UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

Vulnerability profile of Maldives

October 2003

Prepared by the Special Programme on the Least Developed Countries, and Land-locked and Island Developed Countries of UNCTAD, in consultation with the Government of Maldives.

Vulnerability profile of Maldives

Contents

Executive summary

1. Maldives has a gross national income per capita (estimated at $1,983 on a three-year average basis, in accordance with the CDP's methodology) more than twice greater than the graduation threshold, and a score under the Human Assets Index marginally above the graduation threshold (by 3.5%). Its economic vulnerability is still regarded as high insofar as the country has a score below the graduation threshold relevant to the Economic Vulnerability Index. Therefore, for the third consecutive time (1997, 2000, 2003), Maldives meets two of the three graduation criteria used by the United Nations in reviewing the list of LDCs. By virtue of the graduation rule whereby a country will qualify for graduation from Least Developed Country status if it has met at least two of the three graduation criteria (low income, weaknesses in human assets, economic vulnerability) in at least two consecutive reviews of the list, Maldives is deemed technically eligible for graduation, as it was in 2000.

2. However, there are legitimate concerns about the anticipated adverse consequences of graduation. These concerns principally relate to: (i) the competitive threat faced by the fisheries industry as a result of the presumed automatic loss, in the absence of relevant "smooth transition" measures for graduating countries, of preferential market access for tuna exports (the second most important sector of the economy, with a substantial socio-economic impact in terms of employment and household income); and (ii) the erosion of concessionary external financing that is likely to ensue from graduation, while the country faces considerable needs for infrastructure development and social services, notably in the perspective of the population relocation strategy. In this context, retaining the highest level of special treatment, particularly in international trade and in the sphere of development finance, seems vital for the socio-economic stability of the country. There is a fear that, immediate graduation from Least Developed Country status would give an erroneous signal to the international community regarding the ability of the country to pursue its development efforts in a more autonomous manner, at a time when the Government is facing great socio-economic challenges.

3. Maldives sharply illustrates the "island paradox" whereby a small island developing State, though a Least Developed Country for over 30 years, may demonstrate relative prosperity in terms of domestically generated income (typically, as a result of tourism development), and at the same time, may be highly vulnerable to a range of external shocks, and faced with exorbitant structural costs because of its geographical characteristics. Such a country, despite its apparent socio-economic performance, is likely to be among the countries least prepared to graduate from LDC status in the absence of smooth transition measures to mitigate the adverse consequences of losing maximum concessionary treatment. UNCTAD takes the view that the Committee for Development Policy and the Economic and Social Council should reconsider the question of Maldives' graduation with the utmost possible care, in the light of: (i) the Government's efforts to secure the most concessionary modalities of external support to the country, given the paramount need to pursue the costly but necessary regional development strategy; and (ii) the uncertainty in the prospects for progress, in the international community, toward a consensus on smooth transition measures for countries that may be called to graduate from Least Developed Country status, despite continued efforts by the United Nations to encourage such consensus.

Vulnerability profile of Maldives

I. Introduction

4. Maldives was admitted in the category of Least Developed Countries (LDCs) in 1971, when the LDC denomination was instituted. In 1997, for the first time, the country met all the criteria for graduation from LDC status (at that time, a low-income criterion, a "quality of life" criterion, and an economic diversification criterion). This rise above the graduation lines relevant to all criteria at the time of a particular review of the list of LDCs was unique in the history of the category. Sustained economic growth (6.7% average annual real growth in GNP *per capita* in 1985-1995) explained a rapid increase in the level of national *per capita* income (from $380 in 1989 to $1,090 in 1997). Improvements had taken place in the health and education status of the nation, and the structure of the economy had widened rapidly as a result of tourism growth. In this context, Maldives demonstrated, during the 1990s decade, more progress toward graduation borders than any other LDC. In the 2000 review of the list of LDCs, a maintained performance above graduation thresholds was observed with regard to the low-income and "quality of life" criteria, while the graduation threshold relevant to the economic vulnerability criterion was not met. By virtue of the rule whereby a country was found eligible for graduation if graduation thresholds had been met in two consecutive triennial reviews under at least two of the three criteria, a recommendation to graduate Maldives was made in 2000. Subsequently, however, the United Nations decided that the question of the graduation of Maldives should be reconsidered in 2003, in the light of further information on the anticipated implications for the country of its graduation from LDC status.

5. This country profile has been prepared in anticipation of the April 2003 review of the list of LDCs. It aims at providing the Committee for Development Policy (CDP) and the Economic and Social Council (ECOSOC) of the United Nations with some qualitative and quantitative information on the situation of the country under each one of the criteria, with a view to complementing the core international data used in the triennial review. The profile has been designed in response to an observation, by the CDP, that "elements of structural vulnerability and handicaps, besides those covered by the indices used as criteria, need to be considered on a case-by-case basis"[1], and in accordance with the CDP's recommendation "that a document –to be called a country "vulnerability profile"— should be prepared for that purpose on a regular basis"[2].

6. A first vulnerability profile of Maldives was made available to the CDP by UNCTAD at the time of the 2000 review of the list of LDCs[3]. The present profile is structured differently from the 2000 profile, and not confined to an examination of the situation of vulnerability experienced by the country. It was prepared after two field missions to Maldives (in February 2002 and March 2003), in consultation with the Government of Maldives, and with special support from the United Nations Resident Coordinator in Male'. The views expressed by the UNCTAD secretariat in this document are based on factual observations, and the document aims at enabling the CDP and ECOSOC to make sound recommendations in answer to the question of graduation in the 2003 review of the list of LDCs. In carrying out this exercise, UNCTAD recalled the insistence with which the CDP, ECOSOC, and the

[1] United Nations, *Vulnerability and Poverty in a Global Economy*, Report of the Committee for Development Policy on the first session (26-30 April 1999), para. 122.
[2] ibid., para. 123.
[3] UNCTAD, Vulnerability profile of Maldives, 3-7 April 2000, 29 p.

General Assembly have, since 1991, stated that graduation from LDC status should not harm a graduating country in its continued development efforts.

7. Section II of the profile recalls the "history" of the (non-)graduation of Maldives, and the institutional and methodological aspects that are relevant to the principle of graduation. Sections III, IV and V summarize the situation of the country with regard to the low-income, human capital and economic vulnerability criteria, respectively. Section VI then underlines the anticipated implications of a hypothetical immediate graduation of Maldives. Finally, section VII offers concluding remarks on the importance of identifying the most desirable special treatment of Maldives.

II. Institutional context

8. Since 1971, the United Nations has denominated "Least Developed Countries" a category of States (presently 49) that are deemed structurally handicapped in their development process, faced with the risk of failing to escape from the poverty trap, and in need of the most favourable treatment, in their development efforts, by the international community. The U.N. grants these countries a specially favourable treatment in its allocation of resources under relevant cooperation programmes. At the same time, it gives a strong signal to the development partners of the LDCs by periodically (triennially) identifying these countries and highlighting their structural problems, thereby pointing to the need for special concessions in their favour, especially in the area of development financing and in the multilateral trading system.

Three criteria

9. In the 2000 review of the list of LDCs, the Economic and Social Council of the United Nations used the following three criteria for determining the new list, as proposed by the CDP:

. a **low-income** criterion, based on a three-year average estimate of the gross domestic product *per capita* (under $900 for inclusion; above $1,035 for graduation);

. a **low human capital** criterion, involving a composite *Augmented Physical Quality of Life Index (APQLI)* based on indicators of nutrition, health, education, and adult literacy; and

. an **economic vulnerability** criterion, involving a composite *Economic Vulnerability Index (EVI)* based on indicators of the instability of agricultural production, the instability of exports of goods and services, the economic importance of non-traditional activities (share of manufacturing and modern services in GDP), merchandise export concentration, and the handicap of economic smallness (as measured through a population variable).

