentage of GDP) since 2008, albeit recovering since 2014 (UNCTADSTAT, 2019). Graduating LDCs (except Angola) posted a deficit in 2018, and a declining balance since 2014 (IMF 2019). Table 4.2 shows that graduating SIDS' current account balance is marginally positive, whereas their non-SIDS counterparts have a negative balance. The graduating LDCs BoP has worsened since 2015. Similarly, graduating non-SIDS have a higher BoP shortfall (around -9.9 percent of GDP) than SIDS (about 2 percent).[54]

**Table 4.4:** *Graduating LDC Current Accounts and Balance of Payments*

| Country | Exports of Goods and Services (% of GDP) 2018-Average | Merchandise Exports (% of Imports) 2018-Average | Current Account (% of GDP) 2017-Average | Balance of Payments (% of GDP) 2017-Median |
|---|---|---|---|---|
| **All LDCS** | 19.69 | 70.63 | -4.52 | – |
| **Graduating LDCs** | 32.72 | 57.70 | -3.11 | -4.60 |
| **Graduating SIDS** | 42.83 | 22.26 | 0.69 | 1.80 |
| **Graduating non-SIDS** | 22.61 | 93.13 | -6.92 | -9.90 |

Source: Based on UNCTADSTAT, IMF (2019).

Graduating LDC cohorts have a weak external balance, particularly in their current account and BoP (Kharas et al., 2019). Given the volatility of observations and noting the quality of graduating LDC SIDS data, one needs to interpret their current account and BoP situation cautiously.

[54] The BoP figure used is the median instead of the average due to data constraints.

Graduating LDCs are approaching an important milestone in their developmental journey with a number of existing vulnerabilities. These vulnerabilities range from irreversible geographical disadvantages to entrenched macroeconomic imbalances. The situation is further aggravated by major financial institutions' policy decisions on the eligibility criteria for concessional finance. The impact of COVID-19 has made these countries' economic and social situation even more precarious. It has therefore become important for this group to explore (traditional and non-traditional) sources and methods of accessing development finance. One potential and relatively unexplored source is emerging Southern providers and institutions. The following sections are devoted to this theme.

## Section 5. Financial Flows from Southern Providers to Graduating LDCs

Having established (general) LDC and (particular) graduating LDC dependence on external financial grants, this section seeks to explore the dimensions of such flows from the South. It takes note of the difference between SIDS and non-SIDS graduating LDCs. The targets of these financial flows relate to critically important areas of improvement in lives and livelihoods, food and nutrition, as well as social indicators. Directly or indirectly, these have contributed to improving all three LDC graduation criteria and also helped LDCs and graduating LDCs mitigate the challenges of Covid-19. However, the analysis presented suffers from a significant lack of data.

In addition to bilateral Southern ODA, this section also investigates financial flows to graduating LDCs from Southern multilateral institutions. It concludes with a review of two forms of private finance, namely remittances and Southern FDI.

### 5.1 Bilateral Southern flows

There are no systematic global records of South-to-South ODA. The scrutiny of national data is inhibited by definition and other problems. This study therefore relies on OECD.Stat (Development theme) and information from Non-DAC providers reporting to it.

**Table 5.1:** *ODA to all LDCs and Graduating LDCs at Current Prices (in $ million) and Shares (2010-2018)*

| Year | | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Total ODA to all LDCs** | 47 LDCs Total | 43,599.77 | 44,541.61 | 43,109.6 | 47,904.05 | 43,948.58 | 43,434.26 | 43,536.97 | 48,954.81 | 53,809.67 |
| **Total ODA to graduating LDCs** | 12 LDCs Total | 3,991.36 (9.15) | 4,122.09 (9.25) | 5,076.75 (11.78) | 9,074.78 (18.94) | 6,238.18 (14.19) | 6,686.71 (15.40) | 6,451.85 (14.82) | 8,110.07 (16.57) | 7,695.89 (14.30) |
| **Total ODA from non-DAC providers to all LDCs** | 47 LDCs Total | 432.27 (0.99) | 521.99 (1.17) | 700.61 (1.63) | 617.36 (1.29) | 579.9 (1.32) | 2,289.82 (5.27) | 2,215.29 (5.09) | 2,029.5 (4.15) | 5,948.87 (11.06) |
| **Total ODA from non-DAC providers to graduating LDCs** | 12 LDCs Total | -6.42 (-0.01) | 17.35 (0.04) | 6.53 (0.02) | 32.77 (0.07) | 53.33 (0.12) | 99.14 (0.23) | 164.47 (0.38) | 107.99 (0.22) | -1,022.34 (-1.90) |

Source: OECDstat, 2020; Access date: 07.09.20.

