

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

THE LEAST DEVELOPED COUNTRIES REPORT 2009

The State and Development Governance



UNITED NATIONS

EMBARGO

The contents of this Report
must not be quoted
summarized in the print, broadcast
or electronic media before
16 July 2009, 17:00 hours GMT



UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
Geneva

THE LEAST DEVELOPED COUNTRIES REPORT 2009

The State and Development Governance



UNITED NATIONS
New York and Geneva, 2009

Note

Symbols of United Nations documents are composed of capital letters with figures. Mention of such a symbol indicates a reference to a United Nations document.

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area, or of its authorities, or concerning the delimitation of its frontiers or boundaries.

Material in this publication may be freely quoted or reprinted, but full acknowledgement is requested. A copy of the publication containing the quotation or reprint should be sent to the UNCTAD secretariat at: Palais des Nations, CH-1211 Geneva 10, Switzerland.

The overview of this report can also be found on the Internet, in all six official languages of the United Nations, at www.unctad.org.

UNCTAD/LDC/2009

UNITED NATIONS PUBLICATION

Sales No. E.09.II.D.9

ISBN 978-92-1-112769-0

ISSN 0257-7550

What are the least developed countries?

Forty-nine countries are currently designated by the United Nations as “least developed countries” (LDCs). These are: Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, the Comoros, the Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People’s Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Maldives, Mali, Mauritania, Mozambique, Myanmar, Nepal, Niger, Rwanda, Samoa, Sao Tome and Principe, Senegal, Sierra Leone, the Solomon Islands, Somalia, Sudan, Timor-Leste, Togo, Tuvalu, Uganda, the United Republic of Tanzania, Vanuatu, Yemen and Zambia.

The list of LDCs is reviewed every three years by the United Nations Economic and Social Council, in the light of recommendations by the Committee for Development Policy (CDP). The following three criteria were used by the CDP in the latest review of the list of LDCs, which took place in March 2009:

- (a) the **“low-income”** criterion, based on a three-year average estimate of the gross national income (GNI) per capita, with a threshold of \$905 for addition to the list, and a threshold of \$1,086 for graduation from LDC status;
- (b) the **“human assets weakness”** criterion, involving a composite index (the Human Assets Index) based on indicators of: (i) nutrition (the percentage of the population that is undernourished); (ii) health (the child mortality rate); (iii) school enrolment (the gross secondary school enrolment rate); and (iv) literacy (the adult literacy rate); and
- (c) the **“economic vulnerability”** criterion, involving a composite index (the Economic Vulnerability Index) based on indicators of: (i) natural shocks (the index of the instability of agricultural production, and the share of the population displaced by natural disasters); (ii) trade shocks (the index of the instability of exports of goods and services); (iii) exposure to shocks (the share of agriculture, forestry and fisheries in GDP, and the index of merchandise export concentration); (iv) economic smallness (the population in logarithm); and (v) economic remoteness (the index of remoteness).

For all three criteria, different thresholds are used for identifying addition cases and graduation cases. A country will qualify to be added to the list of LDCs if it meets the addition thresholds on all three criteria and does not have a population greater than 75 million. Qualification for addition to the list will effectively lead to LDC status only if the government of the relevant country accepts this status. A country will normally qualify for graduation from LDC status if it has met the graduation thresholds under at least two of the three criteria in at least two consecutive triennial reviews of the list. However, if the GNI per capita of an LDC has risen to a level at least double that of the graduation threshold, the country will be deemed eligible for graduation regardless of its performance under the other two criteria.

Only two countries have so far graduated from LDC status: Botswana in December 1994, and Cape Verde in December 2007. Samoa is currently expected to graduate on 17 December 2010, and Maldives on 1 January 2011. In 2009, the CDP recommended that Equatorial Guinea be graduated from the list of LDCs.

After a recommendation by the CDP to graduate a country has been endorsed by the Economic and Social Council and the General Assembly, the graduating country is granted a three-year grace period before graduation effectively takes place. This grace period, during which the country remains an LDC, is designed to enable the graduating State and its development and trade partners to agree on a “smooth transition” strategy, so that the possible loss of LDC-specific concessions at the time of graduation does not disrupt the socio-economic progress of the country.

