Financing for Development for LLDCs
Non paper

Introduction

The 32 landlocked developing countries (LLDCs) face a wide array of development challenges due to a lack of direct territorial access to the sea. Remoteness and isolation from world markets, additional border crossings, cumbersome transit procedures, inefficient logistics systems, weak institutions and poor infrastructure cause LLDCs to incur substantially higher transport and other trade transaction costs when compared to coastal countries. These high costs present a tremendous trade-reducing effect that has a direct negative impact on economic growth and puts them at a disadvantage in fully harnessing their potential for their sustainable development.

In 2014, the Vienna Programme of Action for LLDCs for the Decade 2014 to 2024 (VPoA) was adopted at the Second United Nations Conference on LLDCs. The VPoA is a comprehensive and ambitious plan to support LLDCs in their effort to achieve inclusive and sustainable economic growth, reduce poverty and ensure their integration into the global economy through six priority areas namely: 1) fundamental transit policy issues, 2) infrastructure development and maintenance, 3) international trade and trade facilitation, 4) regional integration and cooperation, 5) structural economic transformation and 6) means of implementation.

The midterm review of the VPoA held in 2019 revealed that whilst efforts were made by LLDCs, transit countries, and development partners to facilitate the implementation of the VPoA, the progress made was not enough for LLDCs to achieve the VPoA targets and SDGs. The General Assembly therefore called for action to accelerate the implementation of the Vienna Programme of Action. The COVID-19 pandemic has reversed the small progress achieved over the years in implementing the VPoA.

Due to resource constraints, which have been accentuated by the COVID-19 pandemic, LLDCs require external resources to implement the priority areas of the VPoA. Support is particularly needed to: close the financing gap to achieve seamless transport, and digital and energy connectivity; scale up trade facilitation initiatives and fully implement the WTO Trade Facilitation Agreement; increase trade capacity including diversification, value-addition and tradability to join global and regional value chains; promote productive capacities, industrialization and structural economic transformation; accede to and effectively implement relevant global and regional legal instruments that promote regional integration; promote regional cooperation; and enable the mobilization of resources. The full and effective implementation of the VPoA is critical for LLDCs in achieving the 2030 Agenda for Sustainable Development.

The emergence of new COVID-19 variants is compounding the negative socioeconomic impact of the pandemic. Not only it is delaying the recovery phase, but it is also jeopardizing the achievement of objectives encapsulated in the VPoA and the SDGs. The continuation of the pandemic has also worsened LLDCs' structural vulnerabilities as evident by the decline in investment, trade, remittances, fiscal space and growing debt burdens. The decline in LLDCs' exports due to both demand and supply side constraints that particularly affected commodities has impacted their balance of payments and increased their debt vulnerability. According to UNDESA[1] LLDCs' economies after contracting by 1.6% in 2020 grew by only 4.1% on average in 2021. This modest recovery was in all likelihood insufficient to reverse the increase in poverty due to COVID-19 particularly amongst marginalized groups including women, children and informal workers.

LLDCs' are expected to grow by an average of 4.4% in 2022, which is far lower than levels needed to ensure targets enumerated in the VPoA and the 2030 Agenda are met on time. More efforts are required to ensure that the rate of economic growth increases to levels that are needed to sustain LLDCs' development needs. In light of the emergence of new COVID-19 variants, vaccine availability is also of paramount importance to support LLDCs' recovery efforts.

It is widely recognized that the global recovery from the COVID-19 pandemic will be incomplete and unsustainable if it occurs in an unequal and piecemeal manner. Therefore, comprehensive support for vulnerable economies, including LLDCs is paramount for a more equitable, sustainable and resilient world.

The vulnerable situation of LLDCs requires the international community to provide enhanced financing, investment, technical assistance and capacity building to ensure they can build back better, acknowledging that no single source of financing will be enough to meet their development needs. A wide array of domestic and international resources are required including: enhanced domestic finance; elevated Official Development Assistance (ODA); forging sub-regional and regional cooperation on infrastructure projects; increased foreign direct investment (FDI); strengthened South-South and triangular cooperation; harnessing of remittances and enhancing the role of the private sector in infrastructure development.