Note: Brackets show the respective ODA flow as a share of the total ODA flow to all LDCs in percentage.

Currently, only 20 Non-DAC countries and economies share their ODA figures with OECD[55]. This list does not include large Southern providers like China, Brazil, India and South Africa, so the numbers reported in Tables 5.1, 5.2 and 5.3 are significantly low.

Table 5.1 shows that the total (global) amount of ODA flowing annually to all 47 LDCs increased from $43.6 billion in 2010 to $53.8 billion in 2018. The share attributable to graduating LDCs increased from 9.15 percent to 14.30 percent during this period.

[55] Azerbaijan, Bulgaria, Croatia, Cyprus, Estonia, Israel, Kazakhstan, Kuwait, Latvia, Liechtenstein, Lithuania, Malta, Romania, Russia, Saudi Arabia, Chinese Taipei, Thailand, Timor-Leste, Turkey, and United Arab Emirates.

Between 2010 and 2018, flows from reporting Non-DAC providers to all 47 LDCs increased from under $0.5 billion to almost $6 billion. However, this was not reflected in flows to graduating LDCs. Their share of reporting non-DAC contributions remained negative in most years, implying that outflows exceeded inflows. This suggests that the non-DAC providers concerned did not see graduating LDCs as priority ODA destinations.

Table 5.2 presents national breakdowns of non-DAC flows to non-SIDS graduating LDCs. Based on data from six countries (five of which are Asian), this table reveals that, although the initial and final years of the 2010- 2018 period had a negative balance, graduating LDCs received more funds from reporting non-DAC providers than they paid out in other years. A national analysis reveals that (other than Bangladesh and to a lesser extent, Myanmar), graduating non-SIDS LDCs (Angola, Bhutan, Laos and Nepal) enjoyed a positive annual balance from non-DAC providers. One wonders whether this is a supply or demand phenomenon.

A country-specific look at graduating SIDS LDCs reveals a similar trend, although the sub-group balance is much less than their non-SIDS counterparts. The figures on six SIDS (only one in Africa and the rest in the Pacific) reported in Table 5.3 show that apart from the initial years of the reported period (when the Solomon Islands experienced a negative balance,) all of the other countries (Timor Leste, Kiribati, Tuvalu, Vanuatu, and São Tomé and Príncipe) had more non-DAC provider inflows than outflows.

Both aggregate and disaggregated scrutiny of the available data suggests that the overall growth in ODA to LDCs over the last decade was not mirrored by enhanced flows to graduating LDCs from reporting non-DAC providers. This is largely true for both SIDS and non-SIDS graduating LDCs. This suggests that LDCs do not figure prominently in these Southern providers' aid policies. This conclusion can be validated by including the major Southern providers in the dataset and by examining the development cooperation policies of reporting non-DAC providers.

**Table 5.2:** *ODA to Non-SIDS Graduating LDCs From Non-DAC providers at Current Prices (in $ million) and Shares (2010-2018)*

| | Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|
| **ODA from non-DAC to non-SIDS** | **Angola** | 0.09 | 0.25 | 0.93 | 0.16 | 0.22 | 0.36 | 5.46 | 0.16 | 0.66 |
| | | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.01) | (0.00) | (0.00) |
| | **Bangladesh** | -3.14 | -3.56 | -7.53 | -4.88 | -7.84 | 21.93 | 85.28 | 48.81 | -1,060.38 |
| | | (-0.01) | (-0.01) | (-0.02) | (-0.01) | (-0.02) | (0.05) | (0.20) | (0.10) | (-1.97) |
| | **Bhutan** | 0.72 | 0.41 | 1.04 | 1.36 | 0.96 | 0.95 | 1.1 | 1.65 | 0.01 |
| | | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) |
| | **Lao People's Democratic Republic** | 22.09 | 17.5 | 14.1 | 34.96 | 56.38 | 43.27 | 45.77 | 40.37 | 26.85 |
| | | (0.05) | (0.04) | (0.03) | (0.07) | (0.13) | (0.10) | (0.11) | (0.08) | (0.05) |
| | **Myanmar** | -27.71 | -0.72 | -2.78 | 0.8 | -1.05 | 7.27 | 12.8 | 12.37 | 5.16 |
| | | (-0.06) | (0.00) | (-0.01) | (0.00) | (0.00) | (0.02) | (0.03) | (0.03) | (0.01) |
| | **Nepal** | 1.35 | 0.42 | 0.85 | 0.39 | 0.52 | 9.54 | 3.46 | 3.74 | 4.79 |
| | | (0.00) | (0.00) | (0.00) | (0.00) | (0.00) | (0.02) | (0.00) | (0.00) | (0.00) |
| | **Total Non-SIDS** | -6.6 | 14.3 | 6.61 | 32.79 | 49.19 | 83.32 | 153.87 | 107.1 | -1,022.91 |
| | | (-0.02) | (0.03) | (0.02) | (0.07) | (0.11) | (0.19) | (0.35) | (0.22) | (-1.90) |

Source: OECD.Stat, 2020; Access date: 07.09.20.
Notes: Brackets show the respective ODA flow as a percentage of the total ODA flow to all LDCs..
0.00 indicates insignificant figures.