10. Under the rule of eligibility for LDC status, a country qualified to be added to the list if it met the above three criteria and did not have a population greater than 75 million. Application of this rule resulted in the addition of Senegal to the list of LDCs in 2001.

11. Further work in 2001 and 2002 toward refining the criteria has resulted into the following changes in the indicators relevant to the criteria in anticipation of the 2003 review of the list: (a) gross national income (GNI) per capita will replace gross domestic product per

capita among the criteria determining the list; (b) the Augmented Physical Quality of Life Index (APQLI) will be renamed Human Assets Index (HAI) so as to reflect what this indicator is intended to capture, that is, the level of productive human capital; (c) the combined primary and secondary school enrolment ratio will be replaced by the gross secondary enrolment ratio in the HAI, since secondary enrolment is a better indicator of the level of education; (d) when comparable data on the percentage of population made homeless by natural disasters become available and sufficiently reliable, they should be used as an additional component of the EVI; (e) several technical options or simulations in the use of the criteria, such as averaging of the components of composite indices, or simultaneous consideration of these composite indices, will be considered.

12. The question of graduation from Least Developed Country status was first raised in 1991, at the same time as the first major revision of the criteria for determining the list of LDCs. The graduation mechanism was applied in 1991 and 1994 to Botswana (with effective graduation in 1994), so far the only country that ever graduated from LDC status. The question became controversial in 1997, after the Committee for Development Planning had found Vanuatu eligible for graduation. The controversy continued in 2000, when the (successor) Committee for Development Policy found Cape Verde and Maldives technically eligible for graduation, and recommended the immediate graduation of Maldives. Noting the resistance of Vanuatu (1997) and Maldives (2000) to the recommendation that they be graduated, ECOSOC, in recent years, has been giving special attention to the notion of "smooth transition" from LDC status for graduating countries[4].

The rationale for graduation

13. In 1990, the Second United Nations Conference on the Least Developed Countries noted the importance of envisaging the graduation from LDC status of countries that would be deemed to have demonstrated sufficient socio-economic progress to be able to pursue such progress in a less externally dependent manner.

14. The principle of graduation is generally considered important for the credibility of the concept of Least Developed Country: the special treatment offered to LDCs has been expected to help these countries to reverse their marginalization from the global economy. If the LDC status is to continue to exist, there must be chances of success associated with it. Therefore, it is only natural that the eventuality of graduation be envisaged for some LDCs. There is, however, another approach to the rationale for maintaining the category. This approach rests on the fundamental definition of LDCs, which recognizes that these countries are structurally disadvantaged, essentially suffering from external shocks and handicaps beyond their control. By virtue of this definition, one tends to accept that most LDCs are in permanent need of special treatment on the part of the international community, and ought to retain their Least Developed Country status accordingly. If there is indeed a permanent incapacity of some countries to "converge" with the rest of the world in their performance, the

[4] cf. Economic and Social Council resolution 2000/34 (*Report of the Committee for Development Policy*), in which the Council requested the Secretary-General "to make recommendations on additional measures that can be taken to ensure a smooth transition from least developed country status for graduating countries" (para. 3).

principle of graduation becomes more complex. It points to a diversity of situations among relevant countries: some LDCs can be expected to come closer to graduation thresholds, but a large number of LDCs are bound to remain far from graduation borders.

15. With the current potential graduation cases (in particular, the cases of Cape Verde and Maldives), the issue of graduation is further complicated by the "island paradox", which policy makers of small island developing States (SIDS) have been pointing to: SIDS often appear relatively prosperous on the basis of the *per capita* income criterion, which tends to be the overriding factor of their eligibility for graduation. However, they are generally among the most economically vulnerable and structurally handicapped countries. For this reason, they are often least prepared to face the impact of graduation from concessionary treatment, whether concessions have been received by virtue of the LDC status (Least developed SIDS), or as a result of other types of special treatment (other SIDS). The "island paradox" reflects a facet of the limitations of the current special and differential treatment of developing countries by the international community. It reveals the fact that the treatment is insufficiently "differentiated" in the responses brought to the specific problems of handicapped countries, even though these problems have been widely recognized in the United Nations[5].

The graduation rule

16. The graduation criteria are conceptually similar (and broadly speaking, symmetrical) to the criteria for admitting new countries on the list: a low-income criterion, a low human capital ("quality of life") criterion, and an economic vulnerability criterion. The graduation criteria have been based on specific quantitative thresholds for the three indicators relevant to the criteria: *per capita* GDP, APQLI, and EVI, respectively. For each of these indicators, there has been a margin between the inclusion threshold and the graduation threshold[6]. The margin is considered a reasonable estimate of the "additional" socio-economic progress that ought to be observed if one assumes that the graduating country is effectively engaged on a path of improvement: not only is the graduating country expected to exceed the thresholds under which non-LDCs would be admitted into the category, but it is additionally expected to exceed these thresholds by the relevant margin. This rule warrants the robustness of the assumption that a graduating country must be undergoing structural progress. Accordingly, it dispels the risk that graduation be dictated by temporary or insignificant economic circumstances.

17. Two other fundamental elements of the graduation rule also imply durable structural progress in the graduating countries:

---

5 cf. Note by UNCTAD to the Economic and Social Council: "The benefits associated with the least developed country status and the question of graduation", E/2001/CRP.5, para. 59-60.

6 Until the 2000 review of the list, a margin of 15% was used under each one of the criteria. For the 2003 review, an expert group meeting in January 2003 recommended that different margins be used among the criteria: 20% for GNI per capita, 10% for HAI and EVI. The inclusion and graduation thresholds relevant to the low-income criterion were established at $900 (inclusion) and $1,035 (graduation) for per capita GDP in 2000, and at $750 (inclusion) and $900 (graduation) for per capita GNI in 2003.

- <u>at least two of the three graduation criteria</u> must be met for the relevant country to be found eligible for graduation, whereas a symmetrical application of the inclusion and graduation rule would have implied that only one criterion ceased to be met, since all three criteria (plus the 75-million population ceiling) should be met for a country to be added to the list;

- while pre-eligibility for graduation can be observed on the occasion of any review of the list (subject to the threshold margin and asymmetrical rule referred to above), full eligibility, which normally implies a recommendation to graduate the country with immediate effect, will be recognized only after the relevant graduation criteria have been met <u>in at least two consecutive reviews of the list</u>.

18. Subsequent to the graduation of Botswana in 1994, there have been three cases of technically full eligibility for graduation from the Least Developed Country status (i.e., eligibility pronounced after at least two graduation criteria were met in two consecutive reviews): Cape Verde and Vanuatu in 1997; Cape Verde and Maldives in 2000. Yet, none of these three LDCs did graduate.

The "history" of Maldives' non-graduation

19. In the 1994 review of the list of LDCs, the Committee for Development Planning observed that Maldives marginally exceeded the graduation threshold (by 1.9%) under one of the three criteria, namely, the "quality of life" criterion, while none of the graduation lines relevant to the other criteria was near to be reached. It was noted, however, that the relevant *per capita* GDP estimate ($721, an annual average based on the 1990-1992 period) was above the threshold for adding countries to the list, by $22[7].

20. In the 1997 review of the list, the Committee observed that Maldives exceeded the *per capita* income graduation line by 10% (with a *per capita* GDP estimate of $990 based on the 1993-1995 period), the "quality of life" graduation line by 30%, and the economic diversification graduation line by 5.2%. An impressive upturn was noted in the performance recorded under the economic diversification criterion: this performance had increased to 105% of the graduation threshold (from 38% in the 1994 review), principally as a result of the rapid expansion in tourism activities. The Committee therefore –for the first time— recommended "that Maldives be graduated from the list, provided that it continue to meet the criteria for graduation at the time of the next review in 2000, on the basis of a more detailed assessment of its situation at that time"[8].

