

## **Republic of Vanuatu**

### **A Special Submission to the UN Committee for Development Policy on Vanuatu's LDC Status**

*A special request to the CDP to reconsider excluding Vanuatu from 2009 triennial review due to the high vulnerability of the economy to the current global economic crises and the unreliability of statistical information*

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## 1. Introduction

Vanuatu was accorded an LDC status in 1995 and later in 1997, it was found pre-eligible for graduation when its GNP per capita and HAI thresholds were met, but was put on hold in 2000 after a downturn in the HAI score. In 2006, a triennial review of the status of least developed countries undertaken by the Committee for Development Policy (CDP) had concluded that Vanuatu is one of the countries eligible for graduation because it has performed above the threshold for graduation on GNI per capita and HAI criteria which then stood at US\$ 1,187 and 66 respectively for the first time since 1997. The next triennial review will be held in June, 2009 and if Vanuatu continues to perform well in two or all of the three criteria, its qualification for graduation will be finally endorsed and in 2013, Vanuatu would lose its LDC treatment.

This report is being prepared purposely to ask the CDP to consider excluding Vanuatu from the current list of LDC countries recommended for graduation from their LDC status due to two major arguments. Firstly, the Vanuatu Government maintains its stance that the timing for Vanuatu's graduation from its current LDC status is quite too early simply because Vanuatu's income base is comparatively weak due to its limited resources it owns, thus making it difficult to sustain high growth performances in the long run. Additionally, due to its highly vulnerable and fragile economic status, market shocks such as the current global economic crises is likely to have significant effects on its national output. Thus, the Government feels that it would be more appropriate that Vanuatu be exempted from this year's triennial review until the full impacts of the current global economic crises have been assessed.

Secondly, the Government is still not comfortable with the data used to calculate Vanuatu's performance against the three criteria, more specifically the Human Asset Index. Interestingly, some of the data used are found to be inconsistent with the national statistics data available in the country. Thus, the Government feels that it would not be fair for Vanuatu to be recommended for accession from LDC status based on some inconsistent information. The Government through the National Statistics Office will be addressing the data gaps and discrepancies through its current four year strategic plan and work program. For this reason, the Government also requests that Vanuatu be exempted from this year's triennial review of LDC countries, until 2012 when the relevant statistics should have been identified and nationally approved by the Government.

Finally, the paper places more emphasizes on the current highly vulnerable status of the economy which is the major argument why the Government feels it is quite premature for the Country to graduate from its LDC status. Along this line, the Vanuatu Government is planning to make a submission to the UN General Assembly for a change in the LDC graduation rule, later in the year.

## **2. Update on Vanuatu's LDC Status**

### **2.1. GNP per Capita**

The GNP per capita criteria requires a threshold of USD 745 in order for a country to be listed as an LDC. In order for a country to be eligible for graduation, it has to achieve at least USD 900 over three consecutive years and this was the case for Vanuatu during the 2006 triennial review when it was found to have performed exceptionally well that the average GNP per capita for years 2002-2004 was USD 1,187.

Economic growth during the last three years has been performing remarkably well with real growth rates of 6.5, 7.4 and 6.8 percent for years 2005, 2006 and 2007 respectively. The average GNP for these three years is around USD 439 million and by using a medium population estimate of 224,971 for 2007 would give a GNP per capita figure of USD 1,951.36 compared to the UN's USD 900 threshold for graduation.

### **2.2 Human Asset Index (HAI)**

The criteria used for the HAI composed of four indicators, two for health and nutrition which are mortality rate for children aged five years or under, and percentage of population undernourished and the other two for education, gross secondary school enrolment ratio and the adult literacy rate.

#### **2.2.1 Under Five Mortality Rate**

The 1999 National Population Census reports that under 5 mortality rate has declined substantially since the first official census taken in 1967. The figure has reduced from 58 per 1,000 live births in 1989 to 33 in 1999. However, a recent UNICEF data shows a figure of 40 per 1,000 in 2004 compared to 62 in 1990, but, a more recent CDP estimate in 2006 indicated a slight deterioration to 42 per 1,000. Data discrepancy is a big issue in Vanuatu and therefore it is very important that this problem is addressed before a formal decision on Vanuatu's LDC status is made based on some reliable statistics.

