



**United Nations
Conference
on Trade and
Development**

Distr.
GENERAL

TD/B/LDC/AC.1/19
13 May 2003

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Sixth Meeting of Governmental Experts from
Landlocked and Transit Developing Countries
and Representatives of Donor Countries and
Financial and Development Institutions
First Session of the Intergovernmental Preparatory
Committee of the International Ministerial Conference
on Transit Transport Cooperation
New York, 23–27 June 2003

**CHALLENGES AND OPPORTUNITIES FOR FURTHER IMPROVING THE
TRANSIT SYSTEMS AND ECONOMIC DEVELOPMENT OF
LANDLOCKED AND TRANSIT DEVELOPING COUNTRIES**

Report by the Secretary-General of UNCTAD

Executive Summary

The 1995 Global Framework for Transit Transport Cooperation between Landlocked and Transit Developing Countries and the Donor Community provides a sound strategy for dealing with the transit problem. It challenges landlocked and transit developing countries to strengthen their transit transport cooperation by adopting and implementing policy measures and actions designed to improve their transit systems, and it urges the donor community to support such commitments. The countries involved and the donor community have kept their promises only to a limited extent. While the countries have concluded many bilateral and regional agreements, implementation remains patchy. Similarly, while financial and technical assistance from the donor community has continued, resources, particularly in the form of official development assistance, have declined significantly. Steps must be taken to reverse this trend. The International Ministerial Conference of Landlocked and Transit Developing Countries and Donor Countries and International Financial and Development Institutions on Transit Transport Cooperation, scheduled to be held in Almaty, Kazakhstan, from 25 to 29 August 2003, should galvanize greater political will and determination for action. The Conference could agree on performance indicators and implementation modalities for monitoring and reviewing progress in the implementation of a New Global Framework for Transit Cooperation. It should also recognize and underscore the role that regional trade expansion and foreign direct investment can play in reducing the transit cost burden and promoting economic diversification, thereby accelerating the development of landlocked and transit developing countries.

CONTENTS

INTRODUCTION.....	3
I. FACTORS THAT HAMPER ECONOMIC DEVELOPMENT IN LANDLOCKED DEVELOPING COUNTRIES.....	3
A. Geographic and demographic factors, climate, remoteness and isolation from markets.....	3
B. High transit costs.....	5
C. Inadequate trade and investment.....	8
II. PROMOTING EFFICIENT TRANSIT TRANSPORT SYSTEMS AND ECONOMIC DIVERSIFICATION.....	8
A. Improving transit transport systems.....	8
1. Enhancing physical infrastructure and transport services.....	9
2. Improving transit facilities and support services.....	11
B. Expanding trade.....	12
1. Expanding regional trade.....	12
2. Expanding international trade.....	13
C. Attracting foreign direct investment.....	13
1. General policy options.....	13
2. Country-level policy options.....	16
III. INTERNATIONAL SUPPORT MEASURES.....	19

Annex

INTRODUCTION

1. A landlocked country is defined in the United Nations Convention on the Law of the Sea as a State that has no sea-coast. In practical terms, landlocked countries are located in the interior of continents, hundreds or even thousands of kilometres from maritime ports. In Europe, despite this geographical handicap, landlocked countries are as prosperous as their coastal neighbours, which implies that it is also possible for landlocked countries in developing countries to overcome the disadvantage caused by their location and prosper.

2. When the UN General Assembly, in its resolution 1028(XI) (adopted on 20 February 1957) invited the Governments of member States “to give full recognition to the needs of landlocked member States in the matter of transit and trade”, there were only five independent landlocked countries: Afghanistan, Bolivia, the Lao People’s Democratic Republic, Nepal and Paraguay. Forty-four years later, when in 2001 the General Assembly, in its resolution 56/180, decided to convene the first International Ministerial Conference on Transit Transport Cooperation, there were 30 such countries, which together constitute about 7 per cent of the population of all developing countries.¹

3. This report is in response to that resolution and in particular paragraph 15, which requests UNCTAD to provide substantive support to the Conference. The report is divided into three chapters. Chapter I analyses the factors that hamper the economic development of landlocked developing countries (LLDCs). Chapter II identifies three mutually supportive policy instruments which, when used together, can have a major positive impact on their economic development: (a) improvement of transit systems to reduce transit costs and enhance LLDCs’ competitive position in foreign markets; (b) promotion of regional trade and integration to attract increased FDI; and (c) efforts to attract FDI to achieve economic diversification. Chapter III outlines the international support measures needed to promote efficient transit transport systems and economic diversification.

1. FACTORS THAT HAMPER ECONOMIC DEVELOPMENT IN LANDLOCKED DEVELOPING COUNTRIES

A. Geographic and Demographic Factors, Climate, Remoteness and Isolation from Markets

4. LLDCs have to cope with many factors that hamper their economic development. Many of them cannot benefit from economies of scale in production and consumption because of small population size, which is caused either by the country’s small geographic size (Bhutan, Lesotho) or by low population density (Mongolia, Niger). In a third of LLDCs, climatic conditions make economic development particularly difficult and risky, as a single prolonged drought can destroy long-term

¹ Afghanistan, Armenia, Azerbaijan, Bhutan, Bolivia, Botswana, Burkina Faso, Burundi, the Central African Republic, Chad, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People’s Democratic Republic, Lesotho, The former Yugoslav Republic of Macedonia, Malawi, Mali, Mongolia, Nepal, Niger, Paraguay, Rwanda, Swaziland, Tajikistan, Turkmenistan, Uganda, Uzbekistan, Zambia and Zimbabwe.

investments in economic activities such as ranching, which provides a source of livelihood for many people in those countries. Remoteness and isolation from world markets affect most LLDCs. Four Central Asian LLDCs (Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan) are located at least 3,500 kilometres from the nearest maritime ports. Another seven face more than 1,500 kilometres of overland transport for their imports and exports, while the remaining, with the exception of Malawi, Paraguay and Swaziland, are situated more than 1,000 kilometres from maritime ports. Given the long distances and the structure of their exports, which are dominated by low-value bulky commodities, freight and related transit costs are burdensome relative to the low value of exports.

