

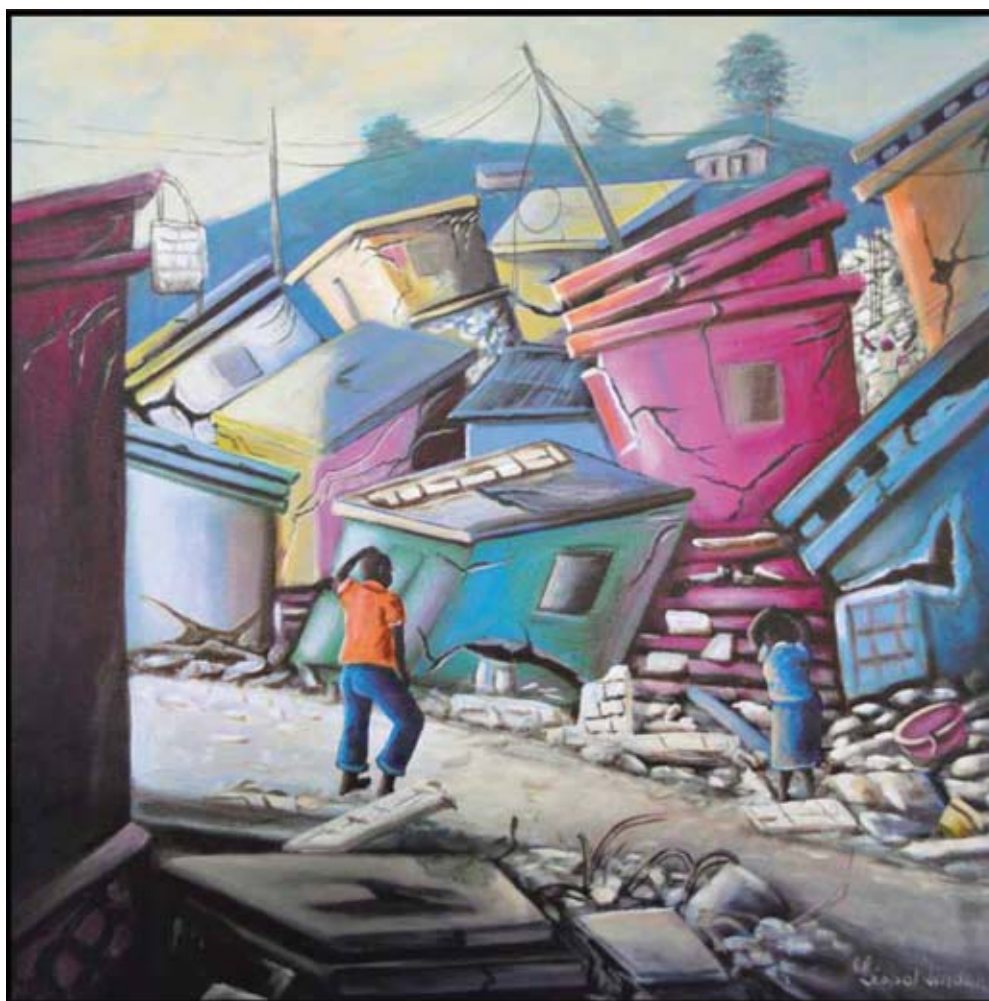
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THE LEAST DEVELOPED COUNTRIES REPORT 2010

Towards a New International Development Architecture for LDCs

CHAPTER 5

AN AGENDA FOR ACTION: (I) FINANCE AND (II) TRADE



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An Agenda for Action:

(I) Finance and (II) Trade

Chapter

5

Governments of the LDCs face many challenges in fostering sustainable growth and structural transformation in a manner that would reduce poverty substantially. Following the analyses in chapters 2 to 4, this Report advocates a paradigm shift towards new, more inclusive development paths based on promoting the productive capacities of LDCs through a strengthened developmental role of the State. This should be facilitated by means of a new international development architecture (NIDA) for the LDCs which encompasses both coherent systemic reforms of the global economic regimes of relevance to the LDCs and improved LDC-specific international support mechanisms (ISMs). Policy changes are necessary in all the five major pillars of the NIDA — finance, trade, commodities, technology and climate change. This chapter focuses on two pillars which generally receive the most attention. These are, firstly, the financial architecture, including domestic resource mobilization, private capital flows, aid, investment and debt relief, and secondly, the multilateral trade regime.

Policy changes are necessary in all the five major pillars of the NIDA. This chapter focuses on two pillars which generally receive the most attention.

A. Finance

Of the five pillars of the NIDA, finance is the most fundamental. Capital accumulation is at the centre of the growth process, and is intimately linked with technological change and structural transformation. And increased investment is the key to an effective development strategy of catching up: it is needed for expanding productive capacities and productive employment, reducing commodity dependence, upgrading production of simple manufactures and promoting productivity growth.

Of the five pillars, finance is the most fundamental. Capital accumulation is at the centre of the growth process, and is intimately linked with technological change and structural transformation.

As indicated in chapter 3, the central problem for LDCs is that they need to raise investment levels in order to achieve sustained growth, structural transformation and poverty reduction, but their domestic resources are grossly inadequate for financing not simply investment but also national governance. In addition, owing to their structural vulnerabilities, their economies are very volatile — a situation which discourages long-term investment and encourages very short-term, opportunistic entrepreneurial activity. Such activity is often focused on natural resource extraction, which does little to build the productive base of their economies.

The central problem for LDCs is that they need to raise investment levels, but their domestic resources are grossly inadequate.

Given the current low levels of domestic financial resources in LDCs, their problem of financing development in a sustained and stable way is sometimes reduced to the question of the quantity and quality of aid. But while the aid architecture remains important, this chapter seeks to place the financing challenge in a broader framework. It focuses on two major areas for action within a positive agenda for NIDA. These are: (i) the provision of resources for productive investment, particularly through the promotion of domestic financial resource mobilization, the creation of innovative sources of long-term development finance and innovative uses of aid to develop productive capacities, in addition to debt relief; and (ii) the promotion of

country ownership and creation of policy space to help mobilize and direct those resources in line with local conditions.

In this framework, aid certainly has an important role to play. Indeed, in the short and medium term there are major financing needs which can only be met through official financial flows. However, the major role of aid should not be humanitarian, to alleviate the immediate suffering of people living in abject poverty; rather it should be developmental and should play a catalytic role in leveraging other forms of development finance. Thus the role of aid should be to promote greater domestic resource mobilization and to promote the creation of an expanding investment-profits nexus embedded within LDCs and based on the domestic private sector. This would also help LDCs' reduce aid dependence. This section of the chapter proposes a number of specific elements of a positive agenda that would support this strategic orientation.

Greater mobilization of domestic financial resources is key to reducing aid dependence.

Many of the elements of the positive agenda involve systemic reforms rather than LDC-specific international support mechanisms. However, one major thrust of these systemic reforms is to promote development financing practices that are more suited to the LDC context. Some LDC-specific international support mechanisms also proposed are: (i) the fulfilment of existing commitments by DAC donors to provide 0.15 or 0.20 per cent of their gross national income (GNI) to LDCs through innovative sources of financing; (ii) technical support for the improvement of national aid management policies in LDCs, including through annual forums, to enable them to exchange relevant information and experiences; and (iii) increased efforts to enhance the development impact of untying aid by DAC donors. The design of contingency financing and anti-shock facilities to ensure real macroeconomic stability in LDCs is also discussed. A specific proposal is made under the commodities pillar.

1. PROMOTING DOMESTIC FINANCIAL RESOURCE MOBILIZATION

The national efforts can be supported by a number of international measures such as: (i) helping build capacity for tax mobilization; (ii) financial and tax cooperation; and (iii) supporting development of the financial sector in the LDCs.

Greater mobilization of domestic financial resources is key to reducing aid dependence. Recent data indicate that official development assistance was on average equivalent to 39 per cent of total public expenditure in 44 LDCs during the period 2006-2008 (Weeks, 2010). In a sample of 25 LDCs in 2008, the median amount of country programmable aid (which excludes humanitarian aid, debt relief, administrative costs, food aid and core funding for NGOs from total aid) was equivalent to 80 per cent of government final consumption expenditure. Building the capacity as well as real democratic foundations of developmental States requires increased domestic tax and revenue generation. National efforts in this regard involve both the public sector, through improved tax mobilization, and the private sector, through greater savings mobilization for domestic investment. The national efforts can be supported by a number of international measures such as: (i) helping build capacity for tax mobilization; (ii) financial and tax cooperation; and (iii) supporting development of the financial sector in the LDCs. Natural resource development strategies are also significant for enhancing domestic financial resource mobilization (as discussed in chapter 6).

(a) Capacity-building for tax mobilization

Donor agencies and international organizations can assist LDCs in building competent and effective tax administrations. They already provide technical assistance and capacity-building support to national revenue agencies, but can

do considerably more by providing training and equipment. Capacity-building should foster a creative approach to tax mobilization which recognizes the realities of the current level of development of the LDCs.¹ As argued in the *LDC Report 2009*, there is a need to increase domestic indirect taxes and to pay greater attention to property taxes, which could be a strong potential source of government revenues. Strengthening property taxes is particularly important in the context of fast urbanization. Such a policy would not only help to make the general tax structure more progressive, it could also help to finance urban infrastructure needs. A strategy that helps to boost the productivity of urban informal economic activities through credit, training and internet connectivity could also be part of a social contract whereby hitherto untaxed informal enterprises are brought into the formal system.

There is a need to increase domestic indirect taxes and to pay greater attention to property taxes, which could be a strong potential source of government revenues.

A “matching fund” approach to some aid flows could also be a useful element of reforms to strengthen government capacities for greater domestic resource mobilization. As explained in the *LDC Report 2009*, currently donors often provide budget support when a Government specifies its expenditure needs and calculates a financing gap to be filled through official development assistance (ODA). However, such an approach can be a disincentive to Governments to raise their own domestic revenues. A better option would be for donors to agree to match a percentage of funds collected by the Governments, up to a fixed limit (Di John, 2008). Such additional matching funds would thereby constitute an incentive to recipient Governments to raise more revenues.

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(b) Financial and tax cooperation²

Global financial and tax cooperation to address the issue of illegal capital outflows, including from LDCs, would further support domestic financial resource mobilization in LDCs. It is difficult to estimate the exact amount of illicit outflows of finance from developing countries – including both capital outflows, which are illegally earned, transferred or utilized, and trade invoicing through overpricing of imports and/or underpricing of exports –, but they appear to be very significant. One recent estimate of illicit outflows of finance from developing countries from these two sources alone suggested a magnitude of between \$373 billion and \$435 billion in 2002, rising to between \$859 billion and \$1.09 trillion in 2006 (Kar and Devon, 2008). Emerging-market economies and some of the more advanced developing countries accounted for the largest share of the illicit outflows from developing countries, while African countries accounted for only 3–4 per cent, and about half of the African total originated in Nigeria. However, available country-specific data relating to particular LDCs suggest that, even though the absolute amounts of such outflows from LDCs are small compared to those from the more advanced developing countries, they are significant relative to their own GDP, aid receipts or export earnings. In a few countries (e.g. Angola, Ethiopia, the Gambia, Guinea, Madagascar, the Sudan and Uganda), illicit outflows over the period 1970–2008 exceeded net ODA receipts, in some (e.g. in Angola, Guinea and Uganda) by a considerable margin. Across all African LDCs, illicit outflows amounted to some 65 per cent of ODA inflows, on average, over this 38-year period (Culpeper, 2010).

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International support to staunch this type of capital flight (but not the legitimate capital outflows based on formal decisions by investors to move money out of developing countries) would require greater financial and tax cooperation. So far, financial and banking authorities in a number of developed and developing countries have been complicit in attracting and domiciling

illicit capital flight through secrecy and other non-transparent mechanisms. Such regimes have protected wrongdoers and at the same time deprived developing countries of investment capital. This practice needs to be outlawed through financial cooperation involving collaboration between the financial sector and banking authorities. The ultimate aim would be to repatriate illicit capital to the countries of origin. The Financial Action Task Force could expedite moves for greater disclosure by enhancing its recommendations on transparency in the global financial system.

In some LDCs, illicit outflows over the period 1970–2008 exceeded net ODA receipts.

By virtue of intra-firm transactions, TNCs are able to shift profits from higher to lower tax jurisdictions in order to minimize global tax liabilities. The most common manifestation of such transfer pricing arrangements involves over- (or under-) invoicing import costs in high- (or low-) tax jurisdictions while under- (over-) invoicing export costs in order to reduce (or increase) taxable profit margins. It is difficult to uncover such transfer pricing arrangements, since TNCs typically report earnings on a globally consolidated basis, thus obscuring the configuration of their country-specific revenues and expenses. However, it is now evident, in the wake of the current economic and financial crisis, that OECD countries are themselves increasingly concerned about substantial tax losses due to transfer pricing, and are, for the first time, prepared to confront the problem. Accordingly, some OECD countries are currently aiming to move towards requiring country-by-country reporting of TNCs headquartered in their jurisdictions. A recommendation by the International Accounting Standards Board that all transnational corporations should adopt country-by-country reporting would expedite uniformity and universality in this regard. It would also assist host developing countries in getting a truer picture of TNC profits realized in their jurisdiction, and potentially in obtaining a fairer share of the global taxes levied on such TNCs.

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In order to stem illicit capital outflows, the LDCs should also consider imposing some levels of capital controls. Although this is unorthodox, the principle that some forms of time-bound and limited capital controls are important for achieving development objectives is now increasingly accepted. For example, the IMF (2010) has agreed with the idea of using capital controls on a short-term basis to deal with the effects of volatility and uncertainty in international financial markets.

(c) Financial deepening

Since an essential part of the new development paradigm entails a much greater focus on the creation of employment in the productive sectors, strengthening the financial sector to ensure that savings are allocated to commercially viable activities is paramount.