**Table 5.3:** *ODA to SIDS Graduating LDCs From Non-DAC Providers at Current Prices (in $ million) and Shares (2010-2018)*

| | Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Kiribati** | 0.11 | .. | .. | .. | 0.98 | 3.46 | 8.59 | 0.24 | 0.00 |
| | | (0.03) | .. | .. | .. | (0.17) | (0.15) | (0.39) | (0.01) | (0.00) |
| | **São Tomé and Príncipe** | .. | .. | 0.04 | .. | 0.24 | 0.01 | 0.05 | 0.06 | 0.25 |
| | | .. | .. | (0.01) | .. | (0.04) | (0.00) | (0.00) | (0.00) | (0.00) |
| | **Solomon Islands** | -0.42 | -0.43 | -0.4 | -0.35 | -0.41 | 3.42 | 0.47 | 0.03 | 0.02 |
| | | (-0.10) | (-0.08) | (-0.06) | (-0.06) | (-0.07) | (0.15) | (0.02) | (0.00) | (0.00) |
| **ODA from non-DAC to SIDS** | **Timor-Leste** | 0.49 | 0.28 | 0.23 | 0.08 | 0.28 | 0.23 | 0.06 | 0.16 | 0.01 |
| | | (0.11) | (0.05) | (0.03) | (0.01) | (0.05) | (0.01) | (0.00) | (0.01) | (0.00) |
| | **Tuvalu** | .. | 3.15 | 0.02 | 0.09 | 1.91 | 2.23 | 0.46 | 0.01 | 0.02 |
| | | | (0.60) | (0.00) | (0.01) | (0.33) | (0.10) | (0.02) | (0.00) | (0.00) |
| | **Vanuatu** | .. | 0.05 | 0.03 | 0.16 | 1.14 | 6.47 | 0.97 | 0.39 | 0.27 |
| | | | (0.01) | (0.00) | (0.03) | (0.20) | (0.28) | (0.04) | (0.02) | (0.00) |
| | **Total SIDS** | 0.18 | 3.05 | -0.08 | -0.02 | 4.14 | 15.82 | 10.6 | 0.89 | 0.57 |
| | | (0.04) | (0.58) | (-0.01) | (0.00) | (0.71) | (0.69) | (0.48) | (0.04) | (0.01) |

Source: OECD.Stat, 2020; Access date: 07.09.20.

Notes:
- Brackets show the respective ODA flow as a percentage of the total ODA flow to all LDCs.
- 0.00 indicates insignificant figures.
- .. indicates data unavailable.

## 5.2 Southern multilateral providers

Recently, multilateral financial institutions set up by Southern countries started to play a growing role in supplying development finance. The most prominent of these is the Asian Infrastructure Investment Bank (AIIB), a multilateral development bank founded to improve social and economic outcomes in Asia. Headquartered in Beijing, AIIB began operating in January 2016 and now has 103 approved members worldwide.

**Table 5.4:** *AIIB Flows to LDCs (2019)*

| Announcement Date | $ Million | Criteria | Country |
|---|---|---|---|
| **AIIB to graduating LDCs (2019)** | | | |
| **20-Dec-19** | 112.3 | Sovereign Loan | Nepal |
| **12-Jul-19** | 100 | Loan | Bangladesh |
| **10-Jun-19** | 90 | Loan | Nepal |
| **4-Apr-19** | 40 | Loan | Lao PDR |
| **28-Mar-19** | 120 | Loan | Bangladesh |
| **Total** | 462.3 | | |
| **AIIB to all LDCs except graduating LDCs (2019)** | | | |
| **12-Jul-19** | 75 | Investment | Cambodia |
| **AIIB Grand Total** | **537.3** | | |

Source: AIIB website, 2019.