21. The United Nations General Assembly, in its resolution 52/210 of 18 December 1997, and in accordance with an earlier proposal by the CDP, called for an assessment of the usefulness of a vulnerability index as a criterion for identifying the LDCs. This call, essentially, was made in response to the issues that had been raised by Vanuatu after that country, in the 1997 review of the list, had been found eligible for graduation. In turn, the Economic and Social Council, at its substantive session of 1998, while deciding "to postpone

[7] United Nations, Committee for Development Planning, Report on the Twenty-ninth Session (12-14 January 1994), Economic and Social Council Official Records 1994, Supplement No. 2, para. 260 and Table 9.
[8] United Nations, Committee for Development Planning, Report on the thirty-first session (5-9 May 1997), Economic and Social Council Official Records 1997, Supplement No. 15, para. 229(b).

its consideration of the graduation of Vanuatu", requested the Committee for Development Planning to assess the usefulness of such an index, and to consider "the work of all relevant international agencies on the vulnerability of small States"[9].

22. The (successor) Committee for Development Policy (CDP), in the report on its first session (April 1999), proposed the establishment of a vulnerability criterion through the construction of an Economic Vulnerability Index (EVI) to replace the Economic Diversification Index (EDI). At the same time, it considered that "an index of economic vulnerability could give only a partial and approximate measure of the relative level of vulnerability of a country"[10], and recommended that a country-specific "vulnerability profile" be prepared for each potential graduation case on the occasion of every review of the list.

23. In February-March 2000, an expert group meeting convened by the United Nations Secretariat observed that, in the context of the 2000 review of the list, Maldives was meeting two of the three graduation criteria, namely, the low-income criterion (with a *per capita* GDP performance above the graduation threshold by 27%), and the "quality of life" criterion. The margin by which Maldives now exceeded the graduation border under the latter criterion had decreased significantly (from 130% of the threshold in 1997 to 112% in 2000). The experts therefore noted that the country would again "be eligible for graduation even if its [new score under the] EVI did not meet the graduation threshold". The experts added that the findings of the 2000 vulnerability profile of Maldives "corroborated the conclusion based on quantitative indicators … that Maldives was less affected … [than other "borderline countries"] … by exogenous shocks", thereby referring to the relatively low degree of economic instability observed through specific indicators entering the composite EVI. Finally, the experts recognized "the specific long-term challenge" faced by the country as a result of the sea-level rise phenomenon, and stressed the need to give special consideration to the high costs of population relocation and infrastructure development in this context[11].

24. In the light of these findings, the Committee, at its second session in April 2000, recommended that Maldives be graduated from the list of LDCs with immediate effect[12].

25. In the annex to a letter of 22 July 2000 addressed to the President of the Economic and Social Council, the Permanent Representative of Maldives to the United Nations stated that, despite the qualitative assessment offered by the 2000 vulnerability profile, "the level of human development … [was] … overestimated and the vulnerability of the economy underestimated"[13]. The Permanent Representative, in the same annex, requested the Economic and Social Council "to look into the matter more closely and defer the question of graduation of Maldives until all relevant and critical facts … have been thoroughly examined and an accurate and proper analysis of the impending consequences of graduation has been made"[14].

---

[9] Economic and Social Council, Resolution 1998/39 (Status of the least developed countries), 30 July 1998, para. 2.
[10] United Nations, *Vulnerability and Poverty in a Global Economy*, Report of the Committee for Development Policy on the first session (26-30 April 1999), para. 122.
[11] United Nations, Committee for Development Policy, Report on the second session (3-7 April 2000), Economic and Social Council Official Records, 2000, Supplement No. 13, Annex 1: Report of the Expert Group Meeting on Testing and Simulations of the Economic Vulnerability Index, 29 February-2 March 2000, pp. 29-30.
[12] Ibid., para. 106.
[13] Economic and Social Council, Annex to the letter dated 22 July 2000 from the Permanent Representative of Maldives to the United Nations addressed to the President of the Economic and Social Council, E/2000/97, p. 2.
[14] ibid., p. 3.

26. In the light of the CDP's recommendation and of the above reaction by national authorities, the Economic and Social Council, in its resolution 2000/34, decided "to defer to its next substantive session the consideration of the recommendation to graduate the Maldives … [and requested the CDP at its 2001 session] … to re-examine its recommendation in this regard"[15], taking into account, *inter alia*, the necessity of measures "to ensure a smooth transition from least developed country status for graduating countries"[16], and UNCTAD's assessment of the implications of graduation for Maldives in the context of an analysis of "the effective benefits derived by the least developed countries specifically on the basis of their inclusion in the list" of LDCs[17].

27. In a letter of 29 March 2001 to the Secretary-General, the Permanent Representative of Maldives to the United Nations stressed his understanding "that CDP's re-examination of the Maldives case will be carried out in the light of all the relevant information referred to"[18] in ECOSOC resolution 2000/34. In responding on behalf of the Secretary-General, the Under-Secretary-General for Economic and Social Affairs confirmed that all efforts were being made by the United Nations so that "sufficient light […] be cast on implications of graduation and desirable measures for a smooth transition after graduation"[19].

28. In the report on its third session (April 2001), the CDP recalled that, by meeting two of the three criteria for graduation, Maldives was "clearly eligible for graduation"[20]. However, as the additional information requested by the Economic and Social Council was not available, the Committee recommended that the Council extend "the transition period until the next triennial review in 2003 before a decision is taken by the General Assembly about the country's graduation"[21]. At the same time, the Committee recommended that the Council request relevant development partners and international organizations "to make available the relevant information on their likely response to a country's graduation … [and] … to respond to the issue of "smooth transition"…"[22].

29. In a statement made to the Third United Nations Conference on the Least Developed Countries (14-20 May 2001), the Minister who headed the delegation of Maldives described as "a glaring omission" from the draft new programme of action for the LDCs "the absence of measures designed to assist countries to graduate from LDC status", and denounced "the propensity for a miscarriage of justice … [vis-à-vis] … a country that does not have the economic resilience to suffer the kinds of external shocks that graduation would impose"[23].

30. The Economic and Social Council, in its resolution 2001/43, requested the CDP "to continue its work on the re-examination of its recommendation to graduate the Maldives from the list of least developed countries … and to submit … final recommendations to the 2003

---

[15] Economic and Social Council, Resolution 2000/34, Report of the Committee for Development Policy, para. 2.
[16] ibid., para. 3.
[17] ibid., para. 4.
[18] Letter from Ambassador Hussain Shihab, Permanent Representative of Maldives, to the Secretary-General of the United Nations, 29 March 2001, p. 2.
[19] Letter from Mr. Nitin Desai to the Permanent Representative of Maldives to the United Nations, 24 April 2001, p. 2.
[20] United Nations, *Participatory Development and Governance: Africa's Special Needs*, Report of the Committee for Development Policy on the third session (2-6 April 2001), United Nations, New York, 2001, para. 112.
[21] ibid., para. 119.
[22] ibid., para. 120.
[23] Maldives (Statement by), Third United Nations Conference on the Least Developed Countries, 14-20 May 2001, pp. 2-3.

substantive session of the Council"[24]. At the same time, it decided "to extend the transition period of the Maldives until the next triennial review of the list of least developed countries in 2003"[25], as recommended by the Committee.

31. In the report on its fourth session (April 2002), the CDP "recalled that the Government of Maldives had pointed out some anomalies…" (over-estimation) in the statistics used in the 2000 review of the list, "…in particular, with regard to the nutrition and school enrolment variables"[26]. In the light of a thorough review of the Maldivian case by an expert group meeting in January 2002, the Committee recommended "that a new country profile be prepared by UNCTAD with a view to assessing the reliability of the figures that will be used in the 2003 review … [and] … the implications for Maldives of the replacement of GDP per capita by GNI per capita among the criteria…"[27]. The Committee also stressed the importance of examining the implications for Maldives of its hypothetical graduation, in the light of new and additional information from multilateral and bilateral donors.