Since an essential part of the new development paradigm entails a much greater focus on the creation of employment in the productive sectors, strengthening the financial sector to ensure that savings are allocated to commercially viable activities is paramount. Donors and international agencies can support the creation of a more active and dynamic financial sector in the LDCs in a number of ways, including through the provision of technical assistance. For example, the establishment of credit reference bureaus is important to facilitate transactions by reducing the information asymmetry facing lenders. Additionally, many donor countries continue to maintain development financing institutions to provide credit and business advice to their small and medium-sized enterprises (SMEs). These institutions could advise their newly established (or re-established) counterparts in LDCs on how to operate independently on a commercially viable basis, and help them achieve their development objectives. It is true that in the past such institutions had a poor track record. However, particularly in the wake of the global financial crisis, it is necessary to re-assess the role for public sector

banks or development financing institutions in an LDC context where private enterprises face a permanent credit crunch. There are also new approaches to increasing access to finance in which targeted and time-limited government interventions help private financial institutions to address specific market failures, for example, through acting to enable private intermediaries to achieve economies of scale or reduce the costs of providing specific financial services (de la Torre, Gozzi and Schmukler, 2007). Examples of such pro-market public activism are operational in middle-income countries, and could also be more widely applied in LDCs. Also, particular attention should be given to mobilizing rural savings, given the continuing dependence of the majority of the population in LDCs on agriculture.

2. INNOVATIVE SOURCES OF FINANCE

Over the next decade, LDCs will face extraordinary challenges for which domestic financial resources are likely to be inadequate, even if more can be mobilized. Against this background there is a continuing need for DAC donors to fulfil their past commitments to provide aid to LDCs equivalent to 0.15 or 0.20 per cent of their GNI. However, if national aid budgets are not increased, new and innovative sources of financing will be required to help LDCs tackle their development challenges.

Over the past decade, and particularly since the 2002 Monterrey Conference on Financing for Development, there has been a number of ideas for new and innovative funding mechanisms for development (Atkinson, 2004). The challenge of identifying and launching new mechanisms was taken up by the Leading Group on Innovative Financing for Development formed in 2006 and now comprising 55 member States (of which 13 OECD members) and 4 observer countries. The Leading Group emerged out of a concern that the MDG targets may not be met. It has spearheaded an airline ticket levy, the International Finance Facility for Immunization, and the Advance Market Commitment for pharmaceutical research. The first two initiatives have raised \$500 million and \$1.2 billion respectively. However, the discussion on innovative financing and the Leading Group predate both the growing consensus on the enormity of the costs of climate change adaptation and mitigation, as well as the global economic crisis of 2008-2009, which have significantly altered the terms of the debate as well as the scope of the challenge (see chapter 7).

In the wake of the crisis, financial sector taxes (now including taxes on domestic financial transactions, or a financial transaction tax and a currency transaction tax) are increasingly being viewed as prudential mechanisms to inhibit speculation as well as means of mobilizing public revenue from a sector that has been seen as paying less than its share of taxes. But most of all, taxes on the financial sector are now considered necessary to help pay for the deficits spawned by the stimulus measures (beyond bank bailouts) that most industrialized countries enacted to thwart a possible depression. However, there is currently very little consensus on introducing these taxes and using the revenues for international development purposes.

Against this background, perhaps the most promising innovative source of financing for meeting aid commitments to the LDCs is from an additional allocation of special drawing rights (SDRs). The G-20 meeting in April 2009 resulted in a decision to substantially expand the amount of SDRs almost tenfold, from SDR 21.4 billion to SDR 204 billion, or the equivalent of \$318

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billion.³ However, there are a number of problems related to the current system of allocating SDRs among IMF member countries, particularly from the standpoint of LDCs, which receive a very small share of the total. Only \$18 billion worth of the \$250 billion allocation recommended by the G-20 in April 2009 was disbursed to low-income countries. Moreover there are some shortcomings relating to the nature of SDRs and the modalities of their allocation.

From the standpoint of the LDCs, SDRs serve two vital purposes. First, they provide reserve assets, and thereby liquidity to ensure the continuity of commercial transactions with trading partners. In this respect, SDRs provide a low-cost alternative to other sources of international reserves. Second, as they can be exchanged (with prescribed SDR holders, typically central banks) for freely usable currencies, they provide holders with real resources that can be used for development purposes.

With regard to the first purpose, SDRs are allocated by the IMF on the basis of their quotas at the Fund. Thus, about SDR 73 billion of the general allocation of SDR 161 billion, or 45 per cent, were allocated to the G-7 industrialized countries, of which SDR 27.5 billion went to the United States alone. In contrast, LDCs were allocated 2.37 per cent (table 34). Thus, the IMF members who least need reserves are getting the lion's share, while the poorest countries, who need them the most, are allocated a pittance.

With regard to the use of the SDR as a means of exchange for development purposes, arguments were made soon after the creation of the SDR in the 1970s to allocate these to developing-country members on the basis of need, that is, as a means of providing unconditional aid resources (sometimes referred to as the "SDR-Aid link"). After the breakdown of the Bretton Woods fixed-exchange rate system, the SDR-Aid Link was included in a number of proposals to reform the international monetary system, along with the more general proposal to transform the SDR into the world's principal reserve asset. However, despite strong support for the link idea from developing countries, it was not taken up.

Recently, there has been a number of new proposals for a growing role for the SDR, including for the provision of resources for development. After the decision in 1997 to allocate additional SDRs, the financier George Soros (2001), among others, proposed that the rich countries not needing them donate their SDRs to a special new competitive mechanism, independent of Governments and existing international institutions, to support international development programmes. In 2001, a report of the United Nations High-level Panel on Financing for Development (the Zedillo Report) recommended the "revival" of SDR emissions after a hiatus of 20 years. More recently, the idea of the SDR-Aid link, or a "development-focused allocation of SDRs" has re-emerged in the context of financing global public goods (Aryeetey, 2004). In addition, the 2009 Report of the Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System (the Stiglitz Report) addressed these issues and proposed a number of alternative ideas aimed at creating a truly global reserve system which could be based on the SDR.

The 2009 general allocation of \$250 billion in SDRs (along with the special allocation of about \$30 billion soon after) is a major opportunity for new thinking. On the basis of the IMF's quota formula, more than half of this amount was allocated to richer countries (not including emerging market

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Table 34

New SDR allocation to LDCs in 2009

Member country	General and Special SDR Allocations (in millions of SDRs)			Share of SDR allocated to LDCs	Share of LDCs GDP in 2008 (current prices and exchange rate)	Share of LDCs' population in 2008
	General SDR allocation ^{1,3}	Special SDR allocation ²	Total ³			
Afghanistan	120	8.6	128.6	3.0	2.5	3.3
Angola*	212.2	60.8	273	6.3	6.9	2.2
Bangladesh	395.3	67.9	463.3	10.7	15.6	19.6
Benin	45.9	3.9	49.8	1.1	1.3	1.1
Bhutan*	4.7	1.3	6	0.1	0.3	0.1
Burkina Faso	44.6	3.5	48.2	1.1	1.6	1.9
Burundi	57.1	3.1	60.2	1.4	0.2	1.0
Cambodia	64.9	3.6	68.5	1.6	2.2	1.8
Central African Republic	41.3	2.8	44	1.0	0.4	0.5
Chad	41.5	2.7	44.2	1.0	1.6	1.3
Comoros	6.6	1.2	7.8	0.2	0.1	0.1
Dem. Republic of Congo	395.1	29.4	424.5	9.8	2.3	7.9
Djibouti	11.8	2.2	14	0.3	0.2	0.1
Equatorial Guinea	24.2	1.3	25.5	0.6	3.5	0.1
Eritrea*	11.8	3.4	15.2	0.4	0.3	0.6
Ethiopia	99.1	17.7	116.8	2.7	5.1	9.9
Gambia	23.1	1.6	24.6	0.6	0.2	0.2
Guinea	79.4	5.5	84.9	2.0	1.0	1.2
Guinea-Bissau	10.5	1.9	12.4	0.3	0.1	0.2
Haiti	60.7	4.1	64.8	1.5	1.4	1.2
Kiribati*	4.2	1.2	5.3	0.1	0.0	0.0
Lao People's Dem. Republic	39.2	2.1	41.3	1.0	1.0	0.8
Lesotho	25.9	3.3	29.1	0.7	0.3	0.3
Liberia	95.8	7.2	103	2.4	0.2	0.5
Madagascar	90.6	7.2	97.8	2.3	1.8	2.3
Malawi	51.4	3.9	55.4	1.3	0.8	1.8
Maldives	6.1	1.3	7.4	0.2	0.2	0.0
Mali	69.2	4.3	73.5	1.7	1.7	1.6
Mauritania	47.7	4.2	51.9	1.2	0.6	0.4
Mozambique*	84.2	24.6	108.8	2.5	1.9	2.7
Myanmar	191.6	10.7	202.3	4.7	5.2	6.1
Nepal	52.9	7.1	60	1.4	2.6	3.5
Niger	48.8	4.8	53.5	1.2	1.0	1.8
Rwanda	59.4	3.7	63.1	1.5	0.9	1.2
Samoa	8.6	1.3	9.9	0.2	0.1	0.0
Sao Tome and Principe	5.5	1	6.5	0.1	0.0	0.0
Senegal	119.9	10.4	130.3	3.0	2.6	1.5
Sierra Leone	76.9	5.2	82.1	1.9	0.5	0.7
Solomon Islands	7.7	1.5	9.3	0.2	0.1	0.1
Somalia	32.8	4.2	36.9	0.9	0.5	1.1
Sudan	125.8	16.1	141.9	3.3	13.8	5.1
Timor-Leste*	6.1	1.6	7.7	0.2	0.1	0.1
Togo	54.4	4.9	59.4	1.4	0.6	0.8
Uganda	133.8	9.9	143.7	3.3	3.1	3.9
United Rep. of Tanzania	147.4	11.7	159.1	3.7	4.2	5.2
Vanuatu*	12.6	3.7	16.3	0.4	0.1	0.0
Yemen	180.5	23	203.5	4.7	6.1	2.8
Zambia	362.6	38.3	400.8	9.2	2.8	1.5
Total LDCs allocation	3 891.4	444.9	4 336.1	100	100	100
Total new allocations³	161 184.33	21 452.70	182 637.00	LDCs share of world population		12.1
LDCs share in new allocations (%)	2.41	2.07	2.37	LDCs share of world GDP		0.8

Source: UNCTAD secretariat calculations, based on IMF, Finance Department (www.imf.org); and UNCTAD's *GlobStat* database.

¹ The general allocation of 74.13 per cent of quotas took place on August 28, 2009.

² Provided under the Fourth Amendment of the Articles of Agreement (took place on September 9, 2009).

³ Assuming that no members opt out.

* Countries that will receive allocations for the first time as a result of both the General and Special SDR Allocation.

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economies or the more advanced developing countries). In other words, possibly a large amount of money could be reallocated almost immediately for development purposes. Thus there is a need to revise the allocation mechanism away from the IMF's quota-based formula towards one based on development needs, particularly those of LDCs. After considering a redistribution of the SDRs allocated in 2009, such a revision should get urgent attention. An LDC-specific international support mechanism should ensure that these countries receive an allocation that is proportional to their share of the global population.

3. ENHANCING COUNTRY OWNERSHIP OF NATIONAL DEVELOPMENT STRATEGIES

An LDC-specific international support mechanism should ensure that these countries receive an allocation that is proportional to their share of the global population.

Country ownership of national development strategies is the cornerstone of development effectiveness and also aid effectiveness. It implies that national Governments should have the ability to freely choose the strategies which they design and implement, and take the lead in both policy formulation and implementation. Enhanced country ownership of national development strategies in the LDCs is vital because it provides the basis for the formulation and implementation of development strategies that reflect local conditions and aspirations. It also enables experimentation, trial and error, pragmatism and policy pluralism. But achieving country ownership is very difficult in a situation of chronic aid dependence, and it is even more difficult when countries need official debt relief. There is a constant tension between the promotion of country ownership and the desire of international financial institutions (IFIs) and bilateral donors to ensure that their assistance is being used to support what they regard as a credible strategy. Ensuring that the high levels of aid dependence do not result in donor domination is a very complex challenge for both aid donors and aid recipients in a context where there are major inequalities between the parties in terms of resources, capabilities and power. In practice, "the greater degree of aid dependence, the greater degree of accountability of the government to donors and the lesser to their citizens" (Culpeper, 2010: 3).

Country ownership of national development strategies is the cornerstone of development effectiveness and also aid effectiveness.

In the long-term, increasing domestic financial resource mobilization is the key to enhanced country ownership. However, in the short-term, international policies can help to promote country ownership of national development strategies in five major ways, discussed below.

(a) Focusing on the core meaning of country ownership

From the start, it is necessary to clarify the meaning of country ownership. Unfortunately, the term is still equated with some form of national commitment (or buy-in) to the policy reforms advocated by the IFIs. Moreover, even in the monitoring of the implementation of the Paris Declaration, there is severe restriction of its meaning. In the Declaration, under the principle of ownership, aid recipients should be committed to:

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- Exercise leadership in developing and implementing their national development strategies through broad consultative processes;
- Translate these national development strategies into prioritized results-oriented programmes expressed in medium-term expenditure frameworks and annual budgets; and
- Take the lead in coordinating aid at all levels in conjunction with other development resources in dialogue with donors encouraging the participation of civil society and the private sector."

The Declaration also states that donors should be committed to: “Respect country leadership and help strengthen their capacity to exercise it” (OECD, 2005: 3). But the systematic monitoring of progress towards country-led development strategies now examines only the second of the aid recipient’s commitments, in particular whether aid recipients have “an operational development strategy”, which is defined in terms of results orientation and financial frameworks.