Since its establishment, AIIB has supported LDCs in general and graduating LDCs in particular. Its Board of Directors approved the first loans amounting to $165 million in June 2016, for an energy sector project in a graduating LDC: Bangladesh. Table 5.4 presents information on AIIB finance for graduating LDCs in 2017. The total amount of six LDC loans amounted to just over $537 million, of which five loans totalling $462 million (86 percent) went to graduating LDCs. The recipients were Bangladesh (two projects), Nepal and Lao PDR. The table further shows that the only non-graduating LDC was Cambodia.

At the fourth BRICS Summit in New Delhi (2012), the leaders of Brazil, Russia, India, China and South Africa considered setting up a new development bank to mobilize resources for infrastructure and sustainable development projects in BRICS, other emerging economies, and developing countries. In February 2016, the New Development Bank (NDB) came into operation, headquartered in Shanghai. The NDB became fully operational on 27 February 2016 with the signature of the Headquarters Agreement (with the government of the People's Republic of China) and the Memorandum of Understanding with the Shanghai Municipal People's Government. To date, NDB has limited its operations to BRICS; LDCs are yet to receive any funds from this entity.

This study also examined other Southern financial institutions such as the Islamic Development Bank (IsDB). However, as Table 5.5 reveals, while IsDB approved 11 loans to eight LDCs worth about $400 million in 2019, none of these recipients were graduating LDCs.

**Table 5.5:** *IsDB Flow to All LDCs (2019)*

| Announcement Date | In $ million | Criteria | Country |
|---|---|---|---|
| **13-Sep-19** | 69.1 | Social Housing Project | Benin |
| **15-Jul-19** | 17.4 | Food security and agriculture project | Burkina Faso |
| **15-Jul-19** | 99.7 | Sustainable electricity | Mozambique |
| **15-Jul-19** | 6 | Construction of 9-storey commercial buildings | Benin |
| **19-May-19** | 64.8 | Health and communication projects | Djibouti |
| **18-Jan-19** | 15.26 | Rice value chain project | Niger |
| **16-Jan-19** | 16.25 | Rice value chain project | Guinea |
| **14-Jan-19** | 0.27 | Technical assistance | Senegal |
| **14-Jan-19** | 32.62 | Rice value chain project | Senegal |
| **14-Jan-19** | 20.1 | Innovative rural road construction | Senegal |
| **14-Jan-19** | 60 | National Program for Islamic Microfinance | Senegal |
| **Total (in 2019)** | **401.5** | | |

Source: IsDB website; (Accessed on September 7, 2020).

However, if we review the 2015 IsDB loan portfolio, the bank granted loans totalling almost $1.5 billion to LDCs, of which 15 percent went to (graduating LDC) Bangladesh, for two projects.

A similar 2010 review shows that IsDB dished out $766.65 million to LDCs, of which about 20 percent went to graduating LDCs. The three projects supported in (graduating LDCs) Bangladesh (two projects) and Nepal (one project) included physical infrastructure and social projects.

These three reviews at three points in time show that the share of graduating LDCs in the IsDB portfolio has fallen. Although unlike the AIIB, its portfolio often covered African LDCs. (Graduating) LDCs' relatively modest presence in the loan portfolio may also be due to an absence of bankable project proposals. Although Southern financial institutions are making inroads in LDCs, they are yet to emerge as a major source of finance. However, their aggregate role is no less pronounced than that of Southern ODA providers.

## 5.3 South to graduating LDC remittance and FDI flows

Given the specific attributes of Southern development cooperation regimes, it is right to explore non-ODA financial flows from the South to graduating LDCs. So let's review the data on expatriate remittances and FDI to understand other aspects of graduating LDC dependence on Southern finance.

Remittances to LDCs, which are mostly to low-income households, have made an important contribution to enhancing their income, reducing vulnerabilities and improving health and nutrition. These have directly and indirectly improved the scores in most graduation criteria indicators. Table 5.6 shows the group of graduating LDCs (12 countries) received more than $19 billion (2017) remittances from Southern countries, which host their expatriate workers. These transfers accounted for over 89 percent of total graduating LDC remittance income, indicating Southern countries' overwhelming importance in this area.

**Table 5.6:** *Remittances from Southern Countries to Graduating LDCs*

| Graduating LDC | | Remittance from Southern Countries | |
|---|---|---|---|
| | | In $ million, 2017 | As a share of total remittances received (%) |
| **1.** | **Angola** | 2 | 50.25 |
| **2.** | **Bangladesh** | 12,086 | 89.73 |
| **3.** | **Bhutan** | 38 | 94.83 |
| **4.** | **Kiribati** | 1 | 5.24 |
| **5.** | **Lao PDR** | 92 | 73.64 |
| **6.** | **Myanmar** | 668 | 92.28 |
| **7.** | **Nepal** | 6,238 | 89.80 |
| **8.** | **São Tomé and Príncipe** | 8 | 39.72 |
| **9.** | **Solomon Islands** | 2 | 9.31 |
| **10.** | **Timor-Leste** | 45 | 53.04 |
| **11.** | **Tuvalu** | 2 | 43.51 |
| **12.** | **Vanuatu** | 13 | 67.23 |
| **All Graduating LDCs** | | **19,193** | **89.38** |

Source: Author's calculations based on data retrieved from https://www.worldbank.org/en/topic/migrationremittancesdiasporaissues/brief/migration-remittances-data; Access date: 16.08.20.