32. In its resolution 2002/36 of 26 July 2002, the Economic and Social Council again requested the Committee for Development Policy "to continue its work on the re-examination of its recommendation to graduate Maldives from the list of least developed countries at its fifth session [April 2003] and to submit its recommendations to the Council at its substantive session of 2003 in the context of the triennial review of the list of least developed countries…"[28]. At the same time, the Council took note of the Committee's recommendation "that country vulnerability profiles be prepared for each country close to the graduation thresholds, including Maldives, and that such profiles be completed before the end of 2002, so that they … be available for the preparation of the next triennial review in 2003"[29].

The situation of Maldives with regard to the graduation thresholds at the time of the 2003 review of the list of LDCs

33. The three graphs below depict the evolution demonstrated by Maldives vis-à-vis the thresholds relevant to the three graduation criteria. All graphic data are based on the performance recorded, in the five institutional reviews of the list of LDCs (1991, 1994, 1997, 2000, 2003), through relevant indicators: Gross Domestic Product per capita (replaced in 2003 by the Gross National Income per capita); the Augmented Physical Quality of Life Index (renamed Human Assets Index/HAI in 2003); and the Economic Vulnerability Index, which replaced the Economic Diversification Index in 2000[30].

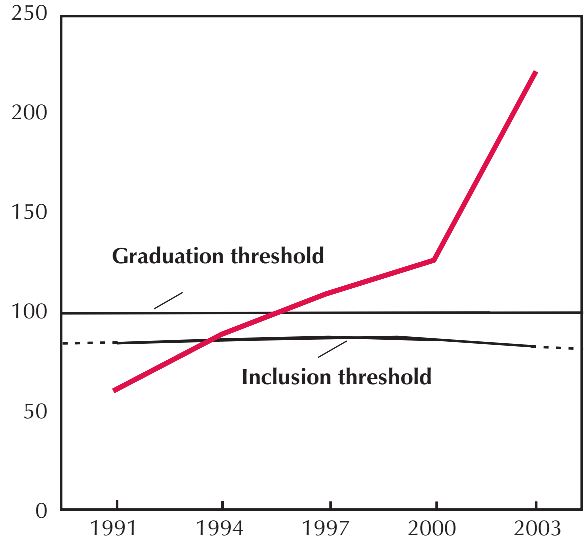
34. To make inter-temporal comparisons possible under any criterion (e.g., to compare the distance to the graduation threshold in 2003 with that in 2000), all performance data have been standardized in the form of an index under which the graduation threshold equals 100.

[24] Economic and Social Council, Resolution 2001/43 (Report of the Committee for Development Policy), para. 1.
[25] ibid., para. 3.
[26] United Nations, *Capacity-building in Africa: Effective aid and human capital*, Report of the Committee for Development Policy on the fourth session (8-12 April 2002), United Nations, New York, 2002, para. 155.
[27] ibid., para. 156.
[28] Economic and Social Council, Resolution 2002/36 (*Report of the Committee for Development Policy*), para. 2.
[29] ibid., para. 4.
[30] These data and relevant comments constitute an updated version of the profile of Maldives which was presented in: UNCTAD, *Graduation from the Least Developed Country status: where do the LDCs stand?*, UNCTAD/LDC/Misc.83, 2002, p. 34.

Each graph, at the same time, shows a line representing the inclusion threshold. The distance between the two lines is the margin between the inclusion threshold and the graduation threshold.

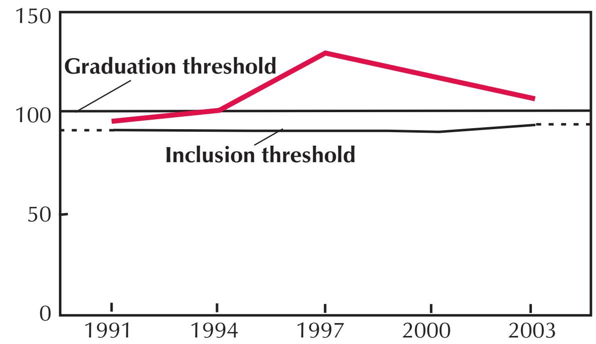
Low-income criterion

(GDP per capita until 2000, GNI per capita in 2003)



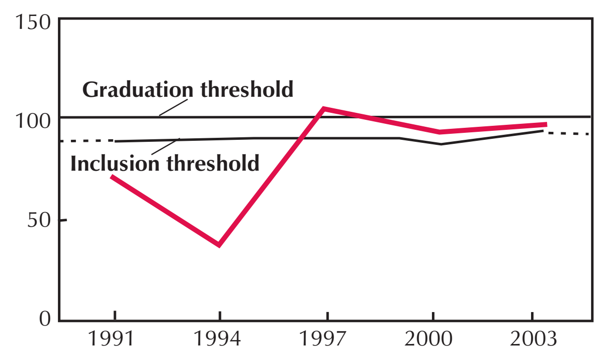
35. Among all LDCs, Maldives has demonstrated the steadiest and fastest progress across the graduation line relevant to the low-income criterion. The graduation threshold was met at the time of the 1997 review of the list, after a historically high growth performance had been recorded. A score of 127% of the threshold was observed in the 2000 review, when the *per capita* GDP performance was estimated at $1,311. In the last years of the 1990s decade, a sustained tourism performance kept Maldives on a high growth path, compared with most developing countries. In 2003, the performance of Maldives (relevant to the 1999-2001 average period) is estimated to culminate at 220% of the graduation threshold, although the real growth of GDP decreased during the three-year period (from 7.2% in 1999 to 3.5% in 2001), and the real growth of per capita GDP, as a result of high demographic pressure, diminished even more rapidly (from 5.1% in 1999 to 1.7% in 2001). It should be noted that the sharp increase above the graduation threshold relevant to the low-income criterion was not caused by the substitution of GNI per capita for GDP per capita as the relevant income aggregate, since the nominal value of the graduation threshold changed at the same time as the income aggregate did.

Human capital weakness criterion
(APQLI until 2000, HAI in 2003)



36. Under the quality-of-life criterion, the graduation threshold was met in the latest three reviews of the list, with a peak of 130% in the 1997 review, followed by a declining trend leading to a score marginally above the graduation threshold in 2003. Re-examination of the components making up the APQLI has revealed that the primary and secondary school enrolment ratio in 1996 (recorded as 92% at the time of the 2000 review) may have been overestimated by 20%. Moreover, the enviable calorie intake estimate (118% of the requirement) in 1997 ought to be considered with caution in the light of findings, by UNDP, of facts such as a nutritional situation “worse than that of Sub-Saharan Africa”. In 2003, the HAI score, estimated at 104.4%, seems more realistic than the 2000 score, principally because of the lower average calorie intake estimate (113% of the relevant requirement), and the substitution of the secondary school enrolment ratio for the primary and secondary school enrolment ratio.

Economic vulnerability criterion
Economic Vulnerability Index/EVI



37. The sharp upturn in the EDI performance which was observed at the time of the 1997 review (from 38% to 105%) was not explained by the predominant tourism activities (services exports were not reflected in the EDI), but caused by sudden growth in the clothing sector, although the latter was still a small part of the economy. With the adoption of the EVI, a more realistic picture has been drawn: the score (marginally) under the graduation line in 2000 and

in 2003 is mainly explained by the serious structural handicaps faced by the islands and measured through the smallness of the population, while the steady growth in tourism and fisheries earnings has made Maldives, among all developing economies, one of those with the least unstable exports of goods and services. It is important to note that the narrowness of the economic base (a dimension that is captured by the EVI) exacerbates the economic vulnerability of the country, as any adverse development in only one of the two dominant sectors can destabilize the overall performance of the economy.

