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# Midterm Review of the Istanbul Programme of Action: From the Istanbul Programme of Action to the 2030 Agenda for Sustainable Development

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## FINANCING STRATEGIES FOR LDCs GRADUATION IN ASIA AND THE PACIFIC: KEY SOURCES, TRENDS AND PROSPECTS

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# FINANCING STRATEGIES FOR LDCs GRADUATION IN ASIA AND THE PACIFIC: KEY SOURCES, TRENDS AND PROSPECTS

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Macroeconomic Policy and Financing for Development Division

# FINANCING STRATEGIES FOR LDCS GRADUATION IN ASIA AND THE PACIFIC: KEY SOURCES, TRENDS AND PROSPECTS*

by

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## Abstract

The United Nations recognizes that productivity capacity-building is key for self-sustained growth and graduation of least developed countries (LDCs) in Asia and the Pacific. To achieve this objective, substantial financing must be mobilized to invest in infrastructure, social development and climate change challenges. Despite the significant progress made by the Asia-Pacific LDCs in restoring macroeconomic stability, deepening the banking sector and attracting foreign direct investment (FDI) and remittances, for many of them, fiscal spaces remain narrow and their financial markets are largely inefficient and undiversified. An ambitious financing strategy is needed to close the financing gap for graduation and to promote sustainable development, which includes strengthening fiscal space, financial intermediation and exploring innovative financing mechanisms, such as blended finance, promoting new forms of development partnership and climate finance. In particular, the paper shows that an estimated $19 billion could be raised annually by Asia-Pacific LDCs through targeted efforts to broaden tax bases, create an enabling environment for FDI and reduce transaction costs of remittances, among others. An additional $15 billion could further be raised if Development Assistance Committee (DAC) members fulfil their commitment to contribute 0.15-0.20 per cent of gross national income for the development of LDCs.

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## I. Introduction

In May 2011, at the Fourth United Nations Conference on the Least Developed Countries (LDCs),[1] adopted the Programme of Action for the Least Developed Countries for the Decade 2011-2020, which called upon the global community to commit to a "renewed and strengthened partnership for development" that would allow the LDCs to progress towards closing financing gaps for graduation, in combination with national policies and international support measures. The Istanbul Programme of Action explicitly stated that during the course of this decade, the action plan would focus on the objectives with the "aim of enabling half the number of least developed countries to meet the criteria for graduation by 2020" (United Nations, 2011).

The ESCAP Commission in its resolution 70/1 also agreed "to assist countries with special needs, especially least developed countries, landlocked developing countries and small island developing States, in taking advantage of opportunities arising from regional economic cooperation and integration, including, as appropriate, through support to enhance their capacities and through technical assistance". It further recognized that "there is a need to implement specific policies that focus on productive capacity-building related to infrastructure development, broadening the economic base, *access to finance* and providing assistance in overcoming the risks and shocks of entering into a regional trade block".

Least developed countries as a group continue to have the lowest per capita incomes in the Asia-Pacific region. Moreover, the income gap with developed economies has increased significantly in recent decades (figure 1), as the region also one of the highest population growth rates.

Most importantly, LDCs lack productive capacity due to limited development in the following areas: infrastructure (such as electricity, transport, information and communications technology (ICT), water, human and institutional capacity), energy (both production and access to energy), science and technology (for instance, to acquire technologies, skills and innovation) and the private sector, namely one that is dynamic, broad-based, well-functioning and socially responsible. Those features have considerably inhibited LDCs from meeting many of the internationally agreed development goals, including the Millennium Development Goals, such that most LDC in the region rank close to the bottom of the Human Development Index. Furthermore, they have also made it difficult for LDCs to progress towards structural transformation and to build adequate resilience against economic vulnerability. These are also added challenges in implementing the ambitions and transformative 2030 Agenda for Sustainable Development.