In effect, what is being monitored as “ownership” are the actions which recipient countries should take in order to increase the confidence of donors which contribute their resources to national budgets of recipients. Such confidence is of course critical for country ownership, in the sense that if donors allocate their funds to general budget support, this can, if no further strings are attached, ensure that aid is well-aligned with country priorities. However, in effect this is ownership of process conditionality relating to how a country undertakes development planning. In equating ownership with whether a development strategy is deemed operational and specifying what should constitute “operational”, the monitoring of ownership has become a way in which process conditionality in financial governance is being reinforced. The deeper issues of freedom of choice of national Governments, as well as their exercise of leadership, are sidelined. Yet these should be at the heart of mutual understanding of what it means “to put countries in the driver’s seat”.

(b) Reducing and reforming policy conditionality

Although there has been a shift in the practice of policy conditionality, there is a need for further reforms, which balance donors’ legitimate concerns about how money is spent with recipients’ legitimate concerns that policy conditionality is still overly detailed and sometimes intrusive. Such conditionality effectively sets the pace and strategic directions of the policy agenda, and generally in ways that ensure the implementation of what IFIs consider being best practices. The IMF Independent Evaluation Office assessment of progress made by the IMF in streamlining conditionality after 2000 concluded that “there is no evidence of a reduction in the number of structural conditions following the introduction of the streamlining initiative” and that “arrangements continued to include conditions that do not appear to have been ‘critical to programme objectives’” (IMF, 2007: 24, 26). An analysis for the LDCs suggests only a very slight decline in the number of structural conditions, but policy reforms in sensitive areas – those which limit fiscal space or require public sector restructuring, involve banking liberalization and privatization, or other types of liberalization – remain important features of the conditionalities (UNCTAD, 2008). These appear to go beyond the IMF’s core mandate and they also seem insensitive to the challenges of the correct policy sequencing, particularly for low-income borrowing countries (Saner and Guilherme, 2008).

Since the financial crisis, the IMF has announced further reforms relating to policy conditionality, in particular the abandonment of structural performance criteria (Bird, 2009). However, it remains to be seen how this is working out in practice. One analysis has concluded that there has been “very little fundamental change in IMF practices” (van Waeyenberge, Bargawi and McKinley, 2010: 36). Ocampo et al. (2010) suggest that in the aftermath of the crisis there have been signs of a reduction in the number of conditions applied, but only with regard to stand-by arrangements, and not to the Poverty

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Conditionality effectively sets the pace and strategic directions of the policy agenda, and generally in ways that ensure the implementation of what IFIs consider being best practices.

One analysis has concluded that there has been very little fundamental change since the crisis in IMF practices regarding conditionalities in low-income countries.

There is need for further debate on the rationale and effectiveness of policy conditionality and reforms, which would make it less intrusive and more supportive of country ownership.

Regional and subregional development banks can and should play an important complementary role to lending by the multilateral development banks

Reduction and Growth Facility (PRGF), which is targeted at low-income countries. For LDCs, the evidence indicates that some of the IMF programmes concluded after the crisis included not only restrictive monetary policies but also procyclical fiscal provisions and other measures, such as freezing of wages in the public sector and cuts in consumer subsidies, which are bound to dampen aggregate demand and negatively affect poor households (table 35). In effect, it appears that there is an asymmetry in the practices between low-income countries and non-low-income countries, with more restrictive policies in the former.

Against this background, there is need for further debate on the rationale and effectiveness of policy conditionality and reforms, which would make it less intrusive and more supportive of country ownership.

(c) Strengthening the role of regional and subregional development banks

Regional and subregional development banks can and should play an important complementary role to lending by the multilateral development banks (Griffith-Jones, Griffith-Jones and Hertova, 2008; Helleiner, 2010). These banks could help in financial deepening, provide cheap finance as well as guarantees to catalyse finance, and also provide contingency finance. The European Investment Bank and Andean Development Corporation provide good examples of the sort of funding support these banks could provide, such as infrastructure financing and guarantees. The following are some of the main strengths of regional and subregional development banks: (i) they allow a far greater voice to developing-country borrowers, as well as a greater sense of regional ownership and control; and (ii) they are able to rely more on exerting informal peer pressure rather than imposing conditionalities. Thus, strengthening the role of these banks in the provision of finance to the LDCs could not only increase the sources of finance, but could also bolster country ownership of national development strategies.

Griffith-Jones, Griffith-Jones and Hertova (2008) argue that there is a clear case for creating new regional and subregional development banks in

Table 35

IMF conditionalities in LDCs during the 2008–2009 crisis

	Fiscal policy	Monetary policy	Public-sector wage bill	Liquidity and money supply growth	Interest rate
Afghanistan	X	X		X	
Burkina Faso	X				
Burundi	X	X	X	X	
Central African Republic	X				
Djibouti	X	X	X		
Gambia	X	X			X
Haiti	V	X	V	X	
Liberia			V		
Malawi		X		X	X
Mali	X				
Mozambique	V				
Niger	V				
Sao Tome and Principe	V		X	X	
Senegal	X				
Togo	V				
United Republic of Tanzania	V	V	V	V	
Zambia	V		V		

Source: Based on Weisbrot et al., 2009.

X = contractionary elements; V = expansionary elements

developing regions, as well as expanding existing institutions. It is perhaps too complicated to envisage a dedicated LDC development bank; however, institutional arrangements could be promoted within regional and subregional development banks to ensure that they cater to the special needs of LDCs.

(d) Rebuilding State capacities

Rebuilding State capacities is essential for enhanced country ownership of national development strategies. At present, about 20 per cent of the aid to LDCs goes towards supporting governance and related activities (UNCTAD, 2009b). It is important that this be used for building developmental State capabilities, rather than promoting an unrealistically ambitious good governance agenda which involves the importation of inappropriate Western institutions, such as techniques of new public management. Rebuilding developmental State capacities should involve improved capacity for collecting and using statistics as well as the promotion of the local production of development knowledge (Zimmerman and McDonnell, 2008). There is also a particularly urgent need to rebuild capabilities for indicative economic planning, as well the capabilities of ministries of agriculture, industry and trade.

(e) Introducing and strengthening aid management policies

One important step that can be taken to increase country ownership is the adoption of an aid management policy in LDCs. This can play an important role in reducing the multiple ways in which aid delivery is undermining ownership by being unaccounted, off-budget, off-plan and misaligned.

An aid management policy differs from a national development strategy. The latter identifies goals, objectives and targets, and the actions needed to achieve them, whereas an aid management policy “is designed and used to ensure that assistance received is of such a type, and is so deployed, as to maximize its contribution to the priorities set out in the country’s statements of development strategy” (Killick, 2008: 5). By adopting an aid management policy, it is possible to separate the development strategy and the aid management policy while ensuring that the two are interrelated. In this way, development (or poverty reduction) strategies would no longer be devised with a view to seeking aid, but instead they would focus on LDCs’ strategic interests and national needs as identified by their own policymakers.

A well-working aid management policy should:

- Improve the coordination of assistance and reduce uncertainties about actual and prospective aid inflows;
- Avoid, or reduce, the proliferation of sources of assistance and of discrete donor initiatives;
- By this and other means, increase the policy space of Governments, reduce the proliferation of conditionalities and increase the predictability of receipts;
- As a result of improved Government-donor relations and better harmonization and alignment, it should reduce transaction costs;
- Provide a platform for greater mutual accountability; and
- Provide a framework through which technical assistance can become increasingly demand-driven and oriented to recipients’ capacity development needs (see Killick 2008).

Institutional arrangements could be promoted within regional and subregional development banks to ensure that they cater to the special needs of LDCs.

Rebuilding State capacities is essential for enhanced country ownership of national development strategies.

One important step that can be taken to increase country ownership is the adoption of an aid management policy in LDCs.

An aid management policy can also provide an institutional framework for coordinating North-South and South-South official finance.

The implementation of an aid management policy can offer a practical way to reduce those processes that weaken country ownership which arise from aid being off-budget, off-plan, unaccounted and unpredictable. It can also be a cornerstone for building trust and mutual understanding between donors and recipients which are essential for tackling the other processes that are undermining the ability of countries to take the lead in the design and implementation of their national development strategies. Moreover, judging from LDCs' experiences thus far, it is apparent that aid management policies can offer a powerful bottom-up approach to better aid coordination around national priorities (Menocal and Mulley, 2006; de Renzio and Mulley, 2006).

One possible international support mechanism for the LDCs would be to organize an international forum under the auspices of the UN, in which LDCs could periodically share their experiences with aid and debt management policies. Such a forum could build on existing work by UNCTAD and UNDP on debt management. This would help them draw up best practices building on the pioneering experiences of countries such as Uganda and the United Republic of Tanzania which have already adopted such policies.

One possible ISM for the LDCs would be to organize an international forum under the auspices of the UN, to periodically share their experiences with aid and debt management policies.

A significant issue for LDCs and their development partners is the low proportion of aid currently allocated to economic infrastructure and production sectors. The current approach is actually perpetuating aid dependence and storing up problems for the future.

Unless donors intend to support the MDGs indefinitely, beyond 2015, the LDCs will have to assume an increasing share of the costs involved.

4. INNOVATIVE USES OF AID TO PROMOTE THE DEVELOPMENT OF PRODUCTIVE CAPACITIES

A significant issue for LDCs and their development partners, as discussed in chapter 4, is the low proportion of aid currently allocated to economic infrastructure and production sectors. Investment in education and other social sectors is certainly vital in the LDCs but the lack of complementary investment in production sectors means that the overall approach to poverty reduction is "walking on one leg". It is in effect ignoring the fact that poverty reduction depends on both private incomes, which are closely associated to employment opportunities, as well as public services. The current approach is actually perpetuating aid dependence and storing up problems for the future. For example, donors are providing front-end investments in social programmes such as universal primary education and child health care to support the achievement of the Millennium Development Goals (MDGs), but for any sector to advance in a sustainable manner, recurrent investment and support for operation and maintenance costs are needed. Unless donors intend to support the MDGs indefinitely, beyond 2015, the LDCs will have to assume an increasing share of the costs involved. This means that Governments will need to generate revenues, primarily through taxation, to support the necessary expenditures. It would ultimately depend not only on increased efforts to promote domestic financial resource mobilization (as discussed above in section 1), but also on building the productive base of the economy. Therefore it is critical to use aid to create an expanding investment-profits nexus embedded within LDCs and based on the domestic private sector.

Aid can play a direct role in this regard through its traditional function of supporting public investment. Assuming that estimates for low-income countries can be applied to the LDCs as well, their annual infrastructure investment needs are roughly equivalent to between 7.5 per cent and 9 per cent of their GDP (Briceno-Garmendia, Estache and Shafik, 2004). This includes new investments in operations and maintenance requirements, including for main networks such as roads, rail, electricity, water and

sanitation and telecommunications. However, in 2004, ODA for transport, telecommunications and energy infrastructure was equivalent to only 0.5 per cent of LDCs' GDP, and ODA and private investment in these sectors together were equivalent to only 0.7 per cent of their GDP (UNCTAD, 2006). This shows a massive infrastructure financing gap. It will be equally important to bridge the electricity divide which currently separates the LDCs from other developing countries, as well as ensuring that the new opportunities associated with investment in information and communication technologies (ICT) are realized. Public investment in rural infrastructure, large-scale national transport, communications and power infrastructure, as well as cross-border regional networks, should have major development benefits, especially in terms of crowding in private investment.

There is a massive infrastructure financing gap in LDCs.

Beyond the traditional use of aid to support public investment, promoting the development of productive capacities also requires innovative uses of public finance. In particular there is a need for: (i) catalytic mechanisms which use public finance for market creation and for promoting private sector development, (ii) public-private partnership mechanisms which use public funds to leverage or mobilize private finance to support infrastructure provision and/or service delivery, and (iii) innovative solidarity mechanisms, such as debt buy-downs and countercyclical lending, which allow countries to adjust borrowing terms and conditions when they are adversely affected by shocks (Girishankar, 2009). International efforts to support such innovative financial solutions are estimated to have cost \$52.7 billion between 2000 and 2008. However, middle-income countries tended to benefit more; official flows to catalyse private sector development to IBRD-eligible countries more than twice the per capita level of IDA-only and blend countries.⁴

Beyond the traditional use of aid to support public investment, promoting the development of productive capacities also requires innovative uses of public finance.

At present, discussions on the catalytic use of aid for developing productive capacities in LDCs have focused mainly on how to use ODA to increase FDI flows to LDCs. This fosters a situation in which FDI and foreign affiliates have a privileged status over domestic investors. As pointed out by Mistry and Olesen (2003: 150), "too much emphasis is put on attracting foreign investment and not enough on retaining domestic capital". For example, foreign investors are given protection and have recourse to remedies from bilateral insurers, export credit agencies and aid agencies in their home countries and risk coverage guarantees from host countries as well as multilateral agencies. In addition, LDCs are trying to attract FDI by offering foreign companies privileges and exemptions that are often not provided to domestic firms. This present Report views the excessive focus on promoting FDI and neglect of domestic investment as a biased and counterproductive approach. Mistry and Olesen (2003: 150) note: "Emerging evidence suggests that an imbalance in emphasis on risk coverage (and incentives) for foreign investors may be encouraging domestic capital flight (especially from LDCs), some of which is round-tripped back as privileged foreign investment (direct or portfolio)". In addition, it is clear that vibrant domestic private investment is very important for attracting sustained foreign capital (Ndikumana and Verick, 2008).

Discussions on the catalytic use of aid for developing productive capacities in LDCs have focused mainly on how to use ODA to increase FDI flows to LDCs. This fosters a situation in which FDI and foreign affiliates have a privileged status over domestic investors.

From this perspective, this section focuses on catalytic support for private sector development and on public-private partnerships for the provision of infrastructure services. Promoting local business development in the LDCs as well as regional linkages by implementing the OECD DAC 2001 Recommendation to Untie Aid is one way of ensuring the catalytic use of aid for private sector development. The International Spark Initiative to promote enterprise innovation in LDCs, discussed in the technology section of chapter 6 (pp. 215–220), is another example of the catalytic use of aid.

(a) Catalytic uses of aid for private sector development

Multilateral and bilateral approaches to private sector development are currently dominated by the idea that given the right enabling environment, the private sector will develop and deliver equitable growth spontaneously.