Technical eligibility for graduation

38. The simultaneous performance, in 1997, above the graduation lines relevant to all three criteria was unique in the history of the LDCs. In the 2003 review of the list, the technical eligibility for graduation is observed by virtue of the graduation rule, because of the maintained performance above the lines relevant to two of the three graduation criteria (low income; human capital weakness).

39. The following sections indicate some differences between the international data used by the CDP, and relevant national data. However, these differences do not challenge the CDP's findings that point to a technical qualification for graduation.

III. <u>The situation of Maldives with regard to the low-income criterion</u>

40. The low-income criterion has always been at the heart of the methodology for identifying the LDCs. Until 2000, the gross domestic product (GDP) *per capita* was used as the indicator relevant to this criterion. In the 2000 review of the list, as in previous reviews, the CDP used a three-year average of GDP *per capita* based on the three latest years for which relevant data were available for all countries (1996-1998), with each year's estimate being converted at the official exchange rate. At its fourth session in April 2002, the CDP recalled that "one of the starting points for determining the list of least developed countries" had been its consideration of the list of low-income countries as determined by the World Bank, and that the Bank, for that purpose, had been using "per capita gross national income (GNI), not gross domestic product"[31]. The Committee decided that, "for the sake of clarity and consistency"[32], GNP per capita should replace GDP per capita, and that in every triennial review of the list of LDCs, GNP per capita as calculated by the World Bank and found in the World Bank Atlas would be the only indicator used in relation to the low-income criterion.

Significance to the CDP of the criterion and relevant variables

41. The Committee for Development Policy has always considered the low-income criterion as a benchmark criterion, in the sense that it provides a synoptic picture of LDCs as countries that are structurally hindered in their development efforts, and accordingly face the greatest risk of remaining trapped in poverty and marginalized from the global economy. A lasting low income may not be a direct indicator of the various factors of structural delays (these are appropriately measured, instead, by human capital and economic vulnerability indicators), but a low income will often reflect the economic consequences of structural handicaps, for example, when malnutrition impairs productivity, or external shocks cause economic stagnation. At the same time, a low level of income is likely to explain the inability

[31] United Nations, *Capacity-building in Africa: Effective aid and human capital*, Report of the Committee for Development Policy on the fourth session (8-12 April 2002), United Nations, New York, 2002, para. 126.
[32] ibid., para. 127

of the relevant country to overcome its structural impediments, because poverty places obstacles on the road to structural progress. While cognizant of the range of impediments a low income can imply, the Committee has been less sensitive to the fallacy a higher-than-average income may sometimes entail. There have been hopes that more efforts will be made to recognize as a fact of life the paradox of simultaneity between a rising per capita income and a continuously high economic vulnerability, a phenomenon that is specially common to small island developing States.

42. In substituting per capita GNP for per capita GDP, the Committee noted that "GNP is regarded as reflecting the productive capacity of a country as adequately as GDP"[33]. This consideration is based on the observation that in several LDCs, remittances from nationals abroad (a variable entering the formulation of the gross national product) have had a positive impact on the productive capacity, in particular, through direct investment in small enterprises, or through savings that could be channelled toward project financing under the auspices of a local financial intermediary, or venture capital investment. The Committee also advised, in its 2002 report, that "the role played by remittances, external aid, and other forms of income be considered with regard to their impact both on GNI figures and on domestic productive capacity", and added that "any significant destruction of capital, including natural capital, should be considered as well, when relevant information is available" [34]. The latter consideration points to an implicit notion of "net national product", in which an amortization of natural or productive capital ought to be accounted for. This notion is of special relevance to developing countries in which key productive capacities are closely linked to the natural environment, such as small island developing countries that rely much on the durability of fragile ecosystems for their tourism industry. Noting the absence of systematic consideration –or only adequate knowledge— of relevant amortization data in LDCs, the Committee stressed the importance of supplementing standard national accounts aggregates with an appropriate qualitative assessment of the impact on future productive capacities of environmental erosion phenomena beyond domestic control, as well as environmental degradation caused by "unsustainable" productive practices.

43. Another issue that has been borne in mind by CDP members in their numerous discussions about the most desirable criteria is the question of income distribution. In its 2000 report, the CDP recognized that situations of inequality in income distribution are common in LDCs and largely overshadowed by traditional national accounts aggregates. However, the Committee noted that national income distribution can be considered "largely a policy variable"[35] and thus not deemed fully relevant to the fundamental definition of the LDCs and its reflection through criteria that capture structural disadvantages caused by factors beyond domestic control. Moreover, CDP members noted that the health and education-related components of the composite APQLI indirectly reflect situations of poverty, and therefore, of income distribution.

44. Overall, and primarily because of serious limitations in the availability of relevant data, the Committee has not considered issues of environmental degradation, income distribution and poverty to be central components of the low-income criterion, even though

---

[33] ibid., para. 126
[34] ibid., para. 127
[35] United Nations, *Poverty amidst Riches: The Need for Change*, Report of the Committee for Development Policy on the second session (3-7 April 2000), Annex 1: Report of the expert group meeting on testing and simulations of the Economic Vulnerability Index, para. 51.

some of these issues “might be considered in later refinements” of both this criterion and the human assets criterion.

Significance to Maldives of the criterion and relevant variables

45. The variable making up the difference between the GDP and the GNP is the net inflow from abroad of factor services income (externally generated income received from non-residents minus domestic income transferred abroad to non-residents). In Maldives, this variable has been negative over time (GNP smaller than GDP), though decreasing in recent years. It was estimated at US $40.7 million in 1999, $39.8 million in 2000, $30.6 million in 2001, and $19.9 million in 2002. In the latter year, the relevant amount was equivalent to 7.8% of total foreign exchange earnings from exports of goods and services. Of all payments abroad of factor services income, profit remittances by the tourism industry has been the largest, with an average $9.6 million annually over the 1997-2001 period, accounting for an average 25% of total payments of factor services income. Comparatively, payments of labour income accounted for a very small portion of total payments of factor services income (an average 0.7% over the 1997-2001 period). Labour income receipts from abroad, which were estimated at $2-2.5 million annually between 1997 and 2001, have been 11 times greater, on average, than labour income payments. The expatriate labour employed in Maldives, in December 2001, was estimated at 29,200 persons. Nearly 60% of these foreign workers were employed by tourism resorts (30%), construction enterprises (16%), and various business activities (12%). The fisheries sector, which is the second largest sector of employment in Maldives, accounts for less than 2% of the total expatriate labour, but the garment manufacturing sector represents 8% of the total population of foreign workers.

46. Overall, net payments abroad of investment income have been the main factor explaining the difference between the GDP and the GNP (or GNI). Using the latter aggregate under the low-income criterion for graduation can therefore be considered a methodological improvement in the case of Maldives, because net payments abroad of investment income amount not only to an overall loss of domestically generated income, but also to lost opportunities to expand the country’s productive capacity and contribute to reducing the structural disadvantages the country is faced with. Comparatively, had the gap between the GDP and the GNP been explained mainly by expatriate workers’ remittances abroad, the likelihood of a changing trend in such remittances (with the eventuality of permanent residency for some expatriate workers) would have reduced the significance of the gap in terms of irreversibility of lost income.

47. The issue of environmental degradation and its implications for a realistic assessment of the national income is much relevant to Maldives. The Vulnerability and Poverty Assessment 1998 identified five factors that have been contributing to environmental degradation: (i) beach erosion (a phenomenon mainly resulting from natural processes and affecting more than 90% of the atoll population); (ii) high population density (mainly on the capital island of Malé); (iii) deforestation (mainly caused by the use of fuelwood for cooking); (iv) dumping of solid waste on beaches; and (v) the leaching of toilet waste into the groundwater, which, from an environmental and health perspective, is a cause of hazards, especially for the most densely populated islands. The coral bleaching phenomenon, a consequence of ocean warming, has also –more recently— become a cause of increasing concern as it directly affects the main pillar of the economy, i.e., the tourism industry. The gradual destruction of the coral mass affects a precious ecosystem that constitutes the natural infrastructure for an important segment of the tourism sector, namely, the diving industry.