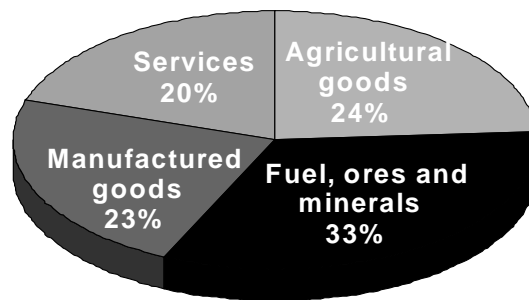


The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

5. LLDCs are characterized by a narrow economic base and poor export performance. Exports per capita in 2000, for example, were only 23 per cent of those of all developing countries, and imports per capita were just over 25 per cent. Statistics also show that over 70 per cent of aggregate exports from the 30 LLDCs are comprised of mineral and agricultural commodities and tourism services (see Figure 1). To illustrate their overdependence on a small number of export commodities: half of LLDCs rely on one commodity for at least 50 per cent of their total exports by value; two commodities account for at least three quarters of their export earnings; and three commodities yield at least 80 per cent of their export earnings.²

² UNCTAD (2001). *Transit Systems of Landlocked and Transit Developing Countries: Recent Developments and Proposals for Future Actions*. Report by the UNCTAD secretariat. (TD/B/LDC/AC.1/17)

Figure 1
LLDCs' Aggregate Structure of Exports (2001)



B. High Transit Costs

6. LLDCs' trade structure weighs heavily in their trade costs. *Ad valorem* trade costs, covering freight and insurance costs for exports, are higher in LLDCs (12.9 per cent) than in other developing countries (8.1 per cent) and developed countries (5.8 per cent), owing to high transit costs and risks associated with exports from LLDCs.³ However, such trade costs vary considerably among LLDCs, from under 5 per cent for the Lao People's Democratic Republic and Swaziland to over 50 per cent for Chad and Malawi, suggesting that the transit cost disadvantage can be mitigated.

7. Economic data for LLDCs show a negative correlation between transit costs and exports; as transit costs rise, exports' share in gross domestic product (GDP) falls (see Figure 2). This suggests that high transit costs may significantly reduce the potential for export-led economic growth in LLDCs. Thus, high transit costs can act to keep LLDCs in a low-level equilibrium income trap by preventing these countries from achieving higher income levels,⁴ particularly given the substantial reductions in potential gains from trade that necessarily result from transit costs (for both imports and exports) that are appreciably higher than the world average.

8. Nearly all LLDCs have low GDP per capita, while coastal economies generally have a relatively higher GDP per capita.⁵ Developing countries with coastal proximity have a clear advantage in establishing competitive manufacturing export sectors, which in turn have contributed significantly to overall economic growth.⁶

9. The median landlocked country tends to incur transport costs 50 per cent higher than those of the median coastal country, and to have trade volumes that are

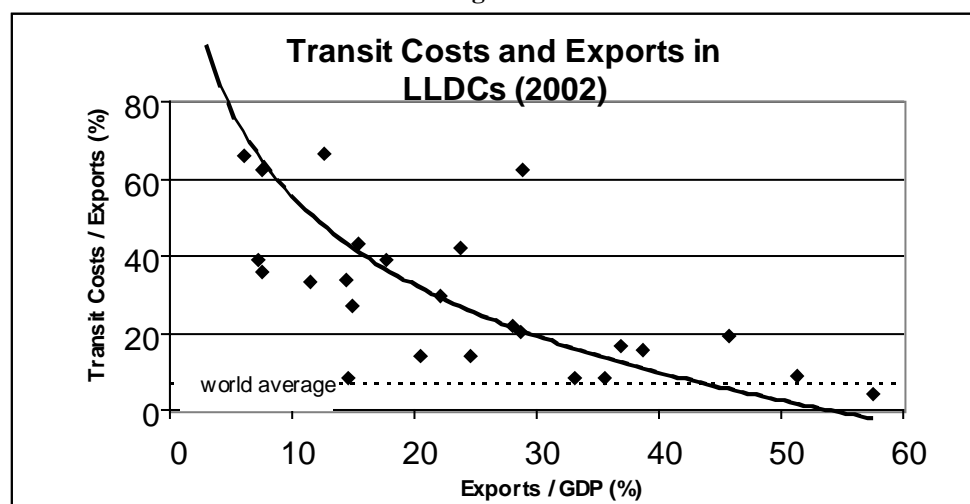
³ UNCTAD (2001). *Transit Systems of Landlocked and Transit Developing Countries: Recent Developments and Proposals for Future Actions*. Report by the UNCTAD secretariat. (TD/B/LDC/AC.1/17)

⁴ Only five of the 30 LLDCs have per capita incomes exceeding US\$1,000.

⁵ See Gallup and Sachs (1999), *Geography and Economic Development*. Working Paper No. 1, Center for International Development at Harvard University.

⁶ See Radelet and Sachs (1998), Shipping costs, manufactured exports and economic growth. Paper presented at the American Economics Association annual meeting, Washington, DC (January).

Figure 2



Note: Includes data for the following years and countries: (2000) Armenia, Azerbaijan, Bolivia, Burundi, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People's Democratic Republic, Lesotho, The former Yugoslav Republic of Macedonia, Mongolia, Nepal, Paraguay, Rwanda, Swaziland, Uganda and Zambia; (1999) Botswana; (1997) Mali and Turkmenistan; (1995) Niger; (1994) Burkina Faso, the Central African Republic, Chad, Malawi and Zimbabwe. No data are available for Afghanistan, Bhutan, Tajikistan or Uzbekistan.

Source: UNCTAD calculations based on IMF Balance of Payments Statistics 2002 and UNCTAD *Statistical Handbook 2002*. The graph has been calculated using each LLDC's most recently reported annual transit costs (transportation and insurance payments incurred for all goods exports) and the corresponding value of goods exports and GDP in that year.

60 per cent lower.⁷ Notably, the high transit costs faced by LLDCs have become a far more restrictive barrier to trade than tariffs in major markets. For instance, tariffs in Canada, the European Union, Japan and the United States vary from averages of 3 to 7 per cent on goods originating in most LLDCs. In contrast, transit costs paid by LLDCs are on average almost three times higher than these average tariffs.