Multilateral and bilateral approaches to private sector development are currently dominated by the idea that given the right enabling environment, the private sector will develop and deliver equitable growth spontaneously. According to Gibbon and Schulpen (2004: 44), the striking feature of this consensus is that “it still pays much more attention to (re-)defining the role of government than it does to the nature of the private sector and its effects on development.” There is also a strong aversion to direct government support to enterprises, even temporary, as this is perceived to distort markets, crowd out private investment and encourage political patronage.

The problem with this approach in an LDC context is that there is a missing middle in the enterprise structure, with very weak development of SMEs in the formal sector.

The problem with this approach in an LDC context is that there is a missing middle in the enterprise structure, with very weak development of SMEs, particularly medium-sized enterprises, in the formal sector. These domestic firms can have considerable local comparative advantage and also development potential, and they may try to develop those assets, but because of problems of risk, poor business support services and weak infrastructure, they are not “commercially bankable”, in the sense that it is difficult to finance their growth on purely commercial terms. Yet such finance could provide market-based solutions to those problems. There is thus a private enterprise gap. Neither private financial institutions nor official development institutions are willing to provide the resources for investment in business development, and without business development the problems which limit SMEs’ access to commercial financing solutions will persist (see UNCTAD, 2000: 91–97).

It is necessary to consider more creative approaches to the provision of direct support for private sector development.

In these circumstances, it is necessary to consider more creative approaches to the provision of direct support for private sector development. One proposal in this regard, which has been promoted by the Commonwealth Secretariat, is the establishment of a new facility focusing specifically on LDCs and other small, vulnerable economies, in the form of a dedicated and separate fund which would be owned by international financial institutions but legally distinct from them. Its specific aim would be to reduce the cost and risks to existing and new private direct investment. It would assist private investment in the production of traded goods and services in eligible States by offering domestic-currency loans, quasi-equity investment capital and guarantees, and by retailing a special form of cover for political risk, similar to that provided by the Multilateral Investment Guarantee Agency (MIGA), only simpler (Hughes and Brewster, 2002).

A new facility is needed that would assist private investment in the production of traded goods and services in eligible States by offering domestic-currency loans, quasi-equity investment capital and guarantees, and by providing a special form of cover for political risk.

It should also be possible to be more proactive in implementing the 2001 DAC Recommendation on the Untying of Aid to support business development in the LDCs. This would require support to local businesses to help them bid for contracts and also modifications in the design of tenders, paying particular attention to the size of lots. There are also possibilities for creating greater synergies between the achievement of human development goals and the building of local productive capacities for the provision of local education and health services.

(b) Public-private partnerships to support private investment in infrastructure in LDCs

Given the scale of the needs for infrastructure development in the LDCs, efforts should also be made to increase private sector participation in the provision of infrastructure (see UNCTAD 2008). Mistry and Olesen (2003) focus on the challenge of mitigating risks for foreign investors in LDCs,

particularly in infrastructure, and make a number of concrete proposals. These proposals, which are directed primarily at the EU (and summarized in UNCTAD, 2003a, box VI.3), include:

- Increase funding of multilateral risk insurance agencies such as MIGA for the creation of a special purpose capital or guarantee pool by like-minded donors which would be dedicated to covering political and non-commercial risk in LDCs.
- Sponsor a regional risk cover agency or create institutional capacity at the EU level which would focus on LDCs political risk cover and would seek the same status as MIGA.
- Create more capacity in regional development banks for providing regional risk cover.
- Increase the non-commercial risk insurance capacity of bilateral export credit agencies and official bilateral insurers through specific funding and subsidies to cover a wider range of non-commercial risks in LDCs.
- Provide project-related subsidies to cover the premium costs of political risk insurance and non-commercial risk insurance for specific projects being undertaken by OECD source countries or eligible developing-country firms in LDCs.
- Establish credit enhancement arrangements for mobilizing available domestic funding, in developing countries in general, but also, and particularly, in LDCs.

These measures could be further enhanced through home-country measures that encourage outward FDI to LDCs. In this regard, Mistry and Olesen (2003) suggest that DAC donor countries should consider:

- Providing full (100 per cent) or a large percentage (50-80 per cent) of tax credits, rebates or deductions (depending on which of these would have the greatest impact on influencing TNC behaviour in the donor country concerned) on equity invested by the home-country companies in LDCs against their tax liabilities in their home countries.
- Establishing special purpose investment promotion departments for FDI in LDCs (with commensurate budgets) within bilateral aid or investment agencies, thus ensuring that support for FDI flows to LDCs becomes a major priority in bilateral aid.
- Exploring the possibility of establishing a small special purpose LDC infrastructure investment fund that would provide equity and debt financing and of mobilizing domestic-currency resources for lending to infrastructure projects in LDCs.

If such measures were to be implemented to attract private capital inflows for infrastructure development, it would be important to ensure that their spillover effects (such as technology and skills transfer) also benefit domestic investors.

5. THE CONTINUING NEED FOR DEBT RELIEF IN LDCs

As a result of the improved external environment in the early and mid-2000s and implementation of the enhanced HIPC Initiative and MDRI, the debt burden of the LDCs as a group has diminished significantly. This has freed much-needed financial resources that were previously absorbed by onerous debt servicing (see chart 34, panels A and B below) and removed a major

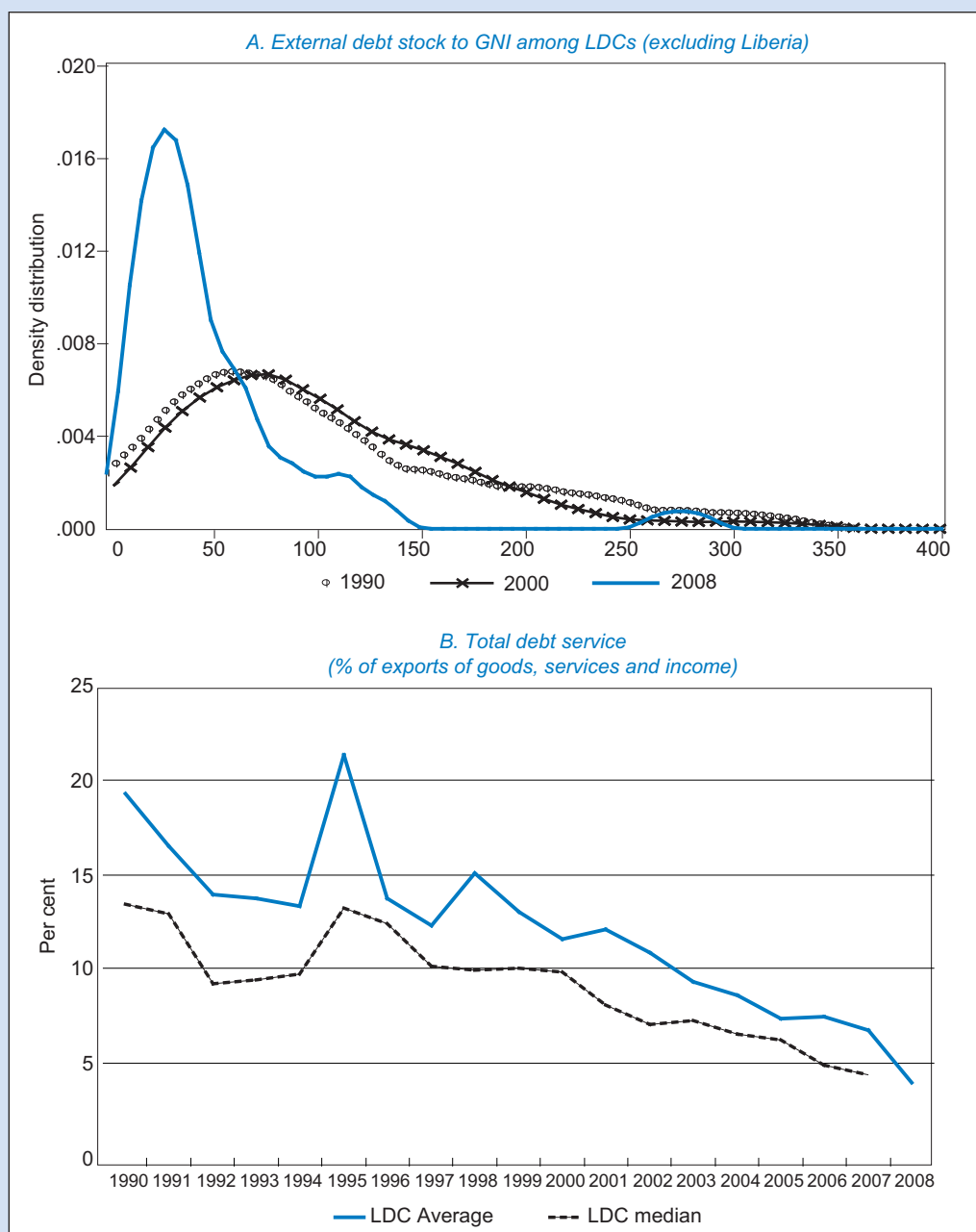
Given the scale of the needs for infrastructure development in the LDCs, efforts should also be made to increase private sector participation in the provision of infrastructure.

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Chart 34

Debt burden in LDCs



Source: UNCTAD secretariat calculations, based on World Bank, *World Development Indicators* (online).

14 LDCs which still remain in debt distress or at high risk of debt distress were not identified as HIPCs or had not reached the completion point.

risk factor which was constraining investment. Most of the debt was owed to official creditors, and high levels of external indebtedness also undermined aid effectiveness. However, this important progress does not mean that the debt issue is no longer relevant in LDCs. Firstly, as at April 2010, 14 LDCs which still remain in debt distress or at high risk of debt distress were not identified as HIPCs or had not reached the completion point. Secondly, there were 6 LDCs at high risk of debt distress and a further 5 at moderate risk, despite having reached the HIPC completion point and benefiting from substantial debt relief (see chapter 1). In addition, even in the best-case scenario of a fast recovery and a long-term growth path, LDCs and developing countries alike will face higher debt burdens as a result of the latest economic and financial crisis.

The persistence of the debt overhang in almost half of the LDCs indicates that there is a need to extend eligibility under the sunset clause of the HIPC Initiative, thereby enabling LDCs which have been unable to get debt relief to do so. Greater participation of multilateral creditors and countries outside the Paris Club in debt relief initiatives would be crucial for enabling a significant reduction of the debt burden on the poorest countries. Indeed, although the composition of debt varies significantly across countries, non-Paris Club countries and multilateral creditors own a fairly large proportion of the debt of low-income countries (IMF, 2010).

The persistence of the debt overhang in almost half of the LDCs indicates that there is a need to extend eligibility under the sunset clause of the HIPC Initiative, thereby enabling LDCs which have been unable to get debt relief to do so.

In the context of further debt relief, it would be desirable to amend the IMF-World Bank Debt Sustainability Framework (DSF) for low-income countries. In particular, the relationship between the external debt threshold and governance, which, in the current DSF is captured through the World Bank Country Policy and Institutional Assessment (CPIA) indicators, is arbitrary. In addition, the DSF should be expanded to include relevant aspects that are currently overlooked. Notably, the DSF does not distinguish between debt for financing current expenditure and debt used for investment projects, which, if and when profitable, could well ensure debt sustainability. Failure to capture this distinction may add to the volatility of public investments, thus further jeopardizing LDCs' development prospects. Similarly, so far the DSF has overlooked the importance of debt composition, both in terms of currency denomination and maturity. In this respect, the structure of debt should be examined within the DSF, as it is an important determinant of sustainability (see also UNCTAD, 2010a).

In the context of further debt relief, it would be desirable to amend the IMF-World Bank Debt Sustainability Framework (DSF) for low-income countries.

There is also a need to review the minimum concessionality requirements faced by countries that are eligible to borrow under the PRGF or IDA. Under the current regulations, these countries are prevented from contracting an external borrowing that does not include a concessionality component of at least 35 per cent. Some form of flexibility would be advisable in this respect, such as focusing on average concessionality requirements rather than on each individual borrowing operation.

6. THE NEED FOR COMPENSATORY FINANCING FOR SHOCKS

The fuel, food and financial crises which the LDCs successively experienced in the latter half of the 2000s are indicative of the need for anti-shock financing facilities for LDCs. The IFIs have certainly responded to the global crisis since 2008 by significantly increasing emergency financing for low-income countries and LDCs (see box 7) so that these countries now have greater recourse to quick-disbursing anti-shock financing. However, there are still weaknesses in the shock-financing architecture. Firstly, although the IFIs now acknowledge the need for applying only low conditionality in their support programmes for countries under severe stress, practice still varies considerably, with some programmes such as the IMF's Exogenous Shock Facility (ESF) still setting economic performance targets. Secondly, grant funding is almost non-existent. The World Bank's recently launched crisis response window (CRW), delivered through the IDA, offers the possibility of grant funding on the basis of debt sustainability criteria. In other words, grant funding is not offered unless the borrower crosses a threshold of unsustainable debt. Thirdly, the key target of IMF programmes is to remedy balance-of-payments disequilibria and thereby strengthen macroeconomic stability. The programmes are not oriented towards longer term development objectives related to poverty reduction and social and economic progress. The World

The fuel, food and financial crises which the LDCs successively experienced in the latter half of the 2000s are indicative of the need for anti-shock financing facilities for LDCs.

Box 7. Recent developments in IMF and World Bank contingency financing facilities open to LDCs

IMF facilities

The IMF has provided emergency financing under a number of different facilities since 1962, offering short-term assistance to countries afflicted by temporary external shocks or natural disasters. The Compensatory Financing Facility (CFF) was created in 1963 to help members avoid undue adjustment to temporary export shortfalls caused by exogenous shocks. This facility was later enhanced to provide funding for a temporary increase in the costs of cereal imports. Although a low-conditionality facility, the financial terms are non-concessional, with repayment expected within five years or less. Because of this, the CFF has been increasingly onerous for low-income countries. Moreover, access has been increasingly difficult because of complexities surrounding eligibility, particularly the “temporariness” of the shock. Although the CFF was streamlined in 2000, because of these problems it has fallen into almost complete disuse, leading to recurring proposals to abolish it altogether, and other Fund facilities have taken its place.