Like beach erosion and the related threat of sea-level rise, but in the shorter run, coral bleaching is one of the factors dampening the durability of productive capacities that ought to be fully taken into consideration in the national accounts.

48. The issue of income distribution is also of significant importance to Maldives and cannot be disregarded in any interpretation of the national income. A household income survey conducted in 1997-1998 throughout the country revealed that the average income of households was 75% higher in Malé than in the atolls, and that the average household income of the four atolls with the highest average income was 116% higher than the average household income of the four atolls with the lowest average income[36]. These facts, reinforced by parallel contrasts in various social indicators (including those entering the HAI), show that income distribution is highly unequal in Maldives[37]. This inequality is a reflection of the limited domestic income multiplier effect of tourism growth in the country, even though tourism development has been the dominant factor of rapid real growth in GDP or GNP in the last decade. Considering the magnitude of leakages in foreign factor income (profit repatriation, expatriate labour's income remittances), and accordingly, the limited multiplier impact of manufacturing and modern services on a large proportion of the national population, GDP growth can be regarded as a poor indicator of progress in the overall standards of living of Maldivians. GNI brings an improvement in providing a benchmark for the low-income criterion, but yet remains much insufficient to substantiate the case for graduation, considering the high structural costs affecting a large part of the population (including transport costs and a high cost of living in the context of heavy reliance on imports), and the absence of quantitative consideration for environmental degradation and inequality in income distribution.

Relevant data from national and international sources

49. In the last years of the 1990s decade, a sustained tourism performance kept Maldives on a high growth path, compared with other LDCs. The real growth of the tourism sector was relatively high (between 5% and 11%) during the 1996-2000 period. However, real growth was estimated to be less high in the early years of the new decade, with annual rates of 4.8% in 2000 and 3.5% in 2001, compared with 10.2% in 1997, 9.8% in 1998, and 7.2% in 1999[38].

50. The main factors explaining the recent economic slowdown were a recession in the fisheries sector in 2000 (followed by a stagnation of the sector in real terms in 2001 and 2002), a sharp decline in the construction sector in the same year, and a zero-growth reaction of the tourism sector to international instability in 2001. As a result of the recent decrease in the real growth trend, per capita GNP at current market prices was lower in 2002 ($2,090) than in 2000 ($2,130) and 2001 ($2,120).

---

[36] Republic of Maldives, Vulnerability and Poverty Assessment 1998, p. 19-20.

[37] The WTO Secretariat, in its report to the Trade Policy Review Body for the first Trade Policy Review of Maldives, stated that "*although the Maldives has made considerable progress in reducing poverty, some 43% of the population still live below the poverty line of Rf15* [US $1.2] *per day, most residing in regional atolls*": cf. WTO, Trade Policy Review, Maldives, Report by the Secretariat, WT/TPR/S/110, 13 December 2002, p. 28. Some 183 islands of the country (92% of all inhabited islands) have a population under 2,000. More specifically, 141 islands have a population under 1,000 inhabitants, 75 islands a population under 500, and 16 islands a population under 250.

[38] Source: Maldives Monetary Authority, Economic Statistics, January 2003, Vol. 3, No. 1.

Summary of the performance observed under the low-income criterion

51. Maldives has been above the graduation threshold under the low-income criterion since 1997. The relevant score, in percentage of the graduation threshold, was 63% in 1991, 90.2% in 1994, 110% in 1997, and 126.7% in 2000. It is estimated at 220% in 2003.

Per capita GDP according to national sources[39]:

2000-2001-2002 average: $2,267
1999-2000-2001 average: $2,257
1998-1999-2000 average: $2,195
1997-1998-1999 average: $2,091

Per capita GDP according to the World Bank[40]:

2000-2001-2002 average: $2,221
1999-2000-2001 average: $2,236
1998-1999-2000 average: $2,182

Per capita GNI according to the World Bank (Atlas method)[41]:

2000-2001-2002 average: $2,113
1999-2000-2001 average: $2,100
1998-1999-2000 average: $2,003

Net private unrequited transfers[42] (net outflows): -$49.6 million in 2001 and -$50.1 million in 2002 (equivalent to 11.5% of total export earnings).

Dominant factor explaining the difference between GDP and GNI:

transfers abroad of profit generated by the tourism sector ($10.7 million in 1999).

IV. The situation of Maldives with regard to the human capital weakness criterion

52. Maldives has been above the graduation threshold under this criterion since 1994. The relevant score, in percentage of the graduation threshold, has been 96.2% in 1991, 101.9% in 1994, 130% in 1997, 111.7% in 2000, and 104.4% in 2003.

53. Under the human capital ("quality of life") weakness criterion, the graduation threshold was met in the latest three reviews of the list, with a peak of 130% in the 1997 review. An examination of the four variables making up the APQLI score observed in 2000 reveals that Maldives demonstrated a better performance than other LDCs with regard to education-related indicators. In 1996, Maldives ranked first, among all LDCs with respect to the adult literacy rate (estimated at 95.3%), and second in the same year with regard to the primary and secondary school enrolment ratio (92%). The health-related variables entering the composite APQLI scored less high, though placing Maldives among the 10 least

[39] Source: Ministry of Planning and National Development, Development Outlook, January 2003, No. 9, p. 12.
[40] Source: calculations based on data from the World Development Indicators (on line: www.worldbank.org)
[41] Source: World Development Indicators (on line: www.worldbank.org)
[42] Source: Maldives Monetary Authority, Economic Statistics, July 2002, Vol. 2, No. 7.

disadvantaged LDCs: six LDCs had lower average child mortality rates than Maldives during the 1995-2000 period, but eight LDCs scored better than Maldives in 1999 with regard to the calorie intake in percentage of the relevant requirement.

Calorie intake

54. **Variable used**: calorie intake ratio (average daily calorie intake as a percentage of the relevant requirement)
CDP estimate of the calorie intake ratio in the 2000 review of the list: 118%
National estimation in 2003: the latest survey of food supply for household consumption (1997) revealed an average value of 2,150 calories per day. An earlier estimate (in 1993) had given a calorie intake of 2,063 calories[43].
CDP estimate of the calorie intake ratio in the 2003 review of the list[44]:113.8% (1998).

The government has pointed out the limitations inherent in the FAO's estimation of the food supply and calorie intake in Maldives, which is based on combined domestic production and importation data. It takes the view that the estimated food supply, through this method, covers a population that is 15% greater than the Maldivian population, essentially because of the magnitude of food imports for tourists. The government's estimate of the rate of under-nourishment in the atolls is close to 50%. In particular, nearly half of all children in the outer islands suffer from poor nutrition (stunting).

Under-5 child mortality

55. **Variable used**: under-5 child mortality rate (number of relevant deaths per 1,000 inhabitants)
CDP estimate of the child mortality rate in the 2000 review of the list: 66 per 1,000 (1995-2000)
National estimation in 2003: two conflicting figures from national sources are 66 per 1,000 and 88 per 1,000[45].
CDP estimate of the child mortality rate in the 2003 review of the list[46]: 47.3 per 1,000 (2000).

School enrolment

56. **Variable used**: gross secondary school enrolment ratio (number of students enrolled in secondary classes as a percentage of the population of secondary school age children)
CDP estimate of the school enrolment ratio in the 2000 review of the list: 92% (1996). This high estimate, a combined primary and secondary school enrolment ratio, was explained by a very high primary school enrolment ratio. The latter did not reflect a high enrolment performance, but the consequences of serious inter-island transport difficulties on school-year repetition. According to government sources, only 11% of the children who completed grade 7 have been able to enrol in a secondary school.