Acknowledgements

The Least Developed Countries Report 2009 was prepared by a team consisting of Zeljka Kozul-Wright (team leader), Alberto Amurgo Pacheco (until February 2009), Agnès Collardeau-Angley, Junior Davis, Marwan El Khoury (until March 2009), Madasamyraja Rajalingam, Rolf Traeger, Giovanni Valensisi (from March 2009) and Stefanie West. Nancy Biersteker, Lisa Borgatti, Pierre Encontre, Charles Gore, Massimiliano La Marca, Terry McKinley (consultant) and Paul Rayment (consultant) also made specific inputs to the Report. Simona Foltyn participated in the final stage of preparing the Report. The work was carried out under the overall supervision of Habib Ouane, Director, Division for Africa, Least Developed Countries and Special Programmes (ALDC), and Charles Gore, Head, Research and Policy Analysis Branch, ALDC.

An ad hoc expert group meeting on “The State, development governance and productive capacities”, was held in Geneva on 5 and 6 March 2009 to review a first draft of the Report and specific inputs. It brought together specialists in the fields of industrial policy, macroeconomic policy, agricultural development, international trade and development strategies. The participants in the meeting were: Heiner Flassbeck, Jörg Mayer, Terry McKinley, Anne Posthuma, Paul Rayment, Helen Shapiro, Servaas Storm, Gianni Vaggi and Giovanni Valensisi. The meeting discussed papers and inputs prepared by Junior Davis, Marwan El Khoury, Charles Gore, Zeljka Kozul-Wright, Massimiliano La Marca, Terry McKinley, Smita Srinivas and Rolf Traeger.

The Report draws on background papers prepared by John Di John, William Kalema and Frances Nsonzi, Paul Jourdan, Mushtaq Khan, Smita Srinivas, Morris Teubal and Ole Therkildsen. Initial thinking on the role of the State and governance issues in LDCs also benefited from in-depth discussions with Brian Van Arkadie — who acted as principal consultant in the preliminary stages of the project — and also Nguyuru Lipumba. Paul Rayment provided the substantive editing and contributed to the overall Report. The text was edited by Michael Gibson, Eleanor Loukass and Daniel Sanderson.

Secretarial support was provided at different times by Regina Ogunyinka, Sylvie Guy and Stefanie West. Hadrien GlioZZo and Sophie Combette designed the cover. The overall layout, graphics and desktop publishing were done by Madasamyraja Rajalingam.

The financial support of donors to the UNCTAD LDC Trust Fund, particularly the Governments of Norway and Finland, is gratefully acknowledged.

Contents

<i>What are the least developed countries?</i>	iii
<i>Explanatory notes</i>	ix
<i>Abbreviations</i>	x
<i>Country classification used in this Report</i>	xii
<i>Overview</i>	I–XV

INTRODUCTION: THE IMPLICATIONS OF THE GLOBAL ECONOMIC CRISIS FOR LDCs..... 1

A. Introduction.....	1
B. The likely impact of the global economic crisis on LDCs.....	1
1. Global prospects.....	1
2. External vulnerabilities of LDCs.....	2
3. The cumulative impact.....	5
C. Alternative development strategies for LDCs.....	7
1. Refocusing attention on developing productive capacities.....	8
2. Building a new developmental State.....	8
3. Ensuring effective multilateral support.....	9
D. Organization of this Report.....	12
Notes.....	14
References.....	14

1. RETHINKING THE ROLE OF THE STATE IN LDCs — TOWARDS DEVELOPMENT GOVERNANCE..... 15

A. Introduction.....	15
B. The good governance reform agenda and development.....	16
1. The imperative of good development governance.....	16
2. The scope, content and propagation of the good governance reform agenda.....	17
3. The mixed evidence on developmental impact.....	19
4. The problem of good governance reform overload.....	25
C. What makes some developmental States more successful than others.....	28
1. What Governments did.....	31
2. How Governments did it: the role of the State and the market.....	32
3. How Governments did it: functions of the State.....	33
4. How Governments did it: institutional capabilities.....	34
D. Adapting the developmental State to the twenty-first century.....	35
1. The democratic developmental State.....	36
2. Modern governance for development.....	37
E. Can LDCs build developmental State capabilities?.....	40
1. Yes they can!.....	40
2. A pragmatic approach to building developmental State capabilities.....	41
3. The critical role of donors.....	46
F. Conclusions.....	50

Notes	52
References	52

2. MEETING THE MACROECONOMIC CHALLENGES 57

A. Responses to the current global economic crisis	57
B. Fiscal policies.....	58
1. Introduction	58
2. Alternative fiscal policies — expenditures and investment.....	60
3. Alternative fiscal policies — domestic revenue mobilization	63
4. The role of ODA in domestic resource mobilization.....	70
C. Monetary and financial policies	74
1. Alternative monetary policies.....	74
2. Why is monetary policy ineffective?.....	78
D. Reforming financial institutions to provide development finance.....	79
1. The financial sector in LDCs	79
2. Mobilizing domestic savings in LDCs.....	79
3. Improving development finance	80
E. Exchange rate and capital management policies	83
1. The need for complementary exchange-rate management.....	83
2. Managing the capital account.....	85
Notes	89
References.....	89