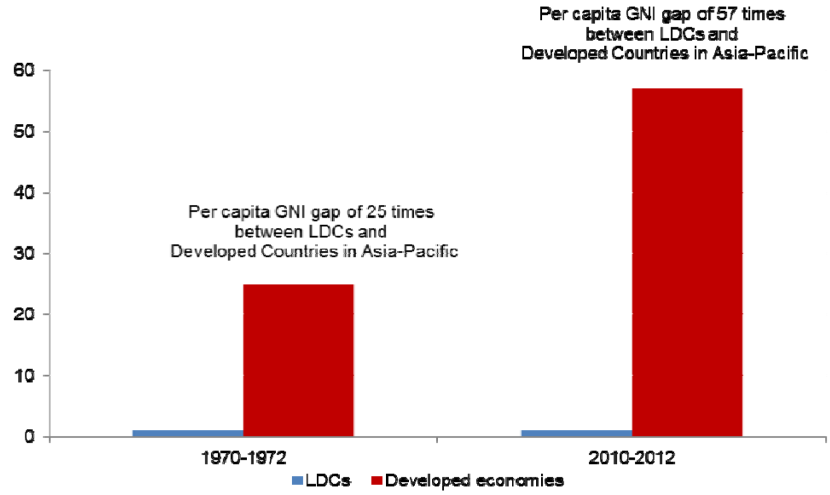
The graduation of LDCs requires making progress in three criteria: gross national income (GNI); human assets; and economic vulnerability to external shocks. Apart from increasing GNI per

[1] The current list of LDCs includes 48 countries (the newest member being South Sudan); 12 are in Asia and the Pacific. They are: Afghanistan; Bangladesh; Bhutan; Cambodia; Kiribati; Lao people's Democratic Republic; Myanmar; Nepal; Solomon Islands; Timor-Leste; Tuvalu; and Vanuatu.

capita, the other two criteria are measures of structural impediments in LDCs. For the Human Assets Index (HAI), the four indicators are based on the following: (a) nutrition: percentage of population undernourished; (b) health: mortality rate for children aged five years or under; (c) education: the gross secondary school enrolment ratio; and (d) adult literacy rate.

Similarly, for the Economic Vulnerability Index (EVI), the measure is based on indicators of (a) population size, (b) remoteness, (c) merchandise export concentration, (d) share of agriculture, forestry and fisheries in gross domestic product, (e) share of population living in low elevated coastal zones, (f) instability of exports of goods and services, (g) victims of natural disasters and (h) instability of agricultural production.

**Figure 1.** Income divergence between LDCs and developed economies of Asia-Pacific




*Source:* ESCAP calculations based on ESCAP Statistics online. Available from www.unescap.org/stat/data/statdb/DataExplorer.aspx (accessed 20 October 2014).

*Note:* LDCs-Asia-Pacific consists of 12 countries, developed economies consists of Japan, Australia and New Zealand (US Dollars at current prices).

The 2015 triennial review of the Committee for Development Policy (CDP)[2] shows that, although many LDCs in Asia and the Pacific are on the path towards graduation, most of the countries have not met the EVI criteria (box 1). With growing uncertainty in the global economic and financial markets, as well as concerns about the consequences of climate change, LDCs must be vigilant and need to focus on mobilizing significant resources, including climate finance, to reduce their economic vulnerability.

Apart from these structural impediments (ESCAP, 2014a), LDCs lack physical infrastructure and seamless connectivity within their national borders. This is inhibiting their productive capacity and reducing their prospects for creating "enabling business environments" for crowding in more private investment for long-term investment projects.

Against this background DESA (2014) stressed that "financing needs also differ across countries and regions. While financing needs are disproportionately large relative to the size of their

[2] The Committee for Development Policy (CDP), a subsidiary body of the United Nations Economic and Social Council, is, among other things, mandated to review the category of LDCs every three years and monitor their progress after graduation from the category. Available from http://unohrlls.org/about-ldcs/criteria-for-ldcs/.

economies in many developing countries, there are specific needs in least developed countries (LDCs)". For a country to reach thresholds in three criteria substantial financing is required, especially through public investment, among others sources, as indicated in ESCAP (2013). Therefore, strategies for mobilizing resources for financing the graduation gaps remain one of the critical areas for LDCs in the Asia-Pacific region.

**Box 1. Status of Asia-Pacific LDCs in the 2015 CDP Review**

The latest LDC review by CDP was conducted in March 2015. The current thresholds for graduation are GNI per capita $1,242 and above, in combination with the country meeting the HAI or EVI thresholds, or $2,484 for "income only" graduation, HAI 66 and above and EVI 32 and below. Among the twelve Asia and the Pacific LDCs, more than half are expected to meet the criteria for graduation if progress is maintained in the next few years.