[43] data communicated to UNCTAD by UNDP in 2002
[44] on the basis of international data from FAO
[45] data communicated to UNCTAD by UNDP in 2002
[46] on the basis of international data from WHO

Substitution of the secondary school enrolment ratio for the combined primary and secondary school enrolment ratio allows a more realistic representation of the national performance in this area, and more meaningful international comparisons.
National estimation in 2003: gross secondary school enrolment ratio (based on 2001 data): 59%
CDP estimate of the secondary school enrolment ratio in the 2003 review of the list[47]: 42.7% (1999-2000).

Adult literacy

57. **Variable used**: adult literacy rate (number of literate adults as a percentage of the total adult population)
CDP estimate of the adult literacy rate in the 2000 review of the list: 95.3% (1996). This figure is correct if the notion of literacy is understood as being in the national language (dhivehi). However, it has been criticized by Maldivian authorities, who take the view that a more meaningful definition of literacy would imply literacy as conducive to socio-economic progress in the context of globalization, i.e., literacy in an international language. This, in the case of Maldives, means literacy in English, which has been estimated at 35% (1998).
CDP estimate of the adult literacy rate in the 2003 review of the list[48]: 96.9% (2000).

V. <u>The situation of Maldives with regard to the economic vulnerability criterion</u>

58. Maldives was above the graduation threshold only once: in 1997. The relevant score, in percentage of the graduation threshold, has been 72% in 1991, 37.9% in 1994, 105.2% in 1997, 96.3% in 2000, and 99% in 2003.

Index of instability of agricultural production

59. This indicator is regarded as reflecting the physical impact of natural disasters. The score of Maldives under the relevant index was relatively high in 2000 (based on the 1979-1998 period): the country ranked as the 19th least unstable among 128 developing countries. Considering that Maldives has a small agricultural production, this index is a poor indicator of significant physical shocks such as coastal erosion, and of the adverse socio-economic impact of monsoon weather. An element of non-price instability in the primary sector (not captured through agricultural statistics) would be the instability observed in the fish catch, a phenomenon that has been caused by variations in tuna stocks due to the highly migratory nature of relevant species. The 2003 estimate of agricultural production instability, based on the 1979-2001 period (as opposed to 1979-1998 in 2000) is exactly identical to the 2000 estimate.

Index of instability of exports of goods and services

60. This indicator reflects the impact of all external (economic and natural) shocks on total gross foreign exchange earnings. The score of Maldives under the relevant index since the 2000 review has been high (based on a 20-year period), as the country ranks

[47] on the basis of international data from UNESCO
[48] on the basis of international data from UNESCO (standard methodology based on literacy in national languages)

among the least unstable among 128 developing countries. This stability has been mainly explained by the domination of tourism in the balance of payments (70% of total foreign exchange earnings in 2000), and steady growth in tourism receipts. However, instability was observed in tourism receipts in 2001 (-1.3% in tourist arrivals, compared with an average +8.2% per annum in 1996-2000) as a result of events in Sri Lanka and in the aftermath of 11th September. The 2003 estimate of export instability, based on the 1979-2001 period (as opposed to 1979-1997 in the 2000 review) indicates a slightly growing instability of export earnings, subject to comparability between 2000 and 2003 estimates.

Share of manufacturing and modern services in GDP

61. This indicator is regarded as reflecting the degree of economic specialization into economic activities with a higher value added. The relevant share of GDP involves (in addition to textile manufacturing) tourism, transport, communications, and financial and business services. It is therefore largely determined by the performance of the tourism sector. The share of this sectoral cluster in GDP has been stable, around 60%, since 1995. The figure used in the 2000 review of the list (relevant to 1997) was 43%. The figure used in 2003 is 44% (1998 or 1999).

Merchandise export concentration index

62. This index is regarded as an indicator of economic diversification. UNCTAD's export concentration index (for the year 2000) was 0.364[49]. There has been no further diversification of the Maldives economy in recent years. With the anticipated termination of the Multifibre Arrangements after 2004, prospects for a continuation of the garments sector are questionable. Meanwhile, diversification into new activities of merchandise or service exports is unlikely to be observed, considering the smallness of the economy. The figure used in the 2000 review of the list (relevant to 1998) was 0.356. The figure used in 2003 (for 2001) is 0.449, which indicates an increased merchandise export concentration.

Economic smallness (population in logarithm)

63. Figure used in the 2000 review of the list: 0.3 million (1997)
Estimate from 2002 government statistics: 270,100 (March 2000)
Estimate from the World Development Indicators (on line): 276,000 (2000); 282,750 (2001)

Maldives is among countries most highly handicapped economically (facing exorbitant structural costs, especially in the areas of infrastructure development and transport). Considering the difficulties in measuring such handicaps, population size, as an indicator of economic smallness, is deemed to provide a fair quantitative approach to the structural handicaps faced by the country.

[49] UNCTAD Handbook of Statistics, 2002, p. 398.

VI. Anticipated implications of a hypothetical immediate graduation of Maldives from LDC status

64. Immediate graduation from Least Developed Country status would have implications in the areas of international trade, development financing, and technical assistance to the country.

Implications in the area of international trade

65. At the bilateral level, graduation would make canned and fresh fish products ineligible for LDC-specific GSP treatment on the EU market, and subject to Most Favoured Nation (MFN) tariffs of up to 24.3%. This would put Maldives at a major disadvantage on the EU market vis-à-vis, not only more competitive MFN exporters to the EU, but also LDCs (e.g., Solomon Islands) and non-LDC ACP countries such as Fiji and Papua New Guinea, which would continue to export fish products on a duty-free basis to the EU under the Cotonou Agreement. As fisheries constitute the second most important sector of the economy (about 60% of domestic merchandise exports, 12% of total foreign exchange earnings, 11% of the labour force), this loss of preferential access would have a serious socio-economic impact on the country, although exports of fish products to the EU market account for a small proportion of the national income. Fishing is the main, and often the only, occupation in the atoll regions, where an estimated 65% of the population directly or indirectly depends on fisheries. Graduation would also bring an end to market access preferences under the SAPTA[50] for dried fish exports to Sri Lanka (destination of 30% of total fish exports in 2001), where the margin of preference has been 35%.

66. Clothing exports to the US, the EU and SAARC countries would not be affected because they do not enjoy preferential access. However, graduation would imply a loss of the more generous rules of origin currently extended by SAARC countries to Maldives because of its LDC status.

67. At the multilateral level, graduation would imply the loss of a number of significant advantages (in particular, implementation delays) with regard to WTO obligations. These advantages are regarded by Maldives as important, considering the severe limitations faced by the country in terms of institutional capacities.

68. The call, by the Economic and Social Council, for greater consideration –and UNCTAD's echoing— of the importance of securing a "smooth transition" for graduating countries has begun to be heard in the multilateral trading system. In reacting to a proposal for "smooth transition" measures in the Work Programme on Small Economies (WPSE) of the World Trade Organization, the United States stated: "we are interested in exploring this idea further", and considered that a transition period should involve "phase-in" modalities that ought to be "optimally effective for the LDC[51]".

69. On 4 November 2002, in the WTO's Committee on Trade and Development holding its third Dedicated Session on small economies (under the WPSE), Maldives, the only

[50] The South Asian Association for Regional Cooperation (SAARC) Preferential Trading Arrangements (SAPTA) have been effective since December 1995.