10. LLDCs are also negatively affected by the high cost of their imports. A rough measure of the transit cost disadvantages faced by LLDCs is provided by balance-of-payments statistics that show freight costs as a proportion of landed cost of imports. In 1995, freight costs for developed countries were approximately 3.5 per cent of the c.i.f.⁸ import values, whereas for LLDCs they were about three times this percentage.⁹ For LLDCs in West Africa they were approximately 19.7 per cent; in East Africa, 13.5 per cent; and in Latin America, 14.2 per cent. The freight costs of the sample of landlocked countries exceeded the freight costs of all countries in their respective continents by 6 to 11 percentage points.

11. The high transport costs of LLDCs' imports inflate the prices not only of consumer goods but also of capital goods and intermediate inputs such as yarn,

⁷ Limão and Venables (1999). Infrastructure, geographical disadvantage, and transport costs. Mimeo. Working Paper. London School of Economics.

⁸ Cost, insurance and freight.

⁹ See UNCTAD (2001), *Transit Systems of Landlocked and Transit Developing Countries: Recent Developments and Proposals for Future Actions*. Report by the UNCTAD secretariat. (TD/B/LDC/AC.1/17)

thereby increasing the cost of domestic agricultural and industrial production (as does import protection unless duty drawback or waiver schemes are in operation). Thus a significant reduction in the transport cost of these countries' imports would increase their purchasing power and boost their domestic production, supporting their diversification efforts and increasing the competitiveness of their exports.

12. With increased competition in major markets forcing business to adapt to just-in-time production and management systems, flexibility, speed and reliability in delivery of goods have assumed significant importance. Yet, for many LLDCs, inadequate infrastructure, poor transport organization and a proliferation of government controls make it difficult to guarantee timely delivery of goods or ensure reliability or flexibility in the supply of goods. The fact that delays can occur outside the territorial boundaries of LLDCs underlines the point that these countries acting alone would not be in a position to overcome the real obstacles.

13. A recent case study prepared by the UN Economic and Social Commission for Asia and the Pacific (UNESCAP) reveals that, in road transport between Kazakhstan and Europe, more than 50 per cent of transit time is spent waiting at border crossing points.¹⁰ The overall time of 10 to 20 days could be reduced by half. With respect to railway border crossing, the same study indicates that whereas the average border crossing times in Europe range from 30 to 40 minutes, those in the Commonwealth of Independent States countries are measured in days rather than hours. Border crossing delays also constitute a major problem in Africa and Latin America. It has been estimated that delays at major border posts in Southern Africa cost the region in the range of \$48 million¹¹ annually. Border post delays in Southern Africa range from 4 to 26 hours on average (see Box 1).

Box 1: Delays at selected Southern African border posts

Corridor	Border post	Countries	Estimated delays (hours)
Beira	Machipanda	Mozambique/Zimbabwe	24
	Zobue	Mozambique/Malawi	24
	Mutare	Mozambique/Zimbabwe	26
Maputo	Ressano Garcia	South Africa/ Mozambique	6
	Namaacha	Swaziland/Mozambique	4
North-South	Beit-Bridge	South Africa/Zimbabwe	36
	Chirundu	Zimbabwe/Zambia	24
	Victoria Falls	Zimbabwe/Zambia	36
	Martins Drift	South Africa/Botswana	6
Trans-Capriivi	Kazungula	Botswana/Zambia	24
Trans-Kalahari	Buitepos	Namibia/Botswana	6
	Pioneer Gate	Botswana/South Africa	4
TANZAM	Nakonde	Zambia/Tanzania	17

Source: SADC Transport Corridor Agenda, July 2000 study by InfraAfrica Consultants.

¹⁰ UNESCAP (2003). *Transit Transport Issues of Landlocked and Transit Developing Countries*. Study prepared by the UNESCAP secretariat.

¹¹ All dollar amounts indicate US dollars.

C. Inadequate Trade and Investment

14. For LLDCs, the proportion of total exports and imports whose destination or source is a country in the same region or continent is low but growing.¹² Regional trade is very important for Afghanistan, the Lao People's Democratic Republic, Nepal, Paraguay and Tajikistan but significantly less well developed in many African LLDCs. One might expect there to be a large proportion of such trade because of lower average transit costs, given the shorter distances involved. However, physical infrastructure bottlenecks and non-physical barriers limit the apparent advantage of proximity and regional trade expansion.

15. In general, LLDCs perform poorly as hosts for foreign direct investment (FDI). Their combined inward FDI flows in 2001 amounted to just \$5.5 billion, accounting for some 3 per cent of total world flows in 2001. The 15 African LLDCs received a total of only \$984 million. The average FDI per capita for LLDCs during the 1990s was \$13, well below the developing-country average of \$36 during the same period. In 2001, the combined stock of FDI in LLDCs was \$41.6 billion, less than 3 per cent of the total stock in developing countries (see table in Annex). The poor performance of LLDCs by these indicators suggests that there may be a connection between lack of territorial access to the sea, remoteness and isolation and the ability of countries to attract FDI.

II. PROMOTING EFFICIENT TRANSIT TRANSPORT SYSTEMS AND ECONOMIC DIVERSIFICATION

16. Paragraph 1 above infers that LLDCs, could ultimately, like Switzerland and Austria, overcome their geographical handicap and prosper. But what strategies can ensure their success? LLDCs may not have to traverse the long development history traced by these role models. However, in designing their development programmes, they may wish to consider three objectives that are mutually reinforcing and that appear to have been fundamental to the success of the role models: (1) the development of adequate national transport networks and efficient transit transport systems, (2) proximity to a large regional market and (3) promotion of industries and activities that are not sensitive to distance.

A. Improving Transit Transport Systems

17. In 1271, when Marco Polo set out for China on the Silk Road, overland travel was done on horseback. Nowadays, rail and road transport have replaced the beast of burden. Even so, overland transport across national borders continues to present many challenges and difficulties, as is discussed below.