Notes:

- These estimates are based on the methodology developed by Ratha and Shaw, (2007). The remittance data is for 2017, disaggregated using host country and origin country incomes.
- These are analytical estimates based on logical assumptions and derived from a global estimation of bilateral remittance flows worldwide. They are not officially reported data. The caveats attached to these estimates are: (a) the data on migrants in various destination countries is incomplete; (b) migrant incomes and the costs of living are both proxied by per capita incomes in PPP terms, which is only a rough proxy; and (c) there is no way of capturing remittances flowing through informal, unrecorded channels.

Table 5.6 also provides specific information about graduating LDCs' respective dependence on Southern remittances. Apart from a couple of SIDS (Kiribati - 5.24 percent and Solomon Islands - 9.31 percent), this source accounts for as much as or over 90 percent of external inflows (Bangladesh, Bhutan, Myanmar and Nepal) or middle ranges of around 50 percent (Angola, Vanuatu and Timor Leste).

These resources are not public finance, but private income. Yet remittances play a significant role in ameliorating poverty and improving household consumption and human development. Furthermore, such incomes are instrumental in propping up national foreign exchange reserves, which provides a strong anchor for national currencies.

**Table 5.7:** *FDI Inflows from Southern Countries to Graduating LDCs*

| | | FDI inflows from Southern Countries | |
|---|---|---|---|
| | **Graduating LDC** | **In $ million, 2012** | **As a share of total FDI (%)** |
| **1.** | **Angola** | 392 | 20 |
| **2.** | **Bangladesh** | 3,220 | 80 |
| **3.** | **Bhutan** | 13 | 25 |
| **4.** | **Kiribati** | - | - |
| **5.** | **Lao PDR** | 208 | 71 |
| **6.** | **Myanmar** | 1,083 | 76 |
| **7.** | **Nepal** | 8 | 86 |
| **8.** | **São Tomé and Príncipe** | - | - |
| **9.** | **Solomon Islands** | - | - |
| **10.** | **Timor-Leste** | - | - |
| **11.** | **Tuvalu** | - | - |
| **12.** | **Vanuatu** | 3 | 11 |
| **All Graduating LDCs** | | **4,927** | **44.35** |

Source: Author's calculations based on data retrieved from https://unctad.org/topic/investment/investment-statistics-and-trends
Access date: 16.08.20.
Note: Missing values indicate either no data available or no FDI from Southern countries

FDI is the other form of non-public financial flows from the South to graduating LDCs. Table 5.6 shows that graduating LDCs received about $5 billion FDI from Southern countries in 2017. This was more than 44 percent of the total FDI received in that year. Countries like Nepal (87 percent), Bangladesh (80 percent), Myanmar (76 percent), and Bhutan (71 percent) receive an overwhelming share of their FDI from the Southern countries.

In 2017, remittances and FDI from Southern countries to graduating LDCs totalled about $24 billion. This compares favourably with ODA from Southern bilateral and multilateral sources.

## Section 6. Southern Financial Flows during COVID-19

Demand for financial resources has increased manifold in (graduating) LDCs during the COVID-19 pandemic. It is interesting to explore how far Southern bilateral providers and financial institutions have responded to this demand.

### 6.1 Bilateral Southern providers

Major Southern countries rolled out support programmes in response to COVID-19, which became a global pandemic in the early months of 2020. This was particularly true for the two largest Southern providers: China and India. This study used extensive online research to compile two tables (Tables 6.1 and 6.2) that illustrate these programmes. It limited itself to assistance given to graduating LDCs by these two countries.