3. SETTING THE AGENDA FOR AGRICULTURAL POLICY IN LDCs 91

A. Agriculture: The heart of the LDC development problem?.....	91
B. Addressing the food crisis and food security in LDCs	99
1. The current food security situation.....	99
2. Foreign trade in agricultural products.....	105
C. Intersectoral linkages and the rural non-farm economy	110
1. Promoting intersectoral linkages.....	114
2. Investment in agriculture and infrastructure supporting farm to non-farm linkages.....	118
3. Finance to support farm to non-farm linkages	122
4. Encouraging market access linkages	125
D. Conclusions and ways forward	127
Notes	135
References.....	136

4. TAILORING INDUSTRIAL POLICY TO LDCs 141

A. Introduction.....	141
1. The crisis as a necessity and an opportunity for change	142
2. Changing destiny variables: from initial conditions to dynamic competitiveness	143
3. Specialization and manufacturing in LDCs.....	144

B. Change of perspective in favour of industrial policy	145
1. Perspectives on market and State shortcomings.....	148
2. Changing parameters of industrial policy.....	149
3. Developmental industrial policies and the profit–investment–export nexus	152
4. Industrial policy agencies and institutions promoting growth	154
5. Key features of a developmental industrial policy.....	155
C. FDI: not a substitute for industrial policy.....	159
D. Enabling conditions for knowledge-based structural change.....	161
1. Technology policy and learning.....	161
2. Learning and technological upgrading in LDCs.....	162
E. Comparative accelerated growth experiences in successful industrializers	164
1. Social compact/partnerships	165
2. Strong developmental States and policy alignment.....	165
3. The role of external finance	166
4. Trade tools, mechanisms and development institutions	166
5. Lessons learned	168
F. Application of industrial policy to LDCs	169
1. Industrial policy case study — Uganda.....	170
2. Industrial policy case study — Senegal.....	171
G. Conclusions.....	173
Notes	175
References.....	176

List of Boxes

1. Measuring the goodness of governance — some methodological problems.....	22
2. Public sector reforms in LDCs: some lessons from experience in African LDCs.....	26
3. Different types of State: developmental States, regulatory States and enabling States.....	29
4. Mushtaq Khan’s approach to building growth-promoting governance capabilities: the example of the Bangladesh garments sector	44
5. The macroeconomic policy space in LDCs.....	59
6. The role of public investment	62
7. Climate change, agricultural growth and diversification.....	93
8. Rural–urban population trends in LDCs	94
9. Fertilizer subsidies in Zambia	96
10. Land governance in LDCs.....	97
11. LDC undernourishment trends	103
12. Institutional and organizational dimensions of farm to non-farm linkages	117
13. Bangladesh: a case of improving rural non-farm linkages.....	118
14. Lessons from the application of smallholder farm technology packages in Malawi	119
15. What role for agricultural development banks?	123
16. Initiatives to promote risk management and access to finance for LDC farmers	124
17. The business linkages programme by Enterprise Uganda	171

List of Charts

1. Monthly commodity price indices, January 2000 to February 2009.....	3
2. External imbalances.....	4
3. Months of imports covered by international reserves.....	5
4. Exchange rates indices by groups of LDCs.....	6
5. GDP per capita, Government effectiveness and Government final consumption expenditure per capita in LDCs, other developing countries and developed countries in 2006	24
6. The Spectrum of substantive and procedural policy instruments	39
7. Schematic representation of fit requirements in public sector reform.....	42
8. Building developmental State capabilities in LDCs: an approach to public sector reforms.....	43
9. Gross fixed capital formation in the LDCs, 1980–2007	61
10. Fiscal revenue trends in African LDCs, 1990–2006	65
11. Trends in tax components in African LDCs, 1990–2006	66
12. Domestic savings in LDCs, 1980–2007	80
13. Food production per capita index and agricultural production per capita in LDCs, 1970–2005	95
14. Food expenditure shares of low-income households in selected LDCs	101
15. Food and global commodity and oil price trend indices, 2000–2008	102
16. Global long-term food price forecasts to 2017	105
17. Agricultural trade in LDCs, 1995–2006.....	106
18. LDC food import bill, 1990–2008	107
19. Food aid as a share of total aid in LDCs, 2000–2007	109
20. Imports and exports concentration indices.....	146
21. FDI inflow to LDCs, by region, 1980-2007	160
22. FDI inflow to LDCs by export specialization, 1980-2007	160
23. FDI inflow as a percentage of GDP of the receiving countries	161