¹² See UNCTAD (2001), *Transit Systems of Landlocked and Transit Developing Countries: Recent Developments and Proposals for Future Actions*. Report by the UNCTAD secretariat. (TD7B/LDC/AC.1/17)

1. Enhancing physical infrastructure and transport services

18. **Rail transit:** Rail transport worldwide has been losing its share of the freight market to road transport, owing to a host of physical, operational and regulatory constraints, and it is likely to lose further ground unless it manages to overcome its problems. The poor financial condition of railways has led to deferred maintenance, weak infrastructure and speed limits;¹³ the aging of rolling stock produced frequent breakdowns, further reducing capacities and ability to meet traffic demand;¹⁴ and the inability to settle inter-railways' accounts for hire of wagons and equipment has undermined cooperative arrangements. As a result, railways have become increasingly reluctant to allow their wagons to move beyond national borders, thereby further undermining customer confidence in international railway services. In the short to medium term, urgent efforts are required to mobilize public and/or private investment to ensure adequate working capital and investment for rehabilitating and upgrading existing infrastructure, including rationalization, which may well entail discontinuation of certain railway lines that do not serve current or anticipated future needs. To enhance the sector's competitiveness, inter-railway agreements and arrangements should reinstate and/or promote *movement of through trains* (block trains, express trains); many adjoining railways no longer operate regular services because of difficulty settling accounts and late return of wagons to home lines. This trend should be reversed through use of *consignment notes*; greater efforts should be made to adopt and/or implement a common consignment note in Asia/Europe as well as Africa and Latin America. *Harmonization of tariffs* is needed; commodity-based tariffs are an obstacle to multimodal transport. Unit rates and through tariffs per container unit would better serve the needs of customers. *Combined liability of railways* is also needed; LLDCs and their transit neighbours should adopt regional agreements that establish uniform rules concerning the contract for international carriage of goods. Finally, the use of current *information and communication technologies* (ICT) to create an *integrated train operation management system* would improve railway operations.

19. **Road transit:** With technological developments enabling the manufacture of larger and faster road vehicles, road transport in the 1980s easily outpaced railways as the leading means of overland transport in developing countries as well as elsewhere in the world. However, the development of road infrastructure was uneven, favouring centres of population at the expense of rural areas where food and agricultural exports are produced. As a result, both domestic and international transport costs are very high.

20. Although road transit dominates the international carriage of goods, its advantage of quick door-to-door service has not been attained. A greater commitment by landlocked and transit developing countries to effective implementation of their bilateral and regional agreements is now required. Three areas call for particular attention.

- The first is ***maintenance of infrastructure***, including improvement of border crossing facilities. Public-sector reforms to establish dedicated road sector

¹³ UNCTAD (2001). *Review of Progress in the Development of Transit Systems in Southern Africa*. (UNCTAD/LDC/101)

¹⁴ UNCTAD (2003). *Improvement of Transit Systems in Central Asia*. (UNCTAD/LDC/2003/5)

planning and maintenance units, as well as road funds and equipment to enforce axle-load regulations, are required.

- Second, *international customs transit systems* must be strengthened. Urgent action should be taken to implement the Customs Convention on the International Transport of Goods under Cover of TIR Carnets (1975) for countries that have acceded to it and to implement other regional schemes (e.g. the regional systems of the Economic Community of West African States and the Common Market for Eastern and Southern Africa). *Customs transit information systems* such as UNCTAD's Automated System for Customs Data (ASYCUDA) can provide the tools for more effective and timely monitoring of transit movements, which can help reduce fraud, smuggling and corruption and enhance confidence in public authorities.
- Third, *harmonization of traffic regulations* is needed through accession to the Convention on Road Traffic (1968) and the Convention on Road Signs and Signals (1968); accession to *regional motor insurance schemes* (e.g. the Green Card in Europe for countries such as Kazakhstan and Kyrgyzstan, the Brown Card in West Africa, and the Yellow Card in Southern and East Africa); and efforts to *harmonize transit charges and licence procedures* for the transport service sector.

21. ***Inland water transport:*** Because of numerous adverse factors stemming from physical/material constraints as well as operational/management-related and regulatory ones, inland water transport in general, and river transport in particular, have lost a significant share of the freight market. Chad's transit trade for example, has ceased to use the Congo-Oubangui river system. Currently 60 per cent of Paraguay's major export crop, soya, is transported by road. To realize its potential, inland water transport should observe international principles related notably to free navigation, equal treatment, free transit and reciprocity, multilateral treatment of cargo reservations, rules for ship owners, transport and trade facilitation, provision of adequate port and navigational services, dispute settlement procedures, navigational safety, environmental protection, and simplified and harmonized customs procedures.¹⁵

22. ***Port facilities and services:*** For many LLDCs, delays in cargo clearance in maritime ports are often associated with problems such as late arrival of documents (notably bills of lading), poor coordination among the principal agents handling cargo at various stages (shipping agents, port authorities, custom forwarders), and inadequate off-take capacity. To improve the situation, measures should be taken to address three issues:

- ***Negotiable bills of lading:*** The use of traditional bills of lading should be discontinued. These should be replaced with non-negotiable transport documents and, where possible, use of electronic alternatives.
- ***Cooperation and communication:*** Improved communication is needed among the principal agents at the port. Advance information about ship arrival and cargo volumes would facilitate planning for both cargo clearance and off-take transport arrangements.

¹⁵ UNCTAD (2001). *Review of Recent Progress in the Development of Transit Transport Systems of Latin America*. (UNCTAD/LDC/113)

- **Deregulation:** Removal of transport service restrictions would increase the capacity and efficiency of off-take transport services.

23. **Airfreight:** LLDCs make considerable use of airfreight expressed in terms of tonnes/kilometre. All of them have at least one international airport that is frequented by international or regional carriers. Although runways in some countries are considered to be short (e.g. 3 kilometres), the more serious problems are related to support services. Several of the airports need new passenger terminals and freight sheds. Facilities like cold storage as well as modern documentation, security and handling systems are inadequate. Air traffic control and navigation do not impair long-haul operations, although some LLDCs are less well equipped and may need greater use of satellites for voice communication.

2. Improving transit facilities and support services

24. **Dry ports:** A number of landlocked and transit countries have established dry ports with the support of the international community, including UNCTAD. Dry ports are inland terminals to which shipping companies issue their own import bills of lading for import cargoes, assuming full responsibility for costs and conditions, and from which shipping companies issue their own bills of lading for export cargoes. Dry ports are closely associated with the promotion of the through-transport concept. For landlocked countries, the concept envisages no internal examination of goods or containers by customs at the seaport. Facilities provided at dry ports include offices of shipping line agents; railway goods offices; road haulage brokerage; cargo packing services; consignment consolidation services; and so on.