**Table 6.1:** *(Bilateral) Chinese COVID-19 Fund for Graduating LDCs*

| Graduating LDC | Support |
|---|---|
| **Angola** | Medical equipment.<br>Work to launch a testing lab.<br>Debt service suspension initiative. |
| **Bangladesh** | Medical equipment. |
| **Kiribati** | Medical supplies. |
| **Myanmar** | Health assistance.<br>Military medical team. |
| **Nepal** | Medical equipment. |
| **São Tomé and Príncipe** | Medical assistance. |
| **Solomon Islands** | Funds and medical supplies from several countries including China. Multifunctional cameras worth $176,200.<br>Five new laboratories totalling 6,000 samples per day. |
| **Timor-Leste** | $14 million medical supplies donated.<br>Construction of a new hospital and a school.<br>Re-launch Chinese-Led Digital Terrestrial Television (DTT) Project.<br>$11 million for medical support. |
| **Vanuatu** | $100,000 donation for prevention and control.<br>Medical aid. |

Sources: Author's compilation based on various sources.

The information and data presented in Table 6.1 shows that Chinese bilateral COVID-related support was given to at least nine graduating LDCs, from Africa to the Pacific via mainland Asia.

Interestingly, the assistance offered usually came in the form of a package of medical equipment and accessories, electronic and digital devices, construction of physical facilities and financial provisions. The latter was usually in the form of an aid grant and temporary suspension of debt repayments.

Table 6.2 shows India's pandemic-related support for graduating LDCs. Note that recipients of Indian assistance are mostly its neighbouring countries: Bangladesh, Nepal. Myanmar and Lao PDR.

**Table 6.2:** *(Bilateral) Indian COVID-19 Fund for Graduating LDCs*

| Graduating LDC | Support |
|---|---|
| **Bangladesh** | Humanitarian aid.<br>COVID-19 testing kits for emergency medical assistance under the SAARC COVID-19 Emergency Fund.<br>Online courses for SAARC country medical professionals under the Indian Technical and Economic Cooperation (ITEC) framework. |
| **Nepal** | Donation of testing kits. |
| **Lao PDR** | Donation of medicines and medical items to fight the pandemic. |
| **Myanmar** | India is working with ASEAN partners to supply pharmaceutical products, exchange experts and share public health information. |

Sources: Author's compilation based on various sources.

India is helping SIDS fight COVID-19 through the India-UN Development Partnership Fund established in 2017 to assist developing countries, (including LDCs, LLDCs and SIDS) with projects that contribute to achieving the SDGs.

Interestingly, India tried to use a wide range of regional inter-governmental platforms to deliver its COVID support. For example, it partnered with ASEAN in Myanmar, and the SAARC COVID-19 Emergency Fund in Bangladesh. Unlike China, Indian aid packages have, to date, rarely included financial support. Tables 6.1 and 6.2 illustrate Southern solidarity at a difficult time when Southern providers were themselves affected by the pandemic.

## 6.2 Southern multilateral sources

In line with sub-section 5.2, this section focuses on the performance of one new and one traditional Southern financial institution: the AIIB and the IsDB.

*AIIB contributions during COVID*

The AIIB created a *COVID-19 Crisis Recovery Facility* in immediate response to the pandemic, to support AIIB members and clients in alleviating and mitigating economic, financial and public health pressures arising from COVID-19. From April 2020 to October 2021, the *Crisis Recovery Facility* will provide up to $13 billion financing to both public and private sector entities in AIIB member countries facing, or at risk of facing serious adverse impacts due to COVID-19.

The Facility is designed to be flexible to emerging demand. This includes financing immediate health sector needs, building members' economic resilience[56] and financing to address liquidity constraints in infrastructure and other productive sectors.

Lower-income countries have become particularly vulnerable to its impact as the pandemic became more global and more severe. AIIB established the Special Fund Window (SFW) under its *Crisis Recovery Facility* to provide interest rate buy-downs on eligible sovereign-backed financing for lower-income members' projects co-financed by the World Bank or the Asian Development Bank.

**Table 6.3:** *AIIB to Graduating LDC Flow during COVID-19*

| Announcement Date | In $ million | Criteria | Country |
|---|---|---|---|
| **21-May 2020** | 250 | Loan | Bangladesh |
| **31-July 2020** | 100 | Investment Project | Bangladesh |

Source: AIIB website; Access date: 20.08.20.

As Table 6.3 shows, Bangladesh received a total of $350 million in two loan agreements during May-June 2020. No other (Asian) graduating LDCs have yet accessed AIIB funds. Further analysis is needed to ascertain the real reasons for graduating LDCs' limited use of AIIB COVID-19 response facilities.

*IsDB contributions during COVID*

Table 6.4 shows that, from April to July 2020, the IsDB approved a total of $476 million to mitigate pandemic impact in 13 LDCs. All these recipients were in Africa and none were graduating. All these loans were offered as Emergency Support. Again, further investigation is required to discover whether such credit decisions were based on demand-side considerations expressed through the intensity of pandemic damage or if this expressed a regional preference.