Although around eighty percent of the population has access to basic health services, this varies from 100% in the urban to only 75% in the rural areas. The quality of health services available to many in the rural areas is still poor and physical access has proven to be still difficult.

### **2.2.2 Percentage of Population Undernourished**

Currently, there are national statistics available on the proportion of population which is undernourished in Vanuatu. However, given the large income disparity which exists in the country especially in the urban areas resulting in pockets of undernourishment as highlighted by an urban squatter settlement report in 2002 which identified the following difficulties as very common;

- Lack of services: water supply, electricity for lighting, rubbish collection, public transport;
- Poor living conditions: poor housing and unhealthy surroundings, particularly from poor drainage; and
- Difficulty in meeting their basic needs for food, clothing and money because of insufficient incomes or jobs.

Temporary undernourishment is also sometimes experienced after occurrences of severe natural disasters especially cyclones which usually devastate gardens and other agricultural produces leaving affected people with no food and income sources particularly in the rural communities.

The National Health Information System (NHIS) is currently working on improving national health statistics.

### **2.2.3 Gross Secondary School Enrolment Ratio**

The gross secondary school enrolment ratio as available from the Ministry of Education indicates the ratios of 32.4 %, 37.4% and 35.4% for the years 2006, 2007 and 2008 respectively, compared to a UNESCO's figure of 41% in 2004.

### **2.2.4 Adult Literacy Rate**

The national figure for adult literacy rate is quite uncertain as the 1999 national census revealed a figure of 74% while recent statistics indicate another figure of 66%. The decision to include Vanuatu as eligibility for graduation was based on the 1999 census figure of 74%. Again the question of consistency and reliability is of great importance to determine Vanuatu's eligibility for graduation.

On the overall, a country must score an index of at least 58 to be included in the list of LDCs and a threshold index of 64 to be eligible for graduation. On the overall, Vanuatu scores a human asset index of 66 making it eligible for graduation from its LDC status. However, the question of data consistency and reliability on the above indicators is of paramount importance to determine whether Vanuatu is really eligible for graduation or not.

### **2.3 Economic Vulnerability Index (EVI)**

This criterion reflects the risk posed to a country's development by external shocks and uses seven indicators, which include;

- Population size,
- Remoteness,
- Merchandise export concentration,
- Share of agriculture, fisheries and forestry in GDP,
- Homelessness owing to natural disasters,
- Instability of agriculture production, and
- Instability of exports of goods and services.

According to the criteria, the threshold for inclusion in the list of LDC is 42 and the threshold for graduation is 38. The last triennial review of the status of LDCs shows that Vanuatu scores a very high EVI figure of 64.3. This implies that Vanuatu is a high risk country in terms of its exposure to external shocks and therefore hindering the development progress plus posing other structural problems.

## **3. Our Development Challenges**

Though much has been achieved during the past twenty nine years of independence in terms of development, there are still major hurdles which the country must unavoidably face in pursuit of our development objectives. While some of our challenges could be addressed through policy interventions, others are fixed in nature, especially those related to the geography natural disasters.

### **3.1 Isolated and mountainous Islands**

Vanuatu has around 80 mostly volcanic islands, most of which are quite mountainous and as a result, most people live on the low coastal areas where the land is more flat and fertile for farming. The mountainous state of these islands poses a great difficulty for infrastructure development therefore some of the parts of the islands are inaccessible by road. For these areas, the only mode of transport is by sea so settlements have to be located on the sea coast. The high terrains provide easy access for surface run-offs which during rainy season can cause devastations to infrastructure works and farmland in the lower plains.

Geographically, the islands are scattered apart and the only mode of transport is either by sea or air. Furthermore, some of the islands are very remote that the only economical mode of transport to them is by sea and currently these islands have average ship calls of

one every three months, thus, impacting on the supply of goods and services to the inhabitants.