25. **Border crossing points:** While delay can occur at any stage of the transit journey, the most notorious delays occur at the main interface or trans-shipment points, namely between maritime and inland transport, between adjoining railways networks, and on both sides of national borders. Action is needed:

- to improve the layout of border facilities and introduce shared facilities as recommended in the International Convention on the Harmonization of Frontier Control of Goods (1982), to provide electricity and telecommunications facilities; and
- to improve inter-agency coordination of all border control services (customs, immigration police) and private-sector operators (forwarders, transporters). The use of **management information systems** to link operators at the border and establish communication between them and their headquarters should be encouraged.

26. **Institutional support arrangements for transit:** Collaboration between public- and private-sector participants in transit transport is critical for the success of transit transport programmes, including introduction of information technologies. Even as many Governments retreat from commercial transport operations, they retain the key roles of financing physical infrastructure, maintaining and managing such infrastructure, and formulating and enforcing laws and regulations. For its part, the private sector, as the main provider of transport services, has first-hand knowledge of the bottlenecks and obstacles encountered in day-to-day operations, and as such is best positioned to propose viable and practical solutions for improving transit systems. The participation of the private sector in policy formulation and decision

making will not only facilitate the adoption of suitable measures but also secure the sector's cooperation in implementing the new measures. To be effective, public- and private-sector consultations should be regular and should be institutionalized through trade and transport facilitation committees.

27. ***Human capacity building:*** The changing role of the public and private sectors requires improvement of the skills of those involved in policy-making as well as of those responsible for day-to-day operations through training, including continuing education for staff members. Increasing the quality and quantity of primary and secondary education in landlocked and transit developing countries is fundamental for building absorptive capacity for investment and implementation of reforms. The shortage of skilled labour is a major impediment to attracting and benefiting from FDI. The private sector, including foreign investors, can and should contribute to the upgrading of professional skills in landlocked and transit developing countries.

28. ***Telecommunications, energy and pipelines:*** Landlocked and transit developing countries should invest in energy and telecommunication infrastructure if they want to accelerate their integration into the world economy. Energy and telecommunications infrastructure in LLDCs is insufficient to provide reliable support to transit transport services and operations. Goods are often held up at the borders because, owing to electricity shortages, work to inspect and clear traffic can be done only during daylight hours. Similarly, lack of telephones hinders communications with headquarters. Telecommunications involve various media, including electronic, voice and warning systems in support of transport services, notably air and rail transport. Installation of modern telecommunication systems in airports or railway systems enables existing infrastructure to serve a greater number of aircraft or trains respectively. Government policy change permitting private-sector ownership and management of telecommunications has helped many LLDCs close the telecommunication gap and reap the benefit of ICT.

B. Expanding Trade

1. Expanding regional trade

29. Paragraph 14 considered the positive impact of regional trade in reducing the high transit costs facing LLDCs. In addition, the changing trade and transport patterns caused by regional trade expansion could turn many LLDCs into important cross-roads or hubs. Indeed, this is already happening. LLDCs such as Zambia and Zimbabwe have become important transit countries for trade between Southern and East Africa. Central Asia is becoming an important land bridge between Europe and Asia. These changes are bound to make transit issues in general, and the removal of transit barriers in particular, a matter of interest to a large group of LLDCs and coastal countries, leading to a surge of political will to take effective measures and actions. Moreover, the new status of LLDCs as both users and providers of transit facilities should give them greater leverage in negotiating terms and conditions for transit. Finally, regional trade expansion and integration would make it possible for small LLDCs in a region to attract increased FDI for development. Indeed, it has often been argued that a major reason for the economic success of landlocked countries in

Europe has been their proximity to and membership in large regional markets, which has made them attractive to FDI.

2. Expanding international trade

30. At the international level, further negotiations should be pursued in the World Trade Organization (WTO) under the Doha work programme in order to achieve greater market access and reduction of market entry barriers to goods (industrial and agricultural products, including commodities) and services. Provision of preferential trade access for all LLDCs and deepening of existing preferential measures should be considered. These preferential measures are, however, useful only to the extent that beneficiaries make effective use of them and that realistic rules of origin matching the productive strength of LLDCs are devised. With respect to services negotiations, at this stage LLDCs and transit member States need to identify their interests so as to be in a position to defend these interests during bilateral negotiations. A major concern of these countries in most services sectors is the building of capacity (supply and competitiveness). Another is the incorporation of their specific needs into the framework of GATS Article IV, leading to transfer of technology and capacity building.

31. Finally, trade facilitation has for the past four years been the subject of a work programme in the WTO. At the WTO Ministerial Conference in Doha, members agreed to create a road map for possible negotiations on Articles V (freedom of transit), VIII (fees and formalities connected with importation and exportation), and X (publication and administration of trade regulations) of the General Agreement on Tariffs and Trade (GATT) after the Fifth Ministerial Conference as part of the Doha Development Agenda negotiations, subject to a decision on the modalities for such negotiations. This means that the trade round launched at Doha may result in new WTO provisions on trade facilitation. The provision of technical assistance – both to help developing countries participate in the negotiations, and to help them implement the results – would thus be essential.

C. Attracting foreign direct investment

1. General policy options

32. *Policies to attract FDI that is not sensitive to distance:* Attracting FDI to industries and activities that are not sensitive to distance from sea and to related transport costs raises a number of challenges. A major issue here is the development of location-specific advantages that enable LLDCs to participate in the global service and knowledge economy. There are several aspects to this issue.

33. First, there is a need to generate the types of skills needed to attract investment and build local technological capabilities. Developing local knowledge-based resources, combined with the low cost of production in LLDCs, would make them attractive investment locations for certain types of activities. Some of these activities (e.g. call centres) may not necessarily require highly skilled employees and can be implemented successfully by semi-skilled ones. LLDCs can target these activities in particular. The low-cost labour of some LLDCs is a significant advantage here. The

emergence of globally integrated production systems based on ICT is a potential opportunity for LLDCs, because it largely eliminates the consequences of geographic distance. LLDCs should pursue policies and actions enabling them to become an integral part of such integrated international production.