Box Charts

1. Government spending financed by grants in selected LDCs, 2008.....	59
2. Rural–urban dynamics in LDCs, 1950–2030	94
3. Farm size distribution: small farm sector in selected African LDCs.....	98
4. Number and share of undernourished LDC population, by region and export specialization.....	104

List of Tables

1. “Ideal types” of governance systems: good governance versus bad governance	18
2. Seven core principles in new public management reforms	19
3. Governance priorities in second-generation PRSPs in LDCs	20
4. Taxonomy of substantive and procedural policy instruments	38
5. The challenge of financing governance in LDCs: GDP per capita, Government current expenditure and domestic resources available for financing governance and investment, 2006.....	47

6. Gross aid disbursements to LDCs for Government and related purposes by main categories in 2005–2007	49
7. Consumer price inflation in the LDCs, 2005–2007	75
8. LDCs with high real interest rate, 2004–2006	77
9. Current account and trade balances of LDCs, by groups, 1995–2007	85
10. Stock of accumulated capital flight over the period 1970–2004 in sub-Saharan Africa.....	87
11. Agricultural employment and share of GDP in LDCs and ODCs, 1980–2006.....	92
12. Selected case studies of the LDC rural non-farm economy.....	111
13. Agricultural growth-linked RNF activities, by sector.....	115
14. Agricultural sector multipliers: From increases in farm output to RNF sectors	116
15. A stylized illustration of long-term priorities for the RNF economy in LDCs	131
16. A guide to potential policy interventions in the rural economy.....	132
17. Trends in industrial sector composition in LDCs, 1970–2007	145
18. Key industrial policies tools and measures used by successful industrializers and policy space currently available under multilateral rules.....	151
19. Instruments of industrial and export promotion policies – Republic of Korea and Japan.....	167
20. Industrial policy instruments – Ireland.....	167
21. Industrial Policy Instruments – Nordic countries (Denmark, Finland and Sweden), 1950s and 1960s.....	168

Box Table

1. Availability of cultivated lands to agricultural populations in selected sub-Saharan African countries, 1960–2005	97
---	----

Explanatory Notes

The term “dollars” (\$) refers to United States dollars unless otherwise stated. The term “billion” signifies 1,000 million. Annual rates of growth and changes refer to compound rates. Exports are valued f.o.b. (free on board) and imports c.i.f. (cost, insurance, freight) unless otherwise specified.

Use of a dash (–) between dates representing years, e.g. 1981–1990, signifies the full period involved, including the initial and final years. An oblique stroke (/) between two years, e.g. 1991/92, signifies a fiscal or crop year.

The term “least developed country” (LDC) refers, throughout this report, to a country included in the United Nations list of least developed countries.

In the tables:

Two dots (..) indicate that the data are not available, or are not separately reported.

One dot (.) indicates that the data are not applicable.

A hyphen (-) indicates that the amount is nil or negligible.

Details and percentages do not necessarily add up to totals, because of rounding.

Abbreviations

AGOA	African Growth and Opportunity Act
ARM	agricultural raw materials
BNDES	Banco Nacional de Desenvolvimento Econômico e Social
BRDB	Bangladeshi Rural Development Board
CAADP	Comprehensive Africa Agriculture Development Programme
CDP	Committee for Development Policy
CGIAR	Consultative Group on International Agricultural Research
CPI	consumer price index
DIP	developmental industrial policy
DME	developed market economy
DRAF	domestic resources available for finance
EU	European Union
FAO	Food and Agriculture Organization of the United Nations
FDI	foreign direct investment
GDP	gross domestic product
GNI	gross national income
HIPC	heavily indebted, poor countries
ICT	information and communications technology
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IFI	international financial institution
IFPRI	International Food Policy Research Institute
ILO	International Labour Organization
IMF	International Monetary Fund
ISI	import substitution industrialization
KBE	knowledge-based economy
LDC	least developed country
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MFI	micro-finance institutions
MVA	manufacturing value added
NEER	nominal effective exchange rate
NEPAD	New Partnership for Africa's Development
NERICA	New Rice for Africa
NGO	non-governmental organization
NIC	newly industrialized countries
NPM	new public management
NSI	national systems of innovation
ODA	official development assistance