[56] This can include infrastructure investments and social and economic protection to prevent long-term damage to productive capacities. It can also protect and restore productive capital, including human capital.

**Table 6.4:** *IsDB Flows to LDCs During COVID-19*

| Announcement Date | In $ million | Criteria | Country |
|---|---|---|---|
| **9-Jul-20** | 33.6 | Emergency support | Yemen |
| **3-Jul-20** | 35.5 | Emergency support | Sudan |
| **17-Apr-20** | 20 | Financial package | Benin |
| **17-Apr-20** | 15 | Emergency support | Guinea-Bissau |
| **17-Apr-20** | 20.2 | Financial package | Uganda |
| **17-Apr-20** | 22.5 | Financial package | Mali |
| **17-Apr-20** | 25 | Emergency support | Sierra Leone |
| **17-Apr-20** | 20 | Financial package | Chad |
| **11-Apr-20** | 35 | Emergency support | Sudan |
| **11-Apr-20** | 162 | Emergency support | Senegal |
| **11-Apr-20** | 33 | Emergency support | Mauritania |
| **7-Apr-20** | 20 | Emergency support | Guinea |
| **ND** | 6 | Emergency support | Burkina Faso |
| **ND** | 28 | Emergency support | Mozambique |
| **Grand Total** | **$475.8 million** | | |

Source: IsDB website; Access date: 20.08.20.

Incidentally, our research was unable to detect any COVID-19 related allocations to graduating LDCs from the NDB or the Chiang Mai Initiative.

Southern bilateral providers (particularly China and India), and Southern financial institutions mounted modest efforts to support weaker developing economies. However, graduating LDCs have not yet been prominent among recipients of their financial support. Bilateral Southern assistance generally took the form of packages focused on medical support

## Section 7. Summing Up, Looking Forward

LDCs are one of the most disadvantaged national groups. Twelve such countries will soon move out of the LDC group, thanks to their achievements under various graduation criteria. However, they will graduate with formidable embedded weaknesses in many areas, hallmarked by the incomplete structural transformation of their economies.

This report therefore argued that deepening SSC could play an important role in helping graduating LDCs address attendant challenges and move towards sustainable graduation. It particularly explored two critically important areas that inform the graduation discourse: trade and financial flows. It also stressed that the ongoing pandemic will exacerbate LDC vulnerabilities, making smooth graduation and graduation with momentum much more challenging. The report argued that SSC could be an important graduation enabler through concrete initiatives to facilitate market access, by deepening trade cooperation and through commitments to enhance concessional financial support.

The evidence provided in the preceding sections shows the increasing integration of graduating LDCs and Global South economies, through trade and financial relationships in various forms. South-South trade has recently been on the rise and graduating LDCs' share of Southern partners' trade has been increasing fast. More than half of graduating LDC trade is with Southern partners. Graduating LDCs are also members of many Southern RTAs. They benefit from preferential market access under LDC-specific GSP schemes provided by several Southern countries and as members of RTAs. Many of these LDCs will therefore suffer significant erosion of their trade-related preferences on graduation. They will also be negatively impacted by the loss of many trade-related flexibilities, including those enjoyed under TRIPS, TRIMS and other WTO Agreements. Middle-income graduation will also mean that the terms and conditions of aid and loans to many of these countries will become more stringent.

This report therefore proposed a number of initiatives Southern partners should undertake as part of their contribution to sustainable LDC graduation. *An extension of LDC schemes to graduated LDCs for a predictable, preferably five-year, period, will provide breathing space to adjust to changing market access and competitivity scenarios.* Extending EU-EBA by three years after graduation would be a good example. LDC *preferential market access under two-tier* Southern *RTAs (LDCs and non-LDCs) could similarly be extended*. Upon graduation, LDCs are expected to assume the obligations and meet the compliance requirements stipulated for developing countries. *Southern developing country members of RTAs could provide flexibility to graduating LDCs for a specific period, to help these countries prepare*. *Beyond facilitating market access, deeper SSC, is needed to enable sustainable graduation.* A number of graduating LDCs are negotiating RTAs and CEPAs with Southern partners. *These multi-track negotiations should recognise the challenges graduating LDCs face and extend similar support to that granted to LDCs, after graduation.*

Southern solidarity should be an important factor in global discussions and negotiations on issues of interest to graduating LDCs. Despite successive UN resolutions and WTO Ministerial decisions; concrete support for graduating LDCs is yet to be forthcoming. *In view of the number of important, upcoming global fora at which these issues will be discussed (e.g. MC 12, LDC V), Southern developing countries should take a common stand on a support package for graduating LDCs*. In the context of the ongoing WTO discussions (e.g. on fisheries, e-commerce, trade-related investment, TRIMS, TRIPS and public health); Southern developing countries should extend support to address LDC and graduating LDC concerns. This report suggests that *these could be in the form of an extension for enforcement obligations and commitments, akin to the TFA for graduating LDCs*.