The Fund’s basic programme for helping countries cope with shocks is the emergency assistance loan, primarily designed to help countries cope with financial shocks associated with natural disasters. In 1995, coverage was extended to countries in post-conflict situations. While these IMF loans do not require adherence to performance criteria, the terms of financing are non-concessional, requiring repayment of the principal within five years. However, since 2005 the interest rate charged on such loans has been subsidized by bilateral donors, bringing it down to 0.5 per cent per year. More recently still, PRGF-eligible Fund members have been allowed even greater concessions in terms of the interest rate: between 0 and 0.25 per cent. The Fund’s emergency loans do not carry performance criteria, but borrowers are required to indicate the general economic policies they propose to follow.

In November 2005, the IMF established its Exogenous Shocks Facility (ESF), specifically designed as a rapid-reaction facility for low-income countries experiencing shocks such as natural disasters, commodity price escalations (e.g. food and fuel prices), conflict, and trade-disrupting crises in neighbouring countries. Access to ESF support was augmented in 2008 and 2009. The ESF effectively extended members’ access to rapid emergency financing from 25 per cent of quota (under emergency assistance loans) to 50 per cent for each shock, and to 150 per cent of quota over two years. Financing terms under the ESF are equivalent to those under the PRGF (i.e. an interest rate of 0.5 per cent and repayment beginning at five-and-a-half years and ending ten years after the disbursement).

Conditionality under the ESF varies: under rapid access, the borrowing member only has to commit to appropriate policies to address the shock, and in exceptional cases to take targeted upfront measures. Under the high access component, which gives access to 150 per cent of quota, conditionality is more demanding, requiring an economic programme of the same standard as required under the PRGF.

World Bank funding programmes

The Bank has had a number of funding programmes to help members cope with crises. For low-income (IDA-eligible) countries, these comprise the two programmes under the Vulnerability Financing Facility: the Global Food Crisis Response Program and the Rapid Social Response Program. The former was launched in May 2008, in coordination with the United Nations High-Level Task Force on Food Security, to provide immediate relief to countries particularly badly hit by high food prices. With initial funds of \$1.2 billion (of which \$200 million were in the form of grants), the amount was increased to \$2 billion in April 2009. Funding has supported vulnerable populations through food-for-work schemes, supplementary rations and micronutrients for mothers and their children, and school feeding programmes. The Rapid Social Response Program aims at sustaining national investments in health, education and social safety nets. Some \$2.03 billion in IDA lending was projected for the period 2009–2011.

However, the mounting demands of the latest economic crisis have left a financing gap for IDA recipient countries. Despite the fact that the fifteenth replenishment of the IDA (IDA-15) for the period 2008–2011 was the largest in the IDA’s history, securing \$41.6 billion in donor pledges, a gap of \$11.6 billion was identified in relation to core spending requirements in IDA countries (IDA, 2009a). The responses to the crisis until 2009 (including that of the Vulnerability Financing Facility) were ad hoc, and in a sense “taxed” normal long-term development programming.

Accordingly, the Pittsburgh meeting of G-20 Leaders in September 2009 acknowledged the need for accelerated and additional concessional financing support for low-income countries to cushion the impact of the crisis on the poorest. The World Bank was asked to explore the benefits of a new crisis response facility to protect low-income countries from future crises.^a The Bank responded by proposing a crisis response window (CRW) on a pilot basis, to be operationalized in 2010 as part of IDA-15 with a view to integrating this facility as part of IDA-16 (IDA, 2009b). The pilot facility was approved by the Bank in December 2009. An amount of \$1.3 billion was allocated to support low-income countries affected by declining trade flows, FDI and remittances, and/or experiencing fiscal stress on account of the crisis. Some 55 countries, most of them LDCs, were proposed as eligible for support.

The CRW was designed to complement the IMF’s crisis facilities, which are aimed at strengthening macroeconomic stability and achieving balance-of-payments equilibrium, while the World Bank’s new programme is aimed at addressing broader key public expenditure needs. It also complements the Bank’s earlier, ad hoc Vulnerability Financing Facility that had focused on food security and key social sectors. Although there is no thematic or sectoral earmarking for support, countries will be encouraged to give priority to core social spending on health, education and social safety nets, which have been jeopardized

Box 7 (contd.)

or reduced on account of the latest crisis. Implementation is expected to be rapid and to make a difference on the ground. The terms of financing would be the same as under the IDA, including the possibility of a grant portion, depending on debt sustainability considerations.

A substantial portion of the pilot CRW is to be allocated during the first half of 2010 and the rest during the 12-month period remaining in the IDA-15 replenishment period. Depending on the outcome of the pilot phase, it is intended to propose a permanent CRW as part of the IDA-16 replenishment.

Source: Culpepper, 2010.

a G-20 Communiqué, Pittsburgh, 25 September 2009.

Bank is more oriented to sustaining social achievements and cushioning the effects of crises through provision of social safety nets. It pays little attention to the need to sustain the development of productive capacities. Finally, it is uncertain whether the level of current facilities is adequate, particularly as one of the more significant initiatives — the World Bank's CRW — is still only in a pilot phase. The adequacy of this and other anti-shock facilities will become more evident as this pilot phase is implemented and evaluated in the course of preparing for the sixteenth round of IDA replenishment (IDA-16), which may include a more permanent facility in the World Bank Group.

There is a strong case for a new compensatory financing architecture to provide funding for shocks to LDCs. The LDCs are not only highly prone to natural disasters (see chapter 4), they are also extremely vulnerable to external shocks, manifested in structural deficits of the current account and a very volatile cyclical component. Volatility in export revenues is a major contributory factor, largely owing to the fact that commodity-dependent countries, typically characterized by high export concentration, are more exposed to terms-of-trade shocks (Williamson, 2005). At the same time, it is clear that private capital flows are also highly volatile (Bhinda and Martin, 2009), though they do not represent as important a source of balance-of-payments volatility in LDCs as in emerging economies owing to the smaller size of these inflows into economies of LDCs. Overall, in view of LDCs' import sensitivity, it is clear that safeguarding their capacity to import, even at times of exogenous shocks to their economy, is critical for the sustainable development of their productive capacities.

In designing a new compensatory financing architecture, it is necessary to learn from past experiences. Recently, the European Commission (EC) approved an ad hoc Vulnerability-FLEX mechanism which is open to 13 ACP countries and seeks to avoid some of the weaknesses of previous EU anti-shock facilities. The aim of this mechanism is to support developing countries in coping with crises. Support under V-FLEX is provided as an additional single payment to the already existing budget support programmes, or, if necessary, it is provided through existing projects or programmes. It is disbursed rapidly and in the form of grants. However, there are questions as to whether the size of the available resources is sufficient (Dalleau, 2010).

Some important principles that should guide a new compensatory financing mechanism are:

- Sufficient speed of disbursement, in order to minimize the costs of adjustment.
- The amount disbursed should be proportional to the needs for responding to the precise shock, in order to prevent long-lasting effects on a country's economic trajectory.

There is a strong case for a new compensatory financing architecture to provide funding for shocks to LDCs. The LDCs are not only highly prone to natural disasters, they are also extremely vulnerable to external shocks, manifested in structural deficits of the current account and a very volatile export revenues.

In designing a new compensatory financing architecture, it is necessary to learn from past experiences.

International trade is vital for development and poverty reduction in the LDCs. But the links between trade, development and poverty reduction are neither simple nor automatic.

- Low or no conditionality, as high conditionality implies lengthier processes; moreover, exogenous shocks should not require domestic adjustment measures until it is proven they have persistent effects.
- Grant funding.
- Alignment with a country's needs.
- Shocks should be precisely measured and monitored – for example, export shortfalls should be measured in terms of export purchasing power, rather than in nominal values.

Compensatory financing is particularly important in relation to commodity-price shocks, and the issue is taken up further in chapter 6.

B. Trade

International trade is vital for development and poverty reduction in the LDCs. But the links between trade, development and poverty reduction are neither simple nor automatic. The evidence presented throughout this Report suggests that the way LDCs have been integrating into the world economy over the past 30 years has not had a favourable impact on their development. Indeed, LDCs are more marginalized within the global economy today than they were three decades ago. Moreover, on average they have less diversified economies and more concentrated exports, and they have become more commodity-dependent than before. Instead of attenuating their structural vulnerabilities, integration has amplified them. Their income levels, instead of gradually catching up with developed countries, have been falling even further behind. As a result, their poverty rates are very high and other social indicators weak (as indicated in chapter 1).

The evidence throughout this Report suggests that the way LDCs have been integrating into the world economy over the past 30 years has not had a favourable impact on their development. LDCs are more marginalized within the global economy today than they were three decades ago.

In an open world economy, LDCs face a major development challenge, which arises quite simply because the productivity gap between LDCs and developed countries is enormous. Based on the purchasing power parity estimates of the World Bank and the employment data of the International Labour Organization, in 2008 the average GNI per worker in LDCs was \$3,022 (at current international dollars), compared with \$68,607 in OECD countries — a ratio of 22 to 1 in favour of OECD countries. When compared with the productivity gap between the leaders (the Netherlands and the United Kingdom) and the poorest countries in the group of now developed countries (Finland and Japan) in the nineteenth century, the situation of LDCs today is far worse. According to Chang (2003), the gap in the nineteenth century was in the range of 2–4 to 1. This suggests that the gap today between the OECD countries and the LDCs is more than five times greater than the gap of the early catching up countries. The magnitude of that gap also suggests that firms from LDCs have few, if any, possibilities to compete with firms from developed countries.

In an open world economy, LDCs face a major development challenge, which arises because the productivity gap between LDCs and developed countries is enormous.

As briefly discussed in chapter 3 and in more detail in UNCTAD (2004), LDCs have undertaken extensive trade liberalization since the late 1980s. Indeed, the extent and depth of their trade liberalization has resulted in very open trade regimes by international standards. Some of them now have even more open trade regimes than other developing countries, and others have trade regimes that are as open as those of developed countries. On average, their tariffs are only slightly higher than in other countries. Hence, the main policy challenge of LDCs is how to promote development in the

context of an open trade regime. To reverse the above-mentioned negative trends, LDCs need to promote diversification of their economies and build up their productive capacities. A major question is how they can achieve these objectives, given the extent of openness of their economies and the size of the productivity gap.

This section of the chapter proposes some aspects of the design of the multilateral trading system to address this challenge as part of a NIDA for LDCs. It focuses on three major areas for action: (i) the possibility of an “early harvest” for LDCs emerging from the Doha Round of multilateral trade negotiations under the aegis of the WTO, in particular in relation to duty-free and quota-free (DFQF) market access; (ii) empowering LDCs to use existing flexibilities provided under current trade rules so that they can implement a strategic trade policy; and (iii) financing trade development through the Enhanced Integrated Framework and Aid for Trade. All three areas of action are complementary, as realizing commercial benefits from preferential market access depends upon both the availability of finance to develop export supply capacities and also on trade policies that provide appropriate incentives.

In contrast to the other pillars of the NIDA, the LDCs themselves formulated a set of detailed proposals on how the multilateral trading system could best promote their development interests. These proposals were contained in a series of LDC Ministers’ Declarations adopted at Zanzibar in 2001, Dhaka in 2003, Dakar in 2004, Livingstone in 2005, Maseru in 2008 and Dar es Salaam in 2009. The Dar es Salaam Declaration (WTO, 2009) includes a very rich and detailed set of proposals (see box 8). While all these proposals are important, the present chapter focuses on a few priorities for LDC-specific ISMs within the multilateral trading system.

1. THE “EARLY HARVEST” FOR LDCs, EMERGING FROM THE DOHA NEGOTIATIONS

(a) The timing of the “early harvest”

It is clear that the successful conclusion of the Doha Round of multilateral trade negotiations at the WTO in a manner which maintains the central importance of development outcomes for all developing countries would also benefit LDCs. Such benefits would arise partly from its overall boost to global prosperity. In addition, LDCs would gain if other developing countries could upgrade their export structures and move up the trade development ladder, thereby creating space for the tail-end latecomer countries. On the other hand, when other developing countries are hindered in their development processes, their competition with LDCs intensifies.

LDCs could also benefit from LDC-specific preferential treatment within the Doha Round. The Dar es Salaam Declaration at the Sixth LDC Trade Ministers’ Meeting was particularly concerned with how to advance and promote the interests of LDCs in the Round. It proposed a set of issues which could constitute an “early harvest” for the LDCs from the negotiations, namely: (i) full implementation of DFQF market access for all products originating from all LDCs, in line with Decision 36 of Annex F of the Hong Kong WTO Ministerial Declaration, (ii) a waiver decision on preferential and more favourable treatment for services and services suppliers of LDCs, and (iii) an ambitious, expeditious and specific outcome for cotton-trade-related aspects,⁵ in particular the elimination of trade-distorting domestic support

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Box 8. The Dar es Salaam Declaration of Trade Ministers of LDCs

Apart from calling for an early harvest of LDC package under the Doha Round, the Dar es Salaam Declaration identified an LDC common platform on key trade and development issues. On the DFQF market access, the Declaration called for a full implementation of the DFQF market access for “all products” from “all LDCs” “by early 2010” “with a view to ensuring commercially meaningful market access for at least 97 per cent of products” which reflects particular concern of Asian LDCs. Developed countries are called upon to specify the products to be included in the 97 per cent coverage “by the time of the draft schedule” and to achieve 100 per cent coverage “no later than the end of implementation period” with the specification of target dates for DFQF treatment on a product-by-product basis, thereby addressing the ambiguity left in the Hong Kong Ministerial Declaration regarding the timing for achieving 100 per cent coverage.