34. The second major task facing Governments of LLDCs in this context is to develop adequate ICT infrastructure. A number of LLDCs have taken initiatives in this direction. Rwanda provides an example of successful development of local ITC infrastructure.¹⁶ The current situation in most LLDCs, however, leaves much to be desired. If the share of high-tech exports in total manufacturing exports is taken as a rough proxy for the intensity of activity in this area, the average share for 15 LLDCs for which data are available is 5 per cent, compared with 20 per cent for the world as a whole and about 13 per cent for low- and middle-income countries. Other indicators of ICT development suggest a similar picture. The average number of personal computers per 1,000 people in the LLDCs is 7, compared with 78 for the world as a whole; the combined number of Internet users in LLDCs is 971,800, which in 2001 accounted for 0.2 per cent of the world total.¹⁷

35. The development of local communication infrastructure can be achieved at least partly on the basis of investments by transnational corporations (TNCs) themselves. The success of Uzbekistan in attracting FDI to its telecommunication industry provides an example. This industry accounted for about one-third of the FDI stock in Uzbekistan in 1997.¹⁸ Malawi provides another example. More than 40 per cent of the inward FDI that Malawi received in the late 1990s was in the telecommunications industry; this grew to about 60 per cent in 2000.

36. An important issue in this context is the privatization of telecommunications infrastructure, which in many LLDCs is controlled by the government. TNC participation, if allowed, could contribute significantly to improving existing infrastructure. The development of a mobile phone service by the Ethiopian Telecommunication Corporation in cooperation with Ericsson is a case in point: the result has been tremendous improvement in telecommunication services.

37. Once the basic ICT infrastructure is in place, a promising direction that LLDCs can pursue in the context of the global knowledge economy is to prepare the ground for becoming sites for outsourcing of semi-skilled activities that can be transferred electronically (e.g. some back-office activities, such as data processing or certain financial transactions). There has recently been a tremendous surge in outsourcing of information- and knowledge-based activities by TNCs,¹⁹ which in the process is revolutionizing entire industries in the recipient countries.²⁰ Estimates are that at least 3.3 million white-collar jobs and \$136 billion in wages will shift from the United States alone to low-cost countries by 2015. Europe, too, is said to be joining the trend towards outsourcing.²¹ Such activities are particularly suitable for LLDCs,

¹⁶ Rwanda. *Forbes* 17 (February 2003): 1–14.

¹⁷ World Bank (2002). *Economic Indicators 2002*. Washington, D.C., World Bank.

¹⁸ UNCTAD (2001). *Investment Policy Review of Uzbekistan*. Geneva and New York, United Nations. (UNCTAD/ITE/IIP/Misc.13)

¹⁹ Is your job next? *Business Week*, 3 February 2003, pp. 50–60.

²⁰ Outsourcing: America's pain, India's gain. *The Economist*, 11 January 2003, p. 57.

²¹ Is your job next? *Business Week*, 3 February 2003, pp. 50–60.

since they are not sensitive to distance from sea and ports. The critical resources that fuel this outsourcing activity are low-cost skilled and semi-skilled labour and telecommunications infrastructure. In particular, LLDCs where such resources are abundant (e.g. Central Asia and some African countries, notably Botswana) should consider making major efforts to place themselves on the TNCs' world map for outsourcing of such activities. Some of the major beneficiaries of this trend (including China, India, the Philippines and the Russian Federation) do not necessarily possess a combination of location advantages (affecting transport costs) superior to those of these LLDCs.

38. Specific attention should also be given to targeting investments by service TNCs that produce services that can be delivered online, particularly those relying heavily on low-cost, semi-skilled labour (e.g. certain kinds of financial services). LLDCs can successfully attract financial-service TNCs seeking low-cost production locations for back-office activity, as well as for establishing local presence as part of their pursuit of a truly global strategy of being present in markets all over the world. Some LLDCs also have attractive domestic firms for acquisition that can be strengthened and can play an important role in the local market. Uganda is one LLDC that has had some success in attracting foreign financial-service TNCs, including Standard Chartered, Barclays, HSBC and Citibank.²² The surge in financial services activity that followed the sale of the state-owned Uganda Commercial Bank to South Africa's Standard Bank Investment Corporation in 2002 illustrates the potential benefits of such investment for the host countries.²³

39. In this context, special consideration might be devoted to industries and activities where LLDCs possess advantages whose full exploitation requires the distribution systems and global market knowledge of TNCs. A case in point is the music industry. While some LLDCs have a thriving local music industry,²⁴ most of the local producers are small and do not have the necessary resources to link with global distribution networks or access global markets. Media TNCs might be attracted to these countries.

40. A special category within the service industries that is not sensitive to distance and should receive specific attention is travel and tourism. Many LLDCs possess tremendous natural beauty that, with the necessary supportive infrastructure (hotels, airports and the like), can be turned into major tourism attractions. The combined number of tourists arriving in the LLDCs in 1999 was 7 million, compared with 13 million in the small island developing states (SIDS).²⁵ Regional tourism appears to be particularly attractive, especially in Africa, where many LLDCs neighbour each other. For example, a tourist landing in Rwanda could reach the tourist attractions of Uganda in less than two hours and those of Tanzania in less than 10 hours, all on relatively good roads.²⁶

²² UNCTAD (2000). *Investment Policy Review of Uganda*. Geneva and New York, United Nations. (UNCTAD/ITE/IIP/Misc.17)

²³ Uganda. *Forbes* 17 (February 2003): 1–14.

²⁴ UNCTAD (2002). *Electronic Commerce and Music Business Development in Jamaica: A Portal to the New Economy*. Geneva and New York, United Nations. (UNCTAD/ITE/TEB/8)

²⁵ World Bank (2002). *Economic Indicators 2002*. Washington, D.C., World Bank.

²⁶ Uganda. *Forbes* 17 (February 2003): 1–14.

41. Another direction for LLDCs to follow when developing strength in areas that are not sensitive to transport costs is encouraging the development of industries and activities (e.g. cut flowers, fruits and vegetables) that can rely on air transport for delivery of products. In this context, there is room to consider regional arrangements between neighbouring LLDCs, which in some cases are too small to support such developments individually. Private investors are particularly well placed to meet the needs of such initiatives.

42. ***Policies to attract FDI that will capitalize on regional integration:*** There are both demand and supply aspects to the link between regional integration and attracting FDI. From the demand side, many LLDCs are small on their own in terms of market size, but by entering regional agreements they increase their attractiveness by providing access to a larger market than their own. In such cases, they become attractive for market-seeking investment because the reduction or elimination of tariffs and other barriers among countries in the region enables major investors to serve them as one large market. The Mekong River subregion (including the Lao People's Democratic Republic, a LLDC) is an example.