### **3.2 Small Market and High Cost of Doing Business**

The geographical nature of the country coupled with the small size of the domestic markets for goods and services makes it difficult to attain economies of scale. The major markets for goods and services are confined to the two major urban centers, mainly Port Vila while in the outer islands markets are quite small and fragmented. Access to market is a big problem for most of the farmers in the rural areas because of the lack of proper infrastructure and adequate transport services. Consequently, most rural dwellers only produce to for subsistence purposes, hence, the productive capacity of the rural economy is under utilized.

The domestic financial system is small, less developed and dominated mainly by the activities of the commercial banks. The banking system is very liquid, yet access to credit has been quite difficult in the past due to stringent credit conditions imposed by the commercial banks. With the introduction of a new commercial bank in 2008, there are been some improvements in terms of credit access due to increased competition by banks, but mainly confined to the two major urban centers. Non-formal financial institutions such as micro-finance institutions and private money lenders also offer financial services to those that could not access funds from the commercial banks, however, rates are comparatively high and as a result private sector growth pattern has been very weak in the rural areas where the eighty percent of the population dwells.

The cost of utilities services are also comparatively high, contributing to the high cost of doing business in Vanuatu.

### **3.3 Vulnerability to Natural Disasters**

Vanuatu has been ranked as one of the highly vulnerable country in the Pacific region due to frequency of natural disasters and external economic shocks that hinder the development progress of the country. Some of the factors that contribute to the high economic vulnerability of the country are discussed below.

#### **3.3.1 Earthquake Risk**

Earthquakes are frequent in Vanuatu. Between 1961 and 1982, about 4000 earthquakes of magnitude greater than 4 on the Richter scale have been recorded by the USGS. The last major earthquake occurred in January 2002 and was located 35 km west of the capital Port Vila. Reaching 7.3 on the Richter scale, this earthquake caused widespread damage to buildings and infrastructure. Some of the consequences of this episode are still being felt in 2004. Some fault movements have in the past produced changes in shoreline

elevations of up to two metres as islands have tilted. Destructive tidal waves (tsunami) occur occasionally as the result of earthquakes. The last tsunami, which resulted in approximately twelve fatalities, occurred in November 1999, following a 7.3 earthquake located near the island of Pentecost.

According to an ORSTOM study in 1983, the islands with major earthquake risk are the Torres Islands, Santo, Ambae, North Malekula, Maewo and Pentecost because of the frequent occurrence of strong shallow earthquakes.

### **3.3.2 Volcano Risk**

Vanuatu currently has nine active volcanoes, the most dangerous are Mount Garet (797 m) located on the island of Gaua in the Banks Group and Manaro in Ambae. The increased volcanic activity in Lake Manaro in late 2005 has led to a temporary evacuation of people away of the vicinity of the volcano and the island. The total cost of the evacuation was estimated to be around USD 446,000.

The islands with past major evacuations of people due to high volcanic risks included Ambrym 1913, Lopevi in 1970, Gaua island in 1973 and Ambae 2005. (Gaua and Ambae were temporary evacuations).

Volcanoes are a well identified natural disaster risk in Vanuatu. In islands where volcanic activity constitutes a real danger, the population has been evacuated. In other areas, a monitoring network has been organised in cooperation between the Department of Geology and the IRD based in Noumea (New-Caledonia).

### **3.3.3 Cyclonic risk**

Cyclones are very common to Vanuatu and can cause extensive damage compared to other natural disasters because more islands can be affected at one cyclone event. Historical figures show that the average cost of damages caused by cyclones exceeds that caused by any other disasters.

Cyclone season starts from November to April the following year. On average, Vanuatu experiences 2.6 cyclones per year and one can expect a cyclone-free year once every seven years. The largest and most destructive cyclone to hit Vanuatu in recent times was Cyclone Uma in 1987, which 48 killed, 48,000 people were affected and the total cost of damage was around USD 25 million. The last cyclone to hit Vanuatu was Cyclone Ivy in 2004 which killed two people, caused injuries to 8 and the total number of people affected was 54,000. Table 1 below shows the year and dates of cyclones affecting the country since 1981.