**Afghanistan** remains below the threshold in the three criteria, with GNI per capita of $672, HAI of 43 and EVI of 35. Regarding **Bangladesh,** its GNI per capita ($926) remains below the graduation threshold, but its HAI (63.8) is very close to the graduation threshold; the country met the threshold on the EVI (25.1) over a decade ago. Bangladesh and Nepal are the only Asia-Pacific LDCs that have met the EVI criteria. **Bhutan** and **Nepal** have met the criteria for graduation for the first time and will be considered for possible graduation at the next triennial review of CPD. Bhutan has met the graduation threshold for GNI per capita ($2,277) and a HAI (67.2) criteria, however, EVI (40.2) has been persistently high in the last decade. On the other hand, Nepal has met the thresholds for HAI (68.7) and EVI (26.8), but its GNI per capita ($659) remains below the threshold and is the lowest among Asia-Pacific LDCs.

As for **Cambodia**, the GNI per capita ($ 852) is below the threshold, HAI (67.2) has already surpassed the threshold and with a fast decreasing EVI (38.3), the country is also on track to meet the criteria for graduation. Regarding **Myanmar**, GNI per capita ($1,063) is still below the threshold, but the country has met the threshold in HAI (72.7) and is on track to meet the threshold on EVI (33.7). The **Lao People's Democratic Republic** may meet the graduation thresholds for the next CPD review if continues to make steady progress, given its current GNI per capita ($1,232), HAI (60.8) and EVI (36.2). **Timor-Leste** also met the eligibility criteria for graduation for the first time in the "income-only" indicator (GNI per capita of $3,767), however the country lags behind in terms of HAI (57.4) and a very high economic vulnerability, with one of the highest EVI (55) among the world LDCs.

As for the LDCs that are also small island developing States, they all share a commonalty of meeting the criteria for graduation while having a very high economic vulnerability index. **Kiribati**, for example, met both the income and HAI criteria for the second time, but is the most vulnerable country in the world due to its EVI of 71.5. **Solomon Islands** met for the first time the graduation criteria, with GNI per capita of $1,402 and HAI of 71.7. However, even though it has been decreasing in the last few years, the EVI remains high (50.8). The country will be considered for possible graduation in the next review. In turn, **Tuvalu** has one of the highest income levels and the highest HAI among the world's LDCs (GNI per capita of $ 5,788) and a high HAI (88.8), meeting the thresholds by a large margin. CPD already recommended Tuvalu for graduation in previous review in 2012, however, following the same pattern of the Asia-Pacific small island developing States, the high level of vulnerability of the country (EVI of 54) is of great concern to the United Nations Economic and Social Council[a], which has postponed the recommendation for graduation twice. Finally, **Vanuatu** is scheduled to graduate from the LDC category in 2017, as it has met and continues to advance in GNI per capita, currently at

$2,997, and HAI (81.3), the two criteria in which the country was indicated for graduation, however, its (47.7) remains very high.

*Source*: ECOSOC (2015).
[a] ECOSOC Resolutions 2012/32 and 2013/20.

This paper argues that traditionally, LDCs experience lack of availability and access to financial resources from domestic as well as external sources, especially in international capital markets, to finance their graduation and overall development gaps. The paucity of financial resources often acts as an obstacle for them to increase their economic activity. It further reduces their potential for investing in human capital and reducing vulnerability from multiple shocks, such as higher energy prices or climate change, as recognized in the three criteria for the graduation of LDCs.

As underscored in the Istanbul Programme of Action, LDCs require an urgent action plan to improve their access to finance, which can support their special needs and priorities, together with enhanced policy coordination and development partnership, including in such areas as official development assistance (ODA), international trade, FDI and debt relief.

Apart from low levels of per capita income, the key challenges LDCs face in terms of mobilization of financing resources are related to low domestic savings and investment, especially in social sectors (figure 2) and physical infrastructure that is related to transport and trade (figure 3) and a small tax base.

**Figure 2**. Health expenditure in LDCs and other economies of the Asia-Pacific region, 2009-2011