As regards agriculture, the Declaration reaffirmed LDCs’ right for access to all SDT and exemption from any form of reduction commitments, including for those LDCs forming customs union with non-LDCs. This is significant as some LDCs that are part of customs union (e.g. Lesotho in SACU, Rwanda, Burundi, Tanzania in EAC) may be subject to deeper liberalization commitments on account of non-LDC partners that have to undertake such commitments under agricultural tariff cutting modalities. It also calls for an early harvest on cotton, strengthened disciplines on green box, prohibition of export restriction on food items by non-LDCs, and elimination of NTBs affecting commodities, as well as greater LDC flexibilities regarding special safeguard mechanism (SSM) and monetization of non-emergency food aid.

On NAMA, as in agriculture, the Declaration reaffirmed LDCs’ right for access to all SDT and exemption from any form of reduction commitments (including sectoral), again also for those LDCs forming customs union with non-LDCs. It reiterated LDCs flexibility in determining the extent and level of tariff bindings, the elimination of all NTBs affecting LDCs exports and LDC flexibility in using export taxes.

Preference erosion was key issue. The Declaration called for provisions on tropical products (in agriculture) and sectoral initiatives (in NAMA), both of which could lead to “formula-plus” deeper tariff cuts, not to harm export interests of LDCs by causing particularly significant preference erosion. As regards NAMA sectorals, it stresses that “DFQF market access should be provided to LDCs in the products included in the sectoral initiatives from the start of the implementation periods”. This may be significant as proposed sectoral initiative include textile and clothing, which are the major products currently not covered under the US GSP scheme. Thus, extending DFQF coverage to this sector will significantly increase coverage in that market.

As regards services, the Declaration stresses the need for immediate decision granting a waiver for preferential treatment for LDCs, particularly in Mode 4 (as early harvest). Since the waiver decision is only enabling in nature (i.e., it does not guarantee effective provision of preferential market access in individual developed country), it is important to ensure that such preferential market opening be expeditiously achieved on sectors and modes of export interest to LDCs.

On trade facilitation, the Declaration rejected the early harvest for trade facilitation, reaffirming it to be part of a single undertaking. It rather highlighted the need for priority to be given to LDCs in the provision of technical assistance and capacity building support, as well as for flexibilities in LDCs’ implementation of commitments, subject to self-assessment, provision of assistance and capacity acquisition.

On TRIPS, the Declaration made a call for TRIPS amendment to include mandatory requirement for the disclosure of the country of origin of genetic resources and traditional knowledge in patent application in the context of TRIPS-Convention on Biological Diversity (CBD) relationship. It also called for an effective provision of incentives for transfer of technology under TRIPS Article 66.2.

As regards rules, the Declaration supported the exemption of LDCs from the prohibition of fishery subsidies. It also supported the incorporation of SDT in GATT Article XXIV on regional trade agreements in view of the continued engagement of African LDCs in ACP-EU negotiations for EPAs.

Reflecting the continued difficulty faced by acceding LDCs, the Declaration reaffirmed the need for “a binding mechanism” to fast-track the LDC accession, “the urgent and effective implementation” and “precise interpretation” of the 2002 LDC Accession Guidelines.

On Enhanced Integrated Framework and Aid for Trade, the Declaration stressed the need for national ownership, additional predictable funding and expeditious approval of projects (EIF) and priorities to LDCs (Aft).

It is significant that the Declaration called for incorporating the development dimension of the Doha Round into the UN LDC-IV Conference.

Source: WTO, 2009.

measures and export subsidies, and the granting of DFQF market access for cotton and cotton by-products originating in LDCs (WTO, 2009: 2). As regards LDC WTO accession, the Dar es Salaam Declaration stressed the need to adopt a binding mechanism to fast-track the accession of LDCs, to avoid raising non-trade concerns, and to take immediate actions including the precise interpretation of the 2002 Decision.

Implementing these measures should not be made contingent on the completion of the Doha Round. Providing DFQF market access for LDCs is also part of Goal 8 of the MDGs, and its accelerated implementation would be an important aspect of strengthening the Global Partnership for Development between 2010 and 2015, even though it has been negotiated under the auspices of the WTO Doha Round. This is ample reason for urgent implementation of this proposal without waiting for completion of that Round.⁶

(b) Improving the commercial benefits of preferential market access for goods

At the Hong Kong Ministerial Conference (WTO, 2005), it was agreed that developed country members of the WTO would allow 100 per cent duty-free quota-free (DFQF) access for all products originating from all LDCs without explicit timeframe. It was also agreed that at least 97 per cent of tariff lines on imports originating in LDCs to enter developed countries DFQF be provided by developed country member facing difficulties to provide 100 per cent DFQF market access by 2008 or by the start of the implementation period of the Doha Round results.

Measures enabling wide-ranging market access, combined with flexible rules of origin, could result in a substantial increase in LDCs' exports to both developed and other developing countries (Carrère and de Melo, 2009; Elliott, 2010). However, as discussed in chapter 2, the legal obligation of DFQF market access does not necessarily bring commercial benefits. To make preferential market access commercially advantageous for LDCs, a number of further measures should be taken.

First, the target for tariff line coverage of at least 97 per cent must be met as expeditiously as possible by all developed countries. Currently, this target has been met by all developed countries but the United States. According to data in Elliot (2010), the current product coverage of the United States' Generalized System of Preferences for LDCs (with the exception of the African Growth and Opportunity Act – AGOA, which covers some LDCs) has product coverage of only 83 per cent. Therefore, it is still possible to substantially improve the preferential market access of LDCs. In practice, the provision of DFQF access for 97 per cent of LDCs' exports of goods as soon as possible should be a matter of priority, and then all developed-country members of the WTO should move towards 100 per cent.

Second, even if 97 per cent target is achieved, given that LDCs' exports are very concentrated, it is possible that the remaining 3 per cent of tariff lines not covered by the DFQF access provision cover a substantial proportion of the exports of LDCs. In other words, it is possible that the products that matter most for LDCs would be excluded from the preferential market access programmes. That is certainly the case with regard to exports originating from the Asian LDCs that concentrate on apparel products. Thus, it is essential that developed countries ensure that when granting 97 per cent coverage, products of commercial interest to LDCs are effectively included in that coverage.

Third, progressing towards 100 per cent coverage in all developed countries must be accelerated. Since the Hong Kong Declaration did not specify target date by which to achieve the 100 per cent coverage, there is risk that the target, which it may be recalled was the ultimate goal of the Declaration, may be further delayed. To date, 100 per cent coverage has been achieved

Implementing the “early harvest” should not be made contingent on the completion of the Doha Round.

Measures enabling wide-ranging market access, combined with flexible rules of origin, could result in a substantial increase in LDCs' exports to both developed and other developing countries.

The target for tariff line coverage of at least 97 per cent must be met as expeditiously as possible by all developed countries.

Progress towards 100 per cent coverage in all developed countries must be accelerated.

only in some developed countries. Thus, it is imperative that momentum be maintained towards meeting this ultimate goal.

One study shows that extending DFQF coverage for 100 per cent in all OECD countries is expected to create an additional export gain of \$2 billion, and gains would be greater up to \$5 billion if major middle-income countries offer DFQF access.

Extending DFQF coverage for 100 per cent in all OECD countries is expected to create an additional export gain of \$2 billion, and gains would be greater up to \$5 billion if major middle-income countries offer DFQF access.⁷ In the United States, for example, an un-adopted draft legislation, “New Partnership for Trade Development Act of 2009 (HR. 4101)”, envisaged extending DFQF benefits for all products from all LDCs.

At the same time, extending product coverage to 100 per cent will affect exports of African countries in the US market as they will experience erosion of AGOA trade preferences, especially its apparel benefits (see box 9). It is thus important to address meaningfully adjustment challenges for certain sub-Saharan African countries, and measures for enhancing their competitiveness would be essential. Innovative mechanism needs to be explored towards addressing such adjustment challenges.

Developing-country members of the WTO in a position to do so could usefully provide trade preferences to LDCs which are expected to generate significant gains given their increasing importance as export markets for a number of LDCs.

In addition, developing-country members of the WTO in a position to do so could usefully provide trade preferences to LDCs which are expected to generate significant gains given their increasing importance as export markets for a number of LDCs. There has been a number of initiatives recently in that direction, including by India, China and Brazil. China improved its market access conditions regarding 30 African LDCs. It would phase in zero-tariff treatment to 95 per cent of tariff lines for them within 3 years starting with 60 per cent in 2010. India grants preferential market access for all 49 LDCs. Effective in 2008, it grants duty-free treatment on 85 per cent of tariff lines with progressive tariff elimination over five years. Brazil announced its intention in 2009 to grant DFQF access for LDCs covering 80 per cent of all tariff lines by mid-2010 and to cover all tariff lines by 2014. Other developing countries should follow suit and strive to provide DFQF access to LDCs by 2015, the year MDGs should be accomplished.

Box 9. Selected issues in DFQF market access^a

Product coverage and simplified Rules of Origin (RoO) are two major issues regarding DFQF. In United States, AGOA benefits for Sub-Saharan Africa (SSA) are significant for those receiving apparel benefits because preferential margin is large and existing preferences are fully used by eligible exporters. In contrast, Asian LDCs trading under normal GSP scheme do not enjoy similar preferences. This implies scope for improvement by extending product coverage for Asian LDCs. UNCTAD's estimates show that full coverage would increase the value of preferences (i.e. tariff rent) from \$1.4 million to \$555 million for Bangladesh. Extending DFQF to 100 per cent of products would however induce preference erosion for SSA. Trade simulation analysis using SMART model suggests that while it will increase Bangladesh's exports by \$847 million and Cambodia's by \$555 million, or 23 per cent and 28 per cent of their pre-policy-change export levels respectively, Lesotho, Madagascar, Kenya, Mauritius and Swaziland will see a decrease in exports in the range of \$3-6 million or 1.6 per cent to 1.9 per cent of their pre-policy-change exports.

RoO are significant in affecting LDCs' ability to effectively utilize existing trade preferences. In the EU, which now provides DFQF treatment for all products under EBA, a key issue under consideration is reforming its preferential RoO. UNCTAD estimates find that the utilization of EBA preferences by 41 LDCs eligible only for EBA was 81 percent in 2008. This rate is contrasted with the higher utilization of 9 ACP-LDCs that had formed EPAs with EU (98%), thus using EPA RoO. Relatively low utilization for EBA-only LDC41 is largely explained by 8 Asian LDCs, owing to their reliance on apparel products which faced relatively stringent RoO in the EU market, requiring them to assemble apparels from yarn, and not from fabric ("double transformation"). New RoO are currently being formulated to help LDCs increase utilization.

^a “Evolution of the international trading system and of international trade from a development perspective: The impact of the crisis-mitigation measures and prospects for recovery (TD/B/57/3)” and “International trade and development: Report of the Secretary-General (A/65/211)”.

Another problem of the preferential market access is that it is unilateral and potentially subject to abrupt changes. Thus, the Hong Kong Declaration specifies that the preferential market access for LDCs should be made long-lasting. Stability and predictability of market access would encourage investments by both domestic and foreign investors in sectors that have export potential. Preference-granting countries may be urged to enact their preferential scheme as at a longest time span as possible so as to ensure stability, security and predictability in their schemes.

In addition, rules of origin have been identified as one of the main obstacles for full utilization of the preferential market access. Therefore, rules of origin for LDCs' exports should be liberalized, simplified and made more transparent in accordance with the Hong Kong Declaration (see box 10).

Finally, new, innovative ways to make preferential market access for the exports from LDCs commercially meaningful should be explored. For example, developed countries could encourage their domestic firms through the provision of favourable tax treatment or grant support for partial cost-coverage to develop supply sources in the LDCs. This would enable the LDCs to take advantage of the preferential market access they have been offered but are at present unable to exploit due to their insufficient supply-side capacity (Mistry and Olesen, 2003). Another possibility is to encourage developing-country investors to invest in LDCs to take advantage of LDCs' preferential market access. This form of South-South cooperation could strengthen development in both LDCs and other developing countries. DFQF initiatives could also be linked with support measures aimed at building productive

Preference-granting countries may be urged to enact their preferential scheme as at a longest time span as possible to ensure stability, security and predictability in their schemes.

Rules of origin for LDCs' exports should be liberalized, simplified and made more transparent.

Box 10. Rules of origin

The mere granting of tariff preferences or duty-free market access to exports originating in LDCs does not automatically ensure that the trade preferences will be effectively utilized. Preferences are conditional on compliance with rules of origin requirements. The function of rules of origin is to reduce the risk of trade diversion, and to ensure that the benefits of tariff reductions under those rules apply to products genuinely manufactured or grown in countries that enjoy trade preferences. However, several studies have shown that excessively stringent rules of origin lead to low levels of utilization (see, for example, UNCTAD, 2003; and Persson and Wilhelmsson, 2006).

Moreover, successive rounds of negotiations in GATT/WTO have substantially lowered the preferential margin since the 1970s, and hence the need for stringent rules of origin is simply anachronistic. Finally, major preference-giving countries believe these rules to be outdated, as stated by the European Commission (2007): "Rules of origin are old and have not followed evolutions in world trade. The present rules were initially drawn up in the 1970s and they have not materially changed much since, whereas the commercial world has."

The LDCs managed to include a formulation on rules of origin in the Hong Kong Ministerial Declaration, wherein WTO members agreed to: "ensure that preferential rules of origin applicable to imports from LDCs are transparent and simple, and contribute to facilitating market access." Although useful, that formulation did not specify what the rules of origin should be, nor did it address their impact on the utilization of trade preferences.^a

The LDCs are currently reviewing a proposal for an across-the-board rule of origin based on a percentage criterion. This would require a calculation of the value of material used in the manufacturing of a given product, which would avoid the shortcomings of other kinds of calculations and it would also avoid the proliferation of product-specific rules of origin by product line. In addition, the calculation methodology takes into account the cost of transport of inputs to the LDCs. This is a factor that unduly penalizes them, especially the island and landlocked LDCs.