**Table 1: Major cyclones passing through Vanuatu during 1981 – 2004**

Year	Name
1981	Cliff / Gyan
1982	Kina
1984	Beti
1985	Eric, Nigel, Odette, Gavin, Hina
1986	Keli, Lusi, Alfred, Osca, Patsy
1987	Uma, Veli, Yali
1988	Anne, Bola, Dovi, Eseta
1989	Delilah, Harry, Ivy, Lili
1991	Lisa, Tia
1992	Betsy, Daman, Esau, Innes, Fran
1993	Prema, Rewa
1994	Serah, Theodore, Troma, Usha, Vania
1996	Zaka, Atu, Beti, Fegus
1997	Drena, Freda, Ian
1998	Susan, Katrina, Yali, Zuman
1999	Dani, Ella, Frank
2000	Iris, Jojo
2001	Paula, Sose
2002	Zoe
2003	Beni
2004	Ivy

Source: Vanuatu Meteorological Services

### **3.4 Narrow Export Base**

Vanuatu's comparative advantage in terms of trade hinges mainly on the low valued primary sector commodities such as copra, cocoa, beef and kava. On the other hand, Vanuatu depends highly on higher valued imports, most of which are manufactured items resulting in rising trade deficits in the recent years due to the increased absorptive capacity of the domestic economy.

Vanuatu's total commodity exports remain quite volatile. For instance, in 2007, it fell to VT2,229 million from VT3,651 million a year earlier. Some of the factors which contributed to this high volatility include;

- Supply shocks relating mainly to effects of natural disasters mainly cyclones,
- volatility in world market prices and domestic prices,

The narrowness of the export sector coupled with the vulnerability of the primary sector

to supply shocks continues to shape the export trend as indicated by the figures in table 2 on the next page.

**Table 2: Vanuatu export commodities (Million Vatu)**

Commodity/Year	1999	2000	2001	2002	2003	2004	2005	2006	2007
Copra	1,384	1,096	323	174	282	446	126	324	485
Coconut Oil	-	126	362	471	382	1,026	733	193	492
Beef Veal	404	380	239	194	287	286	302	332	180
Cocoa	148	147	64	141	295	160	181	277	221
Shells	76	107	95	50	45	30	57	92	24
Timber Sawn	363	415	334	197	249	247	203	306	80
Cowhides	27	47	39	28	36	28	43	33	19
Kava	379	478	503	230	228	440	477	698	442
Coffee	2	-	5	1	-	-	-	-	-
Vanilla	-	4	4	15	34	33	15	8	10
Coconut Meal	-	11	41	62	93	117	85	6	3
Root Crops	-	3	3	14	38	47	39	19	17
Live Cattle	-	-	44	60	52	62	56	-	-
Other Products	124	400	246	349	580	371	592	1,661	255
<b>Total</b>	<b>2,907</b>	<b>3,214</b>	<b>2,302</b>	<b>1,928</b>	<b>2,600</b>	<b>3,293</b>	<b>2,909</b>	<b>3,651</b>	<b>2,229</b>

Source: National Statistics Office

Copra, which was once earning some VT1,384 million in 1999 but only managed to earn VT485 million in exports in 2007, a drop of around 184%. Interestingly, our national statistics does not show any high export figures for tuna and nor recording any export vessels as reported in the CDP report.

### **3.5 Our Fragile and Narrow Income Base**

Given the highly vulnerable status of our economy, so is the vulnerability of our incomes both in the rural and national levels.

#### **3.5.1 Irregular Rural Income Flows**

Most people in Vanuatu live in the rural area and their main means of income is mostly through the primary agricultural commodities, including copra and kava. They also involve root crops, fruits and vegetable farming mainly for subsistence purposes, the excess of which are sold in the local markets. Fishing is mainly done for subsistence purposes and in Vanuatu it is a sector which still needs to be further explored and enhanced.

Thus, the lower level of economic activity in the rural areas implies that cash earnings are usually irregular depending on the income opportunities that may arise. Furthermore, earnings are also tied to the commodity prices which means that during times of high

prices, production would increase while during periods of low prices, production also subsides. The main reason being that most rural farmers are small scale holders and are usually price takers, implying that they will only increase production when price increases because of the high fixed cost of production relating mainly to transport.