ODC	other developing country
OECD	Organisation for Economic Co-operation and Development
PIF	performance improvement fund
PRGF	Poverty Reduction and Growth Facility
PRSP	poverty reduction strategy paper
R&D	research and development
REER	real effective exchange rate
RNF	rural non-farm
RTA	regional trade agreement
SAP	structural adjustment programme
SMEs	small and medium-sized enterprises
SOE	state-owned enterprise
SPS	sanitary and phytosanitary
SSA	sub-Saharan Africa
STI	science, technology and innovation
TNC	transnational corporation
TRIMS	the Agreement on Trade-related Investment Measures
TRIPS	the Agreement on Trade-related Intellectual Property Rights
UNCTAD	United Nations Conference for Trade and Development
UNIDO	United Nations Industrial Development Organization
UNDP	United Nations Development Programme
UNECA	United Nations Economic Commission for Africa
VAT	value-added tax
WGI	Worldwide Governance Indicator
WRS	warehouse receipt schemes
WTO	World Trade Organization

Country classification used in this Report

For statistical and analytical purposes, LDCs are classified according to three criteria: (a) geographical; and (b) export specialization; and (c) net agricultural trade. They are grouped as follows:

1. Geographical groupings

- 1.1 Africa and Haiti:** Angola, Benin, Burkina Faso, Burundi, Central African Republic, Chad, Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Rwanda, Senegal, Sierra Leone, Somalia, Sudan, Togo, Uganda, United Republic of Tanzania, Zambia.
- 1.2 Asia:** Afghanistan, Bangladesh, Bhutan, Cambodia, Lao People's Democratic Republic, Myanmar, Nepal, Yemen.
- 1.3 Islands:** Comoros, Kiribati, Maldives, Samoa, Sao Tome and Principe, Solomon Islands, Timor-Leste, Tuvalu, Vanuatu.

Some of the island LDCs are geographically in Africa or Asia but are grouped together with the Pacific islands due to their structural similarities. For the same reason, Haiti and Madagascar are grouped together with African LDCs.

2. Groupings by export specialization

- 2.1 Oil exporters:** Angola, Chad, Equatorial Guinea, Sudan, Timor-Leste, Yemen.
- 2.2 Agricultural exporters:** Afghanistan, Benin, Burkina Faso, Guinea-Bissau, Kiribati, Liberia, Malawi, Solomon Islands, Somalia, Tuvalu, Uganda.
- 2.3 Mineral exporters:** Burundi, Central African Republic, Democratic Republic of the Congo, Guinea, Mali, Mauritania, Mozambique, Niger, Sierra Leone, Zambia.
- 2.4 Manufactures exporters:** Bangladesh, Bhutan, Cambodia, Haiti, Lesotho, Nepal.
- 2.5 Services exporters:** Comoros, Djibouti, Eritrea, Ethiopia, Gambia, Maldives, Rwanda, Samoa, Sao Tome and Principe, United Republic of Tanzania, Vanuatu
- 2.6 Mixed exporters:** Lao People's Democratic Republic, Madagascar, Senegal, Togo.

For these groupings LDCs are classified according to which export category accounts for at least 45 per cent of their total exports of goods and services, with some adjustments in a few cases. For a detailed discussion of the criteria and data, see UNCTAD (2008: xii–xiv).¹ Updated statistics on exports have been compiled for this Report and have confirmed the country classifications above.

3. Groupings according to net agricultural trade

- 3.1 Net food importers and net importers of agricultural raw materials:** Angola, Bangladesh, Comoros, Djibouti, Eritrea, Gambia, Haiti, Kiribati, Maldives, Nepal, Niger, Samoa, Sao Tome and Principe, Senegal, Sierra Leone, Somalia, Tuvalu, Yemen.
- 3.2 Net food importers and net exporters of agricultural raw materials:** Benin, Cambodia, Central African Republic, Democratic Republic of the Congo, Equatorial Guinea, Guinea, Lao People's Democratic Republic, Lesotho, Liberia, Mozambique, Sudan, Chad, Togo, Mali.
- 3.3 Net food exporters and net importers of agricultural raw materials:** Afghanistan, Bhutan, Burundi, Mauritania, Rwanda.
- 3.4 Net food exporters and net exporters of agricultural raw materials:** Ethiopia, Guinea-Bissau, Madagascar, Malawi, Myanmar, Solomon Islands, Tanzania, Uganda, Vanuatu, Zambia.

For these groupings LDCs are classified according to their average net trade in food and agricultural raw materials in 2004–2006. For a detailed discussion of the criteria and data, see UNCTAD (2008: 79).¹

¹ UNCTAD (2008). *The Least Developed Countries Report 2008: Growth, Poverty and the Terms of Development Partnership*. United Nations publication, Sales No. E.08.II.D.20. New York and Geneva.