[51] World Trade Organization, Committee on Trade and Development, Dedicated Session, *Questions from the United States and initial responses in regard to proposals contained in WTO document WT/COMTD/SE/W/3*, WT/COMTD/SE/W/7, 4 November 2002, p. 8.

member State of the WTO facing the eventuality of graduation, provided the following response to a question by the United States ("Does the [smooth transition] proposal envision a transition that includes benchmarks for phased adoption of normal WTO obligations?"):

> *Benchmarks for a phased adoption of normal WTO obligations could be envisaged as part of smooth transition modalities for members graduating from LDC status. Such benchmarks should be commensurate with the competitive and institutional constraints faced by the graduating member. As all potential graduation cases are cases of small and vulnerable economies, determining smooth transition modalities ought to be done in the light of the peculiar circumstances surrounding the graduation of such States, wherein the economy, though recording an improved performance, remains structurally handicapped and highly dependent on preferential market access. This applies to Maldives (presently the only member State near graduation), where the viability of the fisheries sector acutely depends on the LDC treatment received on the EU market.*

70. The notion of smooth transition for graduating countries has therefore been placed on the agenda of the Work Programme on Small Economies of the World Trade Organization, where Maldives, as a member State, hopes to see progress toward acceptance of some concrete smooth transition proposals. While *ad hoc* smooth transition measures are likely to be considered favourably with regard to systemic obligations under various Agreements, the chances of success of the idea of retaining preferential market access after graduation are uncertain. Regarding preferential access to the EU market for tuna (the most vital trade concession to the country), Maldives, in the event of graduation, could request a 10-year extension of the GSP privilege, thereby asking the European Union to adopt, for the first time in the history of LDCs, a specific measure of continued LDC treatment for an ex-LDC.

71. In answering a question to India, on 17 January 2003, in the first Trade Policy Review of Maldives at the World Trade Organization, the Maldives delegation stated (*verbatim*):

> *The consequences of graduation is not a matter that Maldives can deal with alone. We need the understanding and support of the WTO membership, the Secretariat, other international development organizations, and bilateral donors. If the country is to be graduated without a trajectory for phasing-out or –in to the appropriate levels the preferential treatment in terms of WTO obligations and treatment, unilateral trade preferences, development grants and concessional finance as well as technical assistance from all sources, we may find Maldives sliding back into the LDC category.*

72. In the final meeting of the Trade Policy Review Body gathered on the same day, the representative from the European Commission promised to convey the "tuna concern" to the Commission, and assured the Maldivian delegation of the Commission's willingness to examine the question in the light of relevant ongoing progress in the World Trade Organization.

Implications in the area of development financing

73. Although development partners generally recognize the structural disadvantages Maldives faces in its development efforts, most partners are likely to interpret the eventuality of Maldives graduation from LDC status as the signal of an enhanced capacity of the country to pursue these efforts in a less externally dependent manner. Such interpretation could result

in decreased concessionary treatment in bilateral allocations, with a lesser grant element and a decline in overall allocations at the time of renewal of aid cycles. This could result in an increased debt burden, which even a sustained growth pattern, considering the small economic base, would not be able to overcome. The Asian Development Bank might "upgrade" Maldives eligibility for concessionary treatment from maximum concessionary treatment under the Asian Development Fund (ADF) to a blend of ADF treatment and limited "ordinary capital resources" treatment, considering that the country is still regarded as having a relatively weak debt repayment capacity. Overall, the government fears that immediate graduation would give an erroneous signal to the donor community, which could result in a lesser concessionary content of development financing, or the imposition of a penalty in a context of great need for external financial support.

Implications in the area of technical assistance

74. No U.N. agency or programme is likely to suddenly discontinue the treatment it has been granting to Maldives because of the graduation of this country. However, graduation would disqualify the country from applying for trade-related technical assistance under the "Integrated Framework", and might entail a loss of interest in supporting Maldives among bilateral donors that pay greater attention to the economic performance than to the permanent constraints facing a country.

75. The Integrated Framework (IF) for trade-related technical cooperation in favour of LDCs is sponsored by the International Monetary Fund (IMF), the International Trade Centre (ITC), the United Nations Conference on Trade and Development (UNCTAD), the United Nations Development Programme (UNDP), the World Bank, and the World Trade Organization (WTO). UNDP, as the designated lead agency for the implementation of the IF in Maldives, is to start coordinating a work programme in the country, with a diagnostic trade integration study (DTIS) to be undertaken, through a participatory process, by a team of international and national experts. Based on the findings of the DTIS, a programme of technical assistance to strengthen the competitiveness of the overall economy and of selected sectors will be designed. Key projects of technical assistance might include, *inter alia*, modernizing the fisheries sector to increase the capacity of the fishing fleet, establishing modern plant processing facilities in several atolls, and assisting the country in diversifying its export market for fish.

VII. Conclusion: the importance of identifying the most desirable special treatment of Maldives

76. For the third consecutive time (1997, 2000, 2003), Maldives meets two of the three graduation criteria, and would normally be deemed technically eligible for graduation. One can anticipate that a hypothetical immediate graduation of Maldives would have serious consequences for the country. As a Cabinet minister pointed out, graduation will harm the country if it is envisaged in the absence of an "exit strategy" providing "breathing space" for developing a structural capacity to face the loss of concessions.

77. Considering the permanent structural handicaps Maldives is faced with (mostly resulting from smallness, remoteness, and severe environmental threats), there are modalities of special treatment that are considered essential to the country. Retaining special treatment in the context of graduation would imply a mix of the following options: (i) continuing to enjoy full market access for exports of fish products on a quasi-permanent basis (for example, for a

period of at least 10 years); (ii) accepting a gradual phasing out of other concessionary measures ("smooth transition" *par excellence*); (iii) accepting, if deemed endurable, an immediate loss of certain LDC-specific benefits; and (iv) seeking new modalities of differentiated treatment that were not even granted by virtue of LDC status.

78. In the area of international trade, the most critical need relates to the continuation of preferential market access for tuna, as the loss of such preferential treatment is anticipated to seriously affect the viability of at least a third of the fisheries sector, and have a severe socio-economic impact in the atoll regions. There is also a need to retain the favourable treatment that is currently granted to Maldives as an LDC, in terms of certain obligations under various WTO agreements, including tariff reduction obligations under the GATT.

79. In the area of development financing, there is a paramount need for maximum concessionary terms in financing several elements of the public sector investment programme, particularly for the physical infrastructure that is essential to the regional development strategy of the country. As the pegged exchange rate regime restrains the Government's macroeconomic leverage through fiscal policy, the scope for implementing the national development strategy in a financially more autonomous manner (in particular, through external commercial borrowing) remains small. Moreover, the obligation to accelerate tariff reductions (and be content with less government revenue accordingly[52]) in the event of graduation would put additional pressure on the public revenue, until adjustments are made to the tax regime (such as converting import tariffs into value-added taxes). This makes external financing all the more important. Considering the limited borrowing capacity of the country, a wide range of needs for maximum concessionary financing can only be strongly advocated, and will be high on the list of requests for "smooth transition" measures and other forms of special treatment.

80. In the area of technical assistance, there is a wide range of needs that only the treatment currently granted under the LDC regime can satisfy. Beneficiary sectors have been receiving such assistance from several agencies and programmes of the United Nations system. Of particular importance is the upcoming eligibility of Maldives to technical assistance under the Integrated Framework for trade-related technical cooperation in favour of LDCs. Maldives expects to begin to benefit from the Integrated Framework technical assistance and trust fund resources in the near future. The rationale for seeking continued special treatment in the area of technical assistance is largely explained by the permanent need for strengthening institutional capacities in the context of the relative scarcity of skilled manpower.

81. Considering the wide range of possible modalities of special treatment, Maldives could gain much from seeking retention of a set of highly concessionary measures on the part of bilateral, regional and multilateral development partners. It could do this in the light of a wide re-examination of relevant needs, from which the particular need for "smooth transition" in relation to an eventual loss of the LDC regime would be easily recognizable.

[52] Tariff revenue accounts for about 27% of the total current revenue of the government.