The proposal has given particular attention to the setting of the level of percentages on the basis of field findings from a questionnaire answered by enterprises from Eastern and Southern Africa, and using a methodology developed by UNCTAD (2003). This methodology has also been used by the European Commission (2007) in setting the percentages in the proposed new preferential rules of origin for GSP, including for its Everything-but-Arms initiative, which are under consideration for adoption in the EU. The Commission found that by lowering the threshold from a level of 55–60 per cent to 30–45 per cent, full utilization would be achieved with total trade effects roughly three times greater than if the upper threshold were used. Even greater trade effects could be expected in the case of the LDC proposal where the percentage levels are set at 15–25 per cent.

^a Rules of Origin and Origin Procedures Applicable to LDC Exports (UNCTAD/DITC/TNCD/2009/4).

capacities, facilitating integration into supply chains, promoting trade and competitiveness in beneficiary LDCs such as Aid for Trade.⁸

Preferential treatment of LDCs in respect of services is less likely to cause trade diversion for other developing countries since it is more likely to be new access, and it would not entail government revenue loss unlike trade in goods.

(c) Preferential market access for LDC services exports

Services represent an additional promising area for granting preferential market access to LDCs. In accordance with the Modalities for special treatment for LDCs in service negotiations adopted in 2003 (WTO, 2003a), WTO members are considering “a waiver, available to all Members, from the obligations of Article II, paragraph 1 of the GATS in respect of preferential treatment benefiting all LDC Members” in providing such a mechanism. Thus, early harvest of a waiver decision can be a reasonable way forward. The challenge remains on effectively securing preferential market access opportunities such as in Mode 4 (movement of natural persons) under the waiver.

Service sector development and trade, such as tourism, movement of service suppliers and IT-related services, could become powerful drivers of national development.

Preferential treatment of LDCs in respect of services would likely be welfare enhancing. It is less likely to cause trade diversion for other developing countries since it is more likely to be new access, and it would not entail government revenue loss unlike trade in goods. Significant preference could be offered, given that the existing barriers are prohibitive or quite high. Such access would also give a stronger boost to LDCs’ economic diversification. Service sector development and trade, such as tourism, movement of service suppliers and IT-related services, could become powerful drivers of local and even national development.

Provisions of services through Mode 4, and broader labour movement, covering all skill categories, as well as facilitated recognition of qualification, would be important.

Service exports in the form of Mode 4 are another promising area. Migration to cities and the inability of the labour market to absorb newcomers have resulted in increasing levels of emigration from LDCs. If employment opportunities in LDCs do not improve, that outward flow is likely to grow even further. Thus, provisions of services through Mode 4, and broader labour movement, covering all skill categories, as well as facilitated recognition of qualification, would be important. The rising importance of remittances in many LDCs indicates that the process of spontaneous emigration is already well under way. It also shows that there are benefits for both home and host countries. For the home country, the benefits from emigration include remittances and payments to workers, alleviation of the pressure on the domestic labour market, and opportunities for the transfer back to the home country of ideas and technologies. For host countries, in particular developed ones, foreign workers compensate for the scarcity of less skilled workers.

Members of the WTO could improve market access conditions for LDCs’ services exports, especially those falling under Mode 4, including through the provision of temporary visa schemes.

A more organized process of delivering labour services under Mode 4 could potentially increase these benefits for both. Liberalization of 3 per cent of OECD countries’ labour market is estimated to bring global welfare gains of \$156 billion. The contribution of Mode 4, and broader labour movement, to development is significant as global labour migrants continue to rise as a channel for transfer of skills and ideas. Mode 4 remains relatively restricted due to concern over its impact on domestic labour market, allowing only intra-corporate transferees and business visitors/services salesperson. While inclusion of new categories of services suppliers are under consideration by a few countries, offers have so far fallen far short of expectations from developing countries and LDCs in terms of sectoral coverage, removal of quota and economic needs test/labour market test and facilitation of administrative procedures for entries of Mode 4 services suppliers.

Thus, members of the WTO could improve market access conditions for LDCs’ services exports, especially those falling under Mode 4, including

through the provision of temporary visa schemes. A waiver decision on preferential and more favourable treatment to services and service suppliers of LDCs is therefore important.

(d) Accession to the WTO

The accession process of LDCs to the WTO is cumbersome and slow. Moreover, the accession process has often led to commitments that are deeper and more stringent than those applicable to existing WTO members, with the result that acceding countries' policy flexibilities are reduced substantially while certain SDT provisions such as transitional periods are subject to negotiations on a case-by-case basis. Since acceding countries are in a weaker bargaining position as they seek the membership, concern emerged to streamlining and improving the accession process to make it fairer and more balanced.

Although this aberration is not part of the LDC Ministers' proposed "early harvest", the process of accession could be quickly changed by the significant improvement and prompt and effective implementation by the WTO members of the Decision on the Accession of LDCs of December 2002 (WTO, 2003), to be supported by adequate institutional arrangements, transparency and follow-up mechanisms. A fundamental issue is that the WTO Agreement Article XII does not provide any guidance apart from saying accession should be done "on terms to be agreed". This has been significant challenge for LDCs. This is why the Dar es Salaam Declaration proposed various initiatives, including "precise interpretation of 2002 Decision" with a view to its improvement. So what is needed seem to be not only implementation of the Decision but also improvement, and some practical follow-up mechanism.

In particular:

- Accession of LDCs to the WTO should be facilitated, and should be made consistent with LDCs' development status. In other words, new LDC members should not be forced to accept more onerous commitments than the existing LDC members. Instead, the WTO member States should automatically grant all LDCs the right to benefit from the SDT provisions contained in WTO agreements, and refrain from seeking market accession concessions taking into account the levels of concessions and commitments undertaken by existing WTO LDCs' Members (2002 Decision). This could be promoted by adopting a binding mechanism for fast-track mechanism for the accession of LDCs.
- WTO members should adopt a rule that the LDC accession process be completed within a shortest period of time, e.g., three-year period. This could be made feasible by the automatic granting of SDT to all LDCs at the start of negotiations, which would substantially reduce the length of the process.
- WTO members should simplify the process of accession for LDCs by avoiding unnecessary procedures. This would also reduce the length of the process.

2. EMPOWERING LDCs TO USE FLEXIBILITIES PROVIDED UNDER WTO RULES

Improved market access can potentially help LDCs, but it is economically irrelevant unless they are able to take advantage of that opportunity. This

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Accession of LDCs to the WTO should be facilitated, and should be made consistent with LDCs' development status.

The WTO member States should automatically grant all LDCs the right to benefit from the SDT provisions contained in WTO agreements, and refrain from seeking market accession concessions above the levels undertaken by existing WTO LDC Members.

WTO members should adopt a rule that the LDC accession process be completed within a shortest period of time.

depends on policies and finance, which are the subjects of this present and subsequent section.

LDCs need to develop what could be called a “strategic trade policy”, as opposed to the current trade policy of maximizing trade liberalisation as an end in itself.

As argued in chapter 3 and earlier in more detail by UNCTAD (2004), rapid and comprehensive trade liberalization in the LDCs has not had the desired effects, given the very low level of development of their productive capacities and their large productivity gap with other countries. LDCs need to develop what could be called a “strategic trade policy”, as opposed to the current trade policy of maximizing trade liberalisation as an end in itself. That kind of new trade policy is needed to support their development and poverty reduction efforts. It would have to be compatible with the new post-crisis global macroeconomic environment and would take advantage of the new opportunities associated with South-South trade. They should be given the necessary support to enable them to use all the flexibilities already available under WTO rules to foster the development of their productive capacities and pursue their strategic integration into the global economy.

The first step towards promoting LDCs’ fuller participation in the multilateral trading system, consistent with their wider development goals, is to empower LDCs to use all the policy space currently available to them under the existing multilateral trade regime.

Strategic integration into the global economy means starting at the development end rather than at the trade end of the relationship between trade and development (UNCTAD, 2006a). The first step towards promoting LDCs’ fuller participation in the multilateral trading system, consistent with their wider development goals, is to empower LDCs to use all the policy space currently available to them under the existing multilateral trade regime. In practice, at present most LDCs do not use all the policy space permitted *de jure* under the prevailing rules of the game. Furthermore, proliferation of RTAs, especially North-South RTAs, have meant policy space available for LDCs under WTO are being overridden or bypassed by deeper and broader commitments under such agreements. WTO accession has also led to WTO-plus commitments for acceding LDCs. The next step is to ensure that the flexibilities provided under SDT are genuinely supportive of the development of productive capacities.

(a) Using available flexibilities

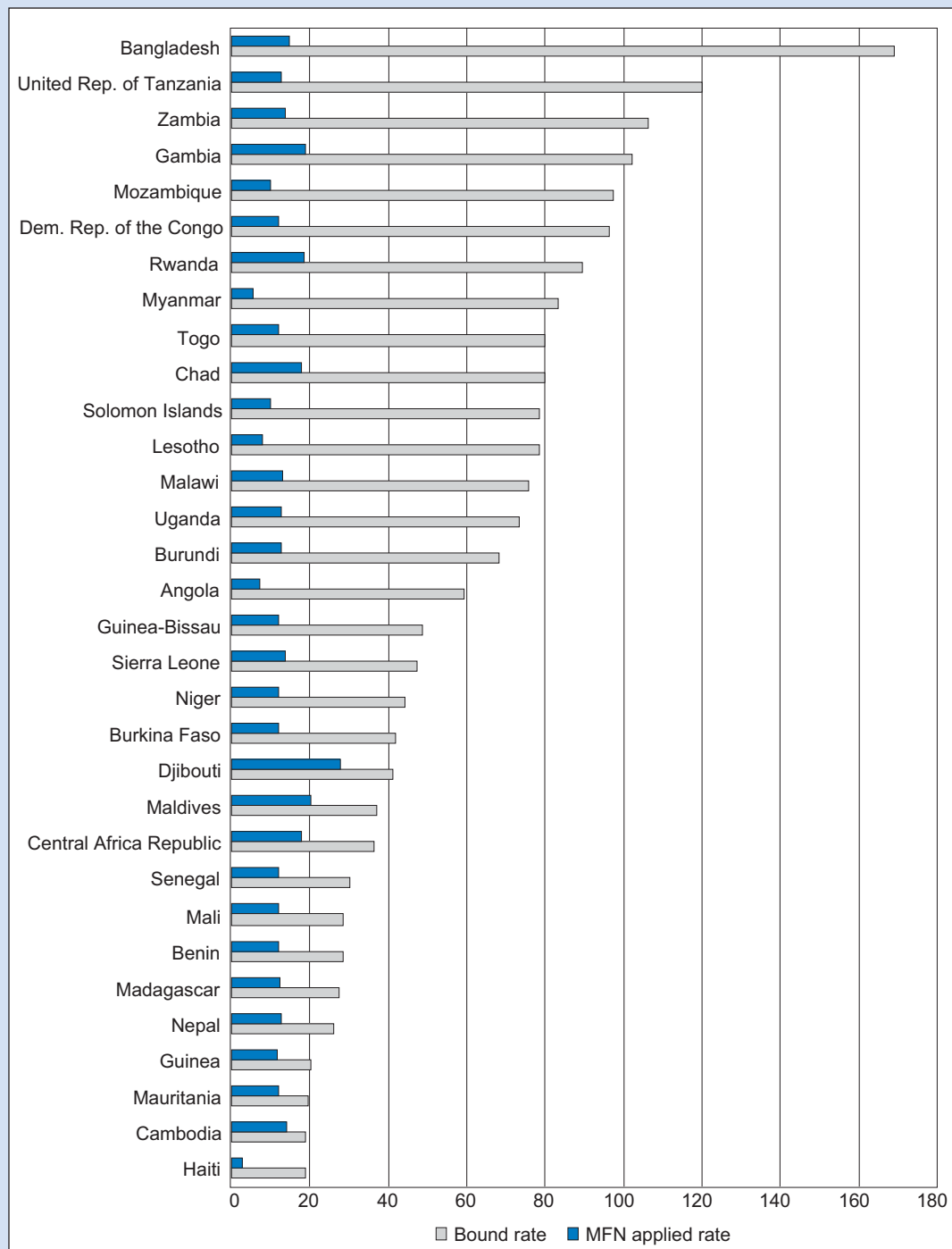
LDCs do not utilize all the flexibilities under the WTO rules and all the policy space available to them partly because of the propagation of one-size-fits-all policies via structural adjustment programmes and the conditionalities attached to financial support from the IFIs, including debt relief.

An example, and probably the most important one, of how LDCs do not use available flexibilities at present is the large gap between bound and applied tariff rates in LDCs. This difference, called “tariff overhang” or “tariff water”, is indicative of the degree of flexibility each member of the WTO has within the current rules. Foletti et al. (2009) find that LDCs have relatively large policy space regarding the “water”, but they do not use it. The bound tariff rates of LDC WTO members are mostly higher than 40 per cent, and in some cases even much higher (chart 35). However, the applied tariff rates are much lower. The gap between the two is very pronounced, which means they could, in principle, use tariff instruments for trade development much more actively than they are currently doing.

LDCs do not utilize all the flexibilities under the WTO rules and all the policy space available to them partly because of the propagation of one-size-fits-all policies via structural adjustment programmes and the conditionalities attached to financial support from the IFIs, including debt relief. Buirra (2003) notes that the weaker the recipient country, the more likely it is that conditionality will lead to an imposition of IMF policies. According to Paul Volcker, former Governor of the Federal Reserve Board, “When the Fund consults with a poor and weak country, the country gets in line. When it consults with a big and strong country, the Fund gets in line” (cited in Buirra,

Chart 35

Bound and applied MFN tariffs of LDC WTO members
(Per cent)



Source: WTO, ITC and UNCTAD (2009) and UNCTAD secretariat calculations based on data from the WTO Tariff Download Facility (http://www.wto.org/english/tratop_e/tariffs_e/tariff_data_e.htm).