43. From the supply side, regional integration enables major investors to capitalize on advantages of the region as a whole as a production site by spreading value-added activities among different members. LLDCs can search for complementarities with neighbouring countries and target investment that can benefit from them. They can also initiate joint FDI promotion programmes with their immediate neighbours in order to capitalize on the comparative advantage of each and to promote investment in the region as a whole. Bolivia and Paraguay are examples of LLDCs that have used close regional integration to enhance their ability to overcome geographic limitations. The membership of these two countries in the Southern Common Market (MERCOSUR) significantly reduces the negative implications of distance from sea. The establishment of regional transport corridors and the adoption of common rules of standards can play a major role in advancing such initiatives.²⁷ A critical condition for the success of such initiatives is the elimination of all barriers to the free flow of goods and factors of production between the relevant countries.

44. In one respect the geographic disadvantage of LLDCs can be an advantage once they are part of a regional integration agreement: their land-locked position often implies that they are located at the centre of a region. For example, Uzbekistan is centrally located in the Central Asia region; Paraguay is similarly located in Central America; Ethiopia's position could enable investors to use it as a location from which to serve both North and East Africa; and Uganda's central location gives easy access to the East African countries. Their central regional location gives these countries a natural advantage in becoming the hub of regional activity and the natural centre from which to serve the entire region.

2. Country-level policy options

45. While the LLDCs share the common attribute of geographic location distant and separated from sea and ports, they vary considerably in a number of other

²⁷ UNCTAD (2002). Specific actions related to the particular needs and problems of landlocked developing countries: Preparatory process for the international ministerial meeting on transit transport cooperation. Report of the Secretary-General of UNCTAD. (UNCTAD/A/57/340)

important aspects. These differences must be taken into account for purposes of policy formulation. To some extent, the best way to overcome their geography-based disadvantage differs from country to country, reflecting their differing individual competitive and comparative advantages and the need for customized policy responses.

46. Some LLDCs may derive a strong advantage from being neighbours of highly attractive markets. For example, in Asia, Bhutan neighbours India; Nepal is located between China and India; the Lao People's Democratic Republic neighbours China; and Kazakhstan and Mongolia are between China and Russia. In Africa, Botswana and Lesotho neighbour South Africa. LLDCs located next to attractive markets can benefit from their location in two ways.

47. First, they can seek to attract investment that will serve the large, attractive markets from locations within their economies. For example, such were the benefits of neighbouring South Africa for Lesotho and Swaziland that in the apartheid years of the late 1980s and early 1990s, most of the investment in these two countries was by investors wishing to serve the large market of South Africa while circumventing economic sanctions.²⁸ Lesotho and Swaziland have continued to benefit, as many investors have maintained their operations in these countries and continue to reinvest their earnings there. Reinvested earnings accounted for about 90 per cent of total FDI inflow to Swaziland in the mid-1990s. As the South African economy improves, these neighbouring countries stand to benefit considerably from increased demand for their exports. About 75 per cent of Swaziland's export is directed to South Africa, much of it by TNCs using Swaziland as a platform from which to serve the growing South African market.²⁹ Similarly, a number of automotive TNCs (e.g. Volvo and Hyundai) established manufacturing operations in Botswana during the 1990s in order to serve the South African market.³⁰

48. The second way in which LLDCs with attractive neighbours can benefit is by facilitating FDI from the latter. For example, by far the largest share of foreign investment in Nepal is from neighbouring India. In 1999, over a third of Nepal's \$14 billion stock of FDI originated in India. About 80 per cent of the FDI that Botswana received in the late 1990s was from neighbouring South Africa, with which Botswana has close economic relationships.³¹ South Africa is also the single largest investor in neighbouring Zimbabwe and accounted for about 20 per cent of the FDI inflows that Zimbabwe received in the late 1990s.

49. One specific area in which LLDCs with large neighbours might be particularly attractive is for TNCs seeking to customize their offerings (e.g. software products, websites) for large countries. For example, Bolivia could be the site for customization

²⁸ Busu A and Srinivasan K (2002). *Foreign Direct Investment in Africa: Some Case Studies*. Working Paper WP/02/61. Washington, D.C., International Monetary Fund.

²⁹ World Economic Forum (2000), *African Competitiveness Report 2000/2001*. New York and Oxford, Oxford University Press.

³⁰ Corporate Location (1994). *Botswana: An Objective Study of Investment Conditions*. Milton Keynes (UK), Century House Information.

³¹ Corporate Location (1994). *Botswana: An Objective Study of Investment Conditions*. Milton Keynes (UK), Century House Information.

for Latin America, or Afghanistan for the Economic Cooperation Organization region (ECO).

50. While many LLDCs are small, many others are of significant size, with populations exceeding 20 million. Such countries may want to target investment seeking to serve the local market, which can benefit from the natural barriers to competition with foreign exports created by distance and transport costs. In such cases, their geographic location becomes an advantage rather than a disadvantage in attracting FDI. A survey of Indian TNCs operating in Nepal undertaken in the early 1990s³² revealed that the overwhelming majority of this investment was directed to the Nepalese market, while only 14 per cent had been undertaken with a view to exporting the output to markets elsewhere. Another 14 per cent was undertaken for both reasons (i.e. market and export seeking). Likewise, in a survey of more than 400 investors in sub-Saharan Africa, the attraction of servicing the local market was ranked as the first motivation for investment in Ethiopia and Uganda.³³ However, given the low purchasing power of many of the larger LLDCs, initiatives for promoting such investments should be carefully conceived, directing FDI to those areas where the purchasing power of the population creates local demand that is large enough to support these activities.

51. Some LLDCs enjoy favourable trade access from some developed countries because of past historical ties. (Examples are the Lomé Convention and its successor, the Cotonou Agreements between the African, Caribbean and Pacific Group of States and the European Community.) This makes them attractive locations for certain types of export-oriented FDI, notably relating to products with low transport costs. Indeed, some LLDCs have been most successful in this direction. For example, more than 90 per cent of FDI to Lesotho involves export-oriented manufacturing. A special opportunity is currently opening up for some African LLDCs, which are able to capitalize on the advantages offered by the African Growth and Opportunity Act (AGOA), passed by the US Congress in 2000.³⁴ According to this agreement, until 2008, 33 African countries, many of which are LLDCs, will export most goods to the United States duty free.³⁵ This agreement increases the attractiveness of these countries as locations for export-oriented FDI that is directed to sales in the United States, including by US TNCs seeking low-cost production locations for output to sell back home.