All such initiatives will give graduating LDCs additional time to address loss of preferences and translate comparative into competitive advantages in regional and global markets. This breathing space will help them make adequate preparations for their journey as developing countries.

Many developed and developing countries are pursuing protectionist policies in view of the pandemic. *These countries should not impose restrictive measures that undermine LDC and graduating LDC trade interests.*

Graduating LDCs are still afflicted by structural vulnerabilities reflected in their savings-investment gaps, fiscal (budgetary) deficit and current account (BoP) shortfalls. As a result, they rely increasingly on public and private financing. COVID-19 has further exacerbated their vulnerabilities and the need for external finance recently registered significant increases.

The discussion showed that larger concessional financing will be crucially important to help LDCs and graduating LDCs undertake structural transformation by building supply-side capacities, establishing production networks and developing value chains.

The study investigated both the direction and the magnitude of public and private finance received from Southern sources by LDCs and graduating LDCs.

The study investigated both the direction and the magnitude of public and private finance received from Southern sources by LDCs and graduating LDCs. It notes that analysis of ODA for LDCs was largely constrained, by the lack of data on aid and financial flows from Southern countries. The need to establish a global dataset was emphasised. An analysis of the ODA figures for non-DAC providers that report their foreign aid contributions to the OECD database was carried out. It revealed that flows from the South to the LDCs in general, and the graduating LDCs in particular, did not experience a visible upswing, although an upturn was observed in the total (global) flows. However, this is a tenuous conclusion as large Southern providers like China and India were not included in the data set. *Nonetheless, this analysis suggests that there is ample scope for non-DAC ODA providers to enhance their contributions to LDCs as they prepare for smooth and sustainable graduation. Southern countries should be encouraged to voluntarily assume a target indicator for LDC and graduating LDC financing.*

Financial institutions set up by Southern countries are becoming increasingly actively involved in LDCs. This report notes that *it would be helpful if these organisations (traditional and new) created a special window to finance the structural transformation of LDC economies* (LICs and LMICs) to ensure irreversible transitions to sustainable graduation. This is particularly important, because these banks provide a large share of the funds required to underwrite infrastructure gaps afflicting developing countries and LDCs. The need to finance social sectors is no less acute for graduating LDCs. *The Southern financial institutions therefore need to enhance overall (graduating) LDC allocations, and allocations for their social sectors.*

Along with access to public finance, private finance from Southern sources plays a very important role in LDC and graduating LDC economies. *In view of the wide-ranging unfavourable developments in the global economy, it is important to maintain remittance income and FDI from Southern countries.* Indeed, private finance reaching LDCs from the South is not only much larger than its public counterpart, it also *plays a direct and critically important role in achieving SDGs at household level*.

Southern financial institutions mounted a rapid response to bridge the fiscal gap of many LDCs (including the graduating group).

The pandemic has highlighted the new importance of SSC. Bilateral Southern providers (including China and India) not only provided various forms of health-related assistance, they also extended financial support. Southern financial institutions mounted a rapid response to bridge the fiscal gap of many LDCs (including the graduating group). This was achieved not only by enhancing liquidity through existing windows but also by opening up new rapid-response facilities. *It is important that these facilities (old and new) remain available to (graduating) LDCs as these economies recover.*

Financial support to underwrite what will probably be significant expenditure for vaccines, and cooperation in making vaccines available to all citizens are also possible avenues for pandemic-related SSC. In view of the fault lines revealed, Covid-19 should be seen as an opportunity to deepen SSC to improve health systems, build health-related infrastructure, enhance epidemiological surveillance, improve public health outcomes and build human resources for health capacities. LDCs and graduating LDCs stand to gain significantly from such SSC cooperation.

This study observes the South's role as an LDC public and private finance provider, and notes the steady rise in Southern finance for graduating LDCs. *However, public financial flows remain sub-optimal considering the recent growth and economic strengths of advanced Southern economies.* Increasing this form of finance for the weaker Southern economies, and particularly for (graduating) LDCs, will acquire increasing importance post-pandemic. *This report recommends establishing a dedicated task force under the auspices of UNOSSC to monitor how SSC will be affected by graduation, and to recommend initiatives that make SSC work more effectively towards sustainable graduation. Southern providers should make a voluntary commitment towards this at the Fifth United Nations Conference on the Least Developed Countries, which will take place in Qatar in January 2022.*

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