The occurrence of natural disasters in the country also greatly affects the production of these agricultural commodities in the short to medium term.

Furthermore, income opportunities are very limited in the rural areas mainly due to the fact most economic activities are confined to Port Vila and Luganville.

### ***3.5.2 Narrow Government Revenue Base***

Given the smaller resource base of the country, the Government has only a limited number of revenue options to choose from. The major revenue earners for the Government are currently VAT and import duty, both of which contributed around 56% to Government's total revenue and grants in 2007. The foreseen risk is that as Vanuatu starts accession to various regional and global trade agreements, earnings from import duty could decline.

In terms of revenue source, much of the inflow is from the services sector of the economy such as tourism, wholesale and retail trade and transportation. However, given the global economic downturn, we could expect the activities in the sector plus other sectors of the economy affected with the possibility of a decline revenue collections.

### ***3.5.3 A Fragile National Output Base***

A detail breakdown of the Country's gross domestic product indicates that the services sector of the economy contributes around 77% in 2007. Wholesale and retail trade and tourism activities contribute to some large extent in this percentage. In fact, the good economic performance has contributed a lot to buoyant overall economic performance in the recent years.

However, the risk is that this sector is quite vulnerable to economic shocks that it could have rippling effects on other sectors of the economy including government revenue.

Given the current global economic downturn, it is quite possible that this sector could be affected. Hence, the Government feels very strongly that Vanuatu be excluded from this year's triennial review until the full impacts of the crises are assessed.

## **4.0 Why it is too early for Vanuatu to graduate from an LDC status**

Based on the above arguments, the Vanuatu Government maintains its position that it is quite too early for the Country to graduate from its LDC status. Thus, until the following issues and challenges are addressed sufficiently then we will be eligible for graduation.

### ***4.1 Data Discrepancies***

Data discrepancy is quite a problem in Vanuatu as revealed by various data inconsistencies in UN reports concerning Vanuatu LDC status. As mentioned earlier on, statistics used in some of the indicators for the Human Asset Index are needed to be verified or even updated so that any decision on Vanuatu's LDC status is based on concrete numbers that are approved nationally. The National Statistics Office planning to undertake another national population census this year and statistics derived from this would be useful in updating the relevant indicators so that future decisions are made on more reliable and most recent statistics.

### ***4.2 Impacts of Current Economic Global Downturn***

Because of the highly vulnerable nature of the economy, economic shocks due natural disasters or international market downturns tend have some extreme effects on the domestic economy. Hence, as a result of the current global crises, already commodity prices have plummeted, affecting Vanuatu's exchange earnings through exports. On the other hand, the current high import demand continues to put pressure on the country's official foreign reserves which is currently earned mainly through donor funds.

On the output front, the services sector is seemed to be likely to be affected because of its direct linkage to the international markets. Any negative effects on this sector implies and consequential effects on the overall economic output.

Therefore, the Government feels that the next triennial review for Vanuatu be postponed until the impacts of the global crises has been fully assessed.

## **5.0 Way Forward**

While awaiting the UN's decision yet to be made on Vanuatu's LDC status, the Government is currently undertaking measures to address some of the issues raised in this report along the following areas.

### ***5.1 Data Discrepancies***

The Government through the National Statistic Office is currently working on a four year strategic plan and work program to address the issue of data gaps and inconsistencies in preparation for the next triennial.

### ***5.2 High Economic Vulnerability Status***

The Government still maintains its stance that the economy is highly vulnerable; therefore graduating from the LDC status may not solve the nation's development challenges in the long- run.

Along with other LDC countries which are currently recommended for graduation, the Government is planning to make a presentation on the country's stance at the next UN General Assembly.

### ***5.3 In Country Visit of the Evaluators***

Before a final decision is made on Vanuatu's graduation, the Government would like to invite a team of evaluators to the Country for a further assessment of the issues raised.

## **6.0 Conclusion**

With the above arguments, the Government maintains its stance that it is quite too early for Vanuatu to graduate from its LDC status. Therefore, the Government feels that it would be more appropriate that the CDP reconsiders its recommendation for Vanuatu's graduation.