52. Notwithstanding these various options for consideration by LLDCs, success in attracting investment of any kind requires FDI policy that establishes a favourable investment environment. Most LLDCs have made major progress in this area in the last decade or so.

³² Chitrakar RC (1994). *Foreign Investment and Technology Transfer in Developing Countries: Motivating Factors and Financial and Economic Performance in Nepal*. Aldershot (UK), Avebury.

³³ UNIDO (2002). *Foreign Direct Investor Perspective in Sub-Saharan Africa: UNIDO Pilot Survey in Ethiopia, Nigeria, Uganda, United Republic of Tanzania*. Vienna, UNIDO.

³⁴ Trade and development: No silver bullet. *The Economist*, 18 January 2003, pp. 69–70.

³⁵ Uganda. *Forbes* 17 (February 2003): 1–14.

III. INTERNATIONAL SUPPORT MEASURES

53. While landlocked and transit developing countries bear the primary responsibility for implementing measures designed to strengthen their cooperative and collaborative efforts, the international community, including financial and development institutions, should provide more support to enable these countries to deal effectively with their transit transport problems and requirements. Sixteen of the LLDCs are also classified by the United Nations as least developed countries, and since most transit countries are themselves developing countries facing serious economic problems, financial assistance from the international community is critical for the development and maintenance of physical infrastructure. There is, therefore, a need to reverse the decline in external financing, especially official development assistance, and encourage greater private-sector investments and managerial resources.

54. Since purely private financing schemes may not be feasible in many landlocked and transit developing countries, the international community is invited to also support new modalities of financing, such as the following:

- **Regional venture funds** use grants from multilateral organizations to pay development and management fees for selected countries or projects and to help promote interest in riskier infrastructure projects by reducing development risk.
- **Equity participation in local financial institutions** occurs when a foreign institution purchases shares in a selected bank that lends to small infrastructure projects.
- **Co-financing** involves parallel loans to an infrastructure project by a multilateral financial institution and the local bank.
- **Bank-to-bank loans** involve a foreign institution's making a long-term loan to a local bank for forward lending to small infrastructure projects.

55. The international community, including donor countries and financial and development institutions, should strengthen its support for technical cooperation programmes in the transit transport sector that are designed to improve the human and technological capacity of landlocked and transit developing countries. UNCTAD's technical cooperation programmes, including ASYCUDA and the Advance Cargo Information System (ACIS), which have made important contributions to the improvement of transit transport in landlocked developing countries and their transit neighbours, should continue to give priority to this group of countries, particularly to regions that have not yet benefited from such programmes.

56. **International trade:** In the Millennium Declaration, the Heads of State and Government committed themselves "to an open, equitable, rule-based, predictable and non-discriminatory multilateral trading and financial system." It is incumbent on the international community to promote this development objective in the context of the Doha Work Programme to achieve development results that are economically meaningful, including in areas of concern to LLDCs and transit developing countries.

57. **Commodities:** At the international level, a concerted effort by LLDC Governments, in partnership with relevant UN agencies, multilateral financial

institutions, and the donor community, could launch a long-term holistic programme to help LLDCs increase their share of value-added agrofood products and mineral.

58. **Competition policy:** International support for LLDCs and transit developing countries in competition matters should involve creating appropriate frameworks for dialogue, as well as complementarities and interaction, relating to technical assistance. Capacity building should aim to maximize the role of competition policy in granting of business licences, privatization, competitive tendering, and granting of concessions relating to infrastructure, taking into account efficiency factors; technical assistance relating to the drafting and enforcement of competition legislation or sectoral regulation; and institution-building.

59. **Trade and environment:** Developed countries and international organizations should integrate into their capacity-building programmes assistance to LLDCs in developing environmental policies adapted to national conditions; adopting environmentally sound production methods; and acquiring the technologies and infrastructure required to prevent and reduce pollution as well as increase efficient consumption of natural resources and reduce desertification.

60. The international community should acknowledge the specific needs of LLDCs, and provide them with assistance designed to overcome the geographic position. Such assistance should, in particular, relate to the development of telecommunications infrastructure to enable LLDCs to participate in the emerging global knowledge economy and attract FDI that would foster non-distance-sensitive activities. Assistance is also needed to strengthen regional integration groupings that would enable participating LLDCs to export their products and services.

ANNEX

FDI in LLDCs in comparison with SIDS, LDCs, other developing countries, developed countries, and the world as a whole (group averages)

Country groups	FDI inflows as % of gross fixed capital formation, 2001	FDI inflows, per-capita dollars (avg. 1992–2001)	FDI inflows (in millions of dollars)		FDI inflows, annual average growth (%), 1996–2001	FDI inward stock (in millions of dollars), 2001	UNCTAD Indices,* 1999–2001	
			Avg. 1995–2000	Avg. 2001			Potential**	Performance (value)
<i>LLDCs</i>	24.5	13	4,647	5,511	-1.6	41,563	0.113	1.189
<i>SIDS</i>	31.0	254	14,415	12,658	-3.4	152,604	0.201	2.193
<i>LDCs</i>	6.8	5	3,611	4,645	8.3	41,513	0.099	0.663
<i>Other developing countries</i>	12.0	36	164,346	184,459	8.0	1,932,052	0.188	0.893
<i>Developed countries</i>	11.0	488	541,757	509,760	30.5	4,504,121	0.388	0.998
<i>World</i>	11.4	100	747,939	740,232	22.6	6,816,849	n.a.	1.000

* The Inward FDI Performance Index is defined as the ratio of a country's share in global FDI flows to its share in global GDP. The Inward FDI Potential Index is constructed as the unweighted average of the normalized values of thirteen variables: rate of GDP growth, share of exports in GDP, telephone lines per 1,000 inhabitants, commercial energy use per capita, share of R&D expenditures in gross national income, share of tertiary students in the population, political and commercial country risk, share in global exports in natural resources, share in global imports of parts and accessories in electronics and in automobiles, share in global exports in services, share in global FDI inward stocks, and the share in global privatized M&A deals. Neither of the two indices is intended to provide a comprehensive model explaining the locational decisions of TNCs or to measure the impact of FDI on host economies. The averages presented in this table cover 140 countries for which data for both indices are available. For the list of the 140 countries, please see UNCTAD, 2002, Chapter II.

** Scores can range from 0 to 1.

Source: UNCTAD database.