2003: 4). This clearly reflects the asymmetry in the current international governance architecture, and partly explains why LDCs undertook such rapid and extensive unilateral trade liberalization in the 1990s. In addition, bilateral free trade agreements with developed countries are another, even more powerful constraint on LDCs' use of the existing policy space for development purposes (UNCTAD, 2009c).

The Dar es Salaam Declaration calls for efforts to ensure that coherence between the WTO and IFIs, in line with the rights and flexibilities that LDCs have obtained under the WTO, be fully operationalized to support LDCs' development objectives.

A new strategic trade policy should first give priority to supporting agricultural production and, second, to selective promotion of new activities that will enable economic diversification and gradual development of international competitiveness.

The international community should strive to enable LDCs to pursue a more proactive agricultural policy using all the policy instruments available, including tariff and non-tariff measures, to increase their food security and stimulate production for exports.

LDCs should be enabled and encouraged to adopt a strategic trade policy within a broader set of policies aimed at developing their productive capacities and increasing employment opportunities. It is important to emphasize that the Dar es Salaam Declaration calls for efforts to ensure that coherence between the WTO and IFIs, in line with the rights and flexibilities that LDCs have obtained under the WTO, be fully operationalized to support LDCs' development objectives.

Ideally, the speed and degree of trade liberalization should take into account, first and foremost, the goal of developing LDCs' productive capacities. However, given the very open trade regimes of most of the LDCs, that option is no longer available to them. Instead, a new strategic trade policy should first give priority to supporting agricultural production and, second, to selective promotion of new activities that will enable economic diversification and the gradual development of international competitiveness.

(i) Strengthening agricultural production in LDCs

Trade liberalization, coupled with agricultural subsidies in developed countries, has seriously reduced the incentives of LDCs to produce and export agricultural products.⁹ It is important that developed countries remove trade-distorting agricultural subsidies on goods that compete with LDC exports, most notably rice, sugar and cotton. In addition, the international community should strive to enable LDCs to pursue a more proactive agricultural policy using all the policy instruments available, including tariff and non-tariff measures, to increase their food security and stimulate production for exports. It will be difficult to promote a new Green Revolution in staple food productivity in LDCs in the absence of an appropriate agricultural trade policy.

(ii) Promoting new activities through the selective use of industrial and trade policies

Carefully managed strategic integration into the global economy should also include the use of trade policy to accelerate industrialization and diversification of the economy. It is necessary to move away from the existing pattern of integration that is based mainly on static comparative advantages. The choice of policy instruments in a dynamic process of structural change itself is bound to evolve over time. New, promising activities may merit time-bound infant industry support, while other, more mature sectors could be opened up to international competition. A reasonable trade policy for LDCs would be to remove the anti-export bias, if and where it still exists. At the same time, it would provide selective, temporary protection to economic activities that have the potential to increase exports or substitute imports, or both. Selective use of import tariffs for purposes of economic diversification is of greater value for LDCs than for developed countries, as the former lack public funds to provide subsidies or other types of incentives to promote new activities. Certain subsidies (tax incentives, tax expenditure, etc.), technology transfer or export performance requirements for investors, local content requirement in government procurement, might be implemented by resource-scarce LDCs as well.

Since various LDCs, most notably in Asia, are in the early stages of industrialization, the production and export of labour-intensive, low-skill manufactures has already brought substantial benefits, such as increased employment, higher incomes and productivity, and the upgrading of basic techniques and organizational skills. Some of them now participate in global

value chains by taking on some of the more labour-intensive segments of production of TNCs, mainly because of their very low labour costs. Others have tried to establish their own firms in these production segments. Both options should be encouraged and extended to all LDCs. However, these measures by themselves do not guarantee a shift towards a permanent path of rapid and sustained development. They should be viewed as only a first step in that direction. Labour-intensive exports have clear limits, as they are also subject to the fallacy of composition.¹⁰ Therefore, technological upgrading in manufacturing, as well as in other sectors, is necessary for shifting production and exports to higher value-added and skill-intensive products.

Countries that successfully increase their low-wage, labour-intensive production and exports should gradually adopt policies designed to replace imported skill- and technology-intensive parts and components with domestically produced ones to raise the domestic value-added content of their exports. This would require a different approach to trade policy than has hitherto been pursued. It would also require a set of complementary policies, notably those concerning technological upgrading, to be able to move to the next stage of development (see chapter 6). The overall aim should be to combine selective, time-bound protection and export promotion as integral parts of a single strategy aimed at accelerating investment, income and productivity growth in the long run (box 11).

When devising a strategic trade policy, important lessons can be learnt to avoid the pitfalls of the earlier import-substitution experiences of many countries, particularly those in Latin America. For example, if certain sectors continue to be protected for too long, the result could be inefficiency and rent seeking. The experiences of successful latecomers, especially in East

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Box 11. Trade policy and the optimal degree of openness of LDCs

Bhaduri (2005) and Akyüz (2009) argue that openness should not be independent of time and space as it is under the present free trade paradigm. Instead, it should take into account each country's stage of development and the direction in which it is trying to steer its economy. These highly specific circumstances therefore require the multilateral trade regime to be flexible enough to allow all countries to reach their "ideal" level of openness suited to their conditions at a particular juncture. It should also be based on the principle of non-reciprocity, to allow LDCs to shield some of their activities from the competition they are not yet prepared to face.

Ideally, such a regime should allow domestic producers to acquire inputs at world prices (i.e. tariff-free inputs), while protecting those producers against damaging competition from abroad. Operationally, this calls for a selective and differentiated tariff structure, where inputs are exempt from import duties while tariff rates on goods that compete with domestic production are raised. Imports of luxury consumer goods should also be subject to the highest tariffs possible under the WTO rules, while imports of food not produced domestically should be duty free. In addition, domestic agricultural production of LDCs should be shielded from foreign competitors, many of which are from developed countries and receive large subsidies by their Governments.

Concerning the development of productive capacities, it makes little sense to levy tariffs on all imports, since LDCs do not produce many of these products. Instead, tariffs should be imposed on the types of products where LDCs have a reasonable chance of developing their own production. Tariffs on capital goods and most machinery at the early stages of industrialization are counterproductive: since they have to be imported, they would be unaffordable if subject to tariffs and would thereby deprive the economy of essential means of production. In order to promote import substituting production, tariffs on imported goods that could be produced domestically, and which either raise value added or are labour-intensive, should be increased to ensure a reasonable period of learning and experimentation by local producers. This would help to enhance productive capacities in the long run, diversify the productive structure and create jobs, thereby reducing pressures on the labour market.

For LDCs to be able to adopt these instruments of trade policy, the WTO rules would have to be interpreted more flexibly to allow LDCs a more active use of promotion measures – both tariffs and non-tariff ones – for LDCs' infant industries. This would give LDCs more policy space to shift from their heavy dependence on commodities to more diversified and higher value added production. Only then would it be possible for these countries to take fuller advantage of their preferential access to the markets of developed countries and integrate more favourably into the global economy.

Asia, show that different mechanisms, such as reciprocal control mechanisms, performance requirements and sunset clauses, could be effectively employed for avoiding these problems.

Even if the present institutional capacities of LDCs are not sufficiently advanced for them to implement a set of complex policies and instruments, this should not deter them. After all, at the time of their industrialization, many of today's developed countries did not have the same set of institutions they now have, but were able to catch up with leaders through a learning process. The consequences for LDCs of the application of one-size-fits-all policies have already been observed, especially with regard to trade liberalization, and the record is at best mixed. Therefore, it is time for them to look for other ways to achieve their development goals.

While the priority should be to enable LDCs to use available flexibilities, strengthening SDT should not be forgotten.

Another important consideration in devising a strategic trade policy should be given to regional economic integration initiatives. In general, LDCs are small countries with very small domestic markets, which means they are unable to benefit from economies of scale. This drawback can be overcome through regional economic integration, which provides a much larger market and offers LDCs an opportunity to export to other countries while being shielded to some extent from competition from the more advanced developing and developed countries. In addition, evidence suggests that intraregional trade, even among LDCs and/or low-income countries, usually has a higher technological content than North-South trade (chapter 4). Thus, LDCs should strive to strengthen the existing regional integration schemes among partners at similar levels of development, and engage more forcefully in South-South cooperation, as argued in chapter 7. This would help increase the policy space of these countries regionally.

In sum, LDCs need all the flexibilities provided under the multilateral trading rules in order to spur development of their productive capacities. Such flexibilities should be firmly secured for them and should not be diluted by RTAs or WTO accession processes. Empowering them to use these flexibilities should be made the overarching feature of the international community's support for the development of these countries.

A major problem is that the transition period in SDT is not related in any meaningful way to the capacity of individual LDCs to produce and export, and to their overall level of development.

(b) Strengthening special and differential treatment for LDCs

As discussed in chapter 2, the SDT provisions for LDCs in WTO agreements mainly take the form of longer transition periods so that they are not immediately exposed to multilateral disciplines. However, the length of the transition period is currently completely arbitrary. For example, in the TRIPS Agreement, the transition period for LDCs was 11 years from the date of entry into force (1 January 1995), and was extended in 2005 until 1 July 2013. A major problem is that the transition period is not related in any meaningful way to the capacity of individual LDCs to produce and export, and to their overall level of development. It would be possible to improve SDT for LDCs if the transition periods granted to LDCs for non-application of WTO rules were linked to objective economic and social criteria, rather than to fixed time frames as is currently the case. Thus, while the priority should be to enable LDCs to use available flexibilities, strengthening SDT should not be forgotten.

3. ACCELERATING THE PROVISION OF AID FOR TRADE

Finance is also critical for trade development and for enabling LDCs to take advantage of market access opportunities. As shown in chapter 2, the EIF offers an important operational mechanism for ensuring that aid for trade development in the LDCs is focused on priority activities and is integrated within national development and poverty reduction strategies. However, thus far, the flow of aid for trade, using the OECD statistical definition of this category, has been increasing more slowly in LDCs than in other developing countries. A priority international support mechanism for LDCs should be to accelerate the flow of aid for trade to LDCs, and ensure that it is directed at enhancing their productive capacities and international competitiveness. Trade capacity-building should be seen as part of the wider objective of developing LDCs' productive sectors and promoting the development of their private sectors.

As the Diagnostic Trade Integration Study (DTIS) is the basic building block of the EIF, it is clear that its content is vital for the overall outcome of the process of mainstreaming trade into national development strategies. In this regard, it is necessary to elaborate appropriate methodologies for mainstreaming trade into development and poverty reduction strategies. UNCTAD (2004) offers an approach which places the balance of trade, export and import forecasts and the growth elasticity of poverty reduction at the centre of policy analysis for the purpose of identifying trade policy options.

Special care needs to be taken to ensure that the DTIS is carried out in a way that promotes country ownership. This can be facilitated through technical support for the establishment of an efficient trade-policy-making process within LDCs in which: (i) the country's trade interests are clearly identified within an overall development strategy; (ii) those interests are translated into policies and negotiating goals; and (iii) roles are distributed and resources allocated for implementation of those policies and promotion of those interests (Solignac Lecomte, 2003: 3). Inter-ministerial coordination across a range of government ministries, as well as consultation with the private sector, are a vital part of this process (Saner, 2010).

In general, it is clear that trade facilitation which reduces the transaction costs that are currently inhibiting trade flows is an important element that needs to be financed. However, it is necessary to go beyond the technical assistance that facilitates trade to also supporting national policies geared to increasing the supply capacity of LDCs. An important component would be to help LDCs develop more dynamic and diversified economies by reducing their commodity dependence, increasing their local value added and developing their technological capabilities. Finance is required for promoting sustainable agriculture in LDCs, and for boosting their manufacturing and services sectors as well as for improving their trade-related infrastructures, especially transport and communications. Some of the priority actions which could be supported to promote resource-based diversification and technological development are discussed in the next chapter.

A priority international support mechanism for LDCs should be to accelerate the flow of aid for trade to LDCs, and ensure that it is directed at enhancing their productive capacities and international competitiveness.

It is clear that trade facilitation which reduces the transaction costs that are currently inhibiting trade flows is an important element that needs to be financed. However, it is necessary to go beyond the technical assistance that facilitates trade to also supporting national policies geared to increasing the supply capacity of LDCs.

Notes

- 1 For a discussion on the practicalities of domestic resource mobilization in Africa, see UNCTAD, 2009a.
- 2 This and the next section draw largely on Culpeper, 2010.
- 3 The increase in 2009 included both the SDR 161.2 billion recommended by the G-20 plus a special allocation of SDR 21.5 billion, proposed in 1997 under the Fourth Amendment of the IMF Articles, to allow all members to participate equitably in the SDR system, even if they joined the Fund after prior SDR allocations.
- 4 “IDA-only” are countries with the GNI per capita below \$1,165, eligible for interest-free credits and grants from the International Development Association, while “blend” countries are IDA-eligible based on per capita income levels, but are also creditworthy for some IBRD borrowing.
- 5 Addressing cotton ambitiously, expeditiously, and specifically is the stated objective of the WTO membership since July 2004 (July 2004 Package). Cotton issue enjoys a wide-spread strong support from the LDC Group, as well as Africa, ACP, G20 and some developed countries as “litmus test” for the development dimension of the Doha Round. Cotton-4 has proposed specific formula to reduce cotton domestic support which remains to be agreed. The outstanding issue is the ability of the US to reduce domestic support, particularly product-specific limit on blue box support which US has argued could only be determined after agreement on a general reduction formula on domestic support, and subject to better market access opportunities in large emerging economies.
- 6 This idea was initially proposed by the Center for Global Development (Elliott, 2010).
- 7 Bouët et al. 2010.
- 8 Such support mechanism was proposed in the above mentioned draft US legislation (HR 4101).
- 9 A good example is rice production in Haiti (for details, see UNCTAD, 2010b).
- 10 “Fallacy of composition” refers to a situation where a strategy that is good for one producer or one country turns out to be bad if this same strategy is used by all of them at the same time.

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