Domestic Public Resources

Domestic public revenues are essential to providing public goods and services, increasing equality, supporting macroeconomic stability and allocating resources for achieving the SDGs. A viable path to fiscal self-sufficiency in the long-term is imperative for LLDCs' development prospects. Many LLDCs still need to raise more domestic fiscal revenues in order to meet their development financing gap. Tax mobilization remains a challenge in many LLDCs in spite of significant efforts and recent reforms. Furthermore, proportion of tax revenues to GDP ranges considerably amongst the LLDCs. Based on the latest World Bank[2] data available between 2018 and 2020, 10 of the 22 LLDCs where data is available, had tax revenue to GDP ratios below 15% and the cumulative average of all 22 was 15.6%. In comparison, the proportion of tax revenues to GDP the European Union it was 19.9% and the world average was 15%.

Mobilization of domestic resources in LLDCs is undermined by trade imbalances, volatile commodity prices, limited tax administration capacity, narrow tax bases and an underdeveloped private sector comprising mainly of informal sector, amongst other challenges. The enaction of periodic lockdowns after the onset of the COVID-19 pandemic have further compounded domestic

[1] UN DESA (2022) *World Economic Situation and Prospects,* United Nations: New York
[2] World Bank (2022) *World Development Indicators,* Online, available at: https://databank.worldbank.org/source/world-development-indicators

revenue constraints. The enhancement of domestic revenue generation capacity is imperative for LLDCs' long-term development prospects.

It is also important to address illicit financial flows in LLDCs to enhance resource mobilization. Towards this end, measures to support LLDCs to re-establish correspondent banking relationships and to establish legal and effective public private partnerships (PPPs) for tracking and tracing transactions are imperative. LLDCs also need technical assistance to build policy oriented anti-corruption and anti-money laundering solutions.

Sustainable Recovery

The most immediate need for LLDCs is support towards facilitating a sustainable recovery from the COVID-19 pandemic. As stated above, LLDCs resource constraints have been compounded by the pandemic and without external support they risk being left behind. Following are some key recommendations:

- Ensure LLDCs' immediate COVID-19 related needs are met by prioritizing them for the delivery of vaccines, socioeconomic aid and other COVID-19 related expenses
- Give support to LLDCs to establish National Disaster Risk Reduction Strategies (NDRRS), to proactively prepare for future crises and minimize their impact
- Technical support for the preparation of Integrated National Financing Frameworks (INFFs) to promote sound financing and ensure expenditure and investments in all sectors are disaster risk informed
- Make the processes and procedures for accessing finance from international development institutions more accessible for LLDCs and provide multidimensional support to recipients to access financial resources
- LLDCs require technical support to utilize climate finance including capacity building on developing bankable projects
- Supporting LLDCs efforts towards their integration into global trade including through enhanced market access and trade facilitation.

International Development Cooperation

ODA represents one of the major resource inflows for many LLDCs. ODA to LLDCs increased by 3.8 per cent between 2018 and 2019 to $29.5 billion, accounting for 18 per cent of ODA to developing countries. Yet, ODA flows continue to be concentrated in a few landlocked developing countries. In 2019, five countries[3] received almost half of total ODA that went to LLDCs. Although full data for ODA in 2020 have not yet been released, based on overall trends, LLDCs are likely to have received higher ODA inflows in 2020[4].

[3] These five LLDCs include: Afghanistan, Ethiopia, Mali, Uganda and South Sudan
[4] All ODA data is based on OECD (2022) *Official Development Assistance Database,* Online, available at: https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/official-development-assistance.htm

Although recent trends are encouraging, LLDCs need enhanced ODA support. ODA will be vitally important means for LLDCs to support national responses to the COVID-19 crisis, as well as the achievement of long-term development goals. For 45% of the LLDCs (15 of the 32), ODA constitutes more than 5 per cent of gross national income (GNI). ODA is important for these countries to continue and enhance investments in health, education and social safety nets, humanitarian needs, as well as supporting productive sectors and recovery.

While the increase in ODA globally by about $10 billion between 2019 and 2020 to $161.2 billion is positive, it is important to ensure the continuity of this trend. Political will and global solidarity are critical to ensure that ODA flows to the most vulnerable countries in particular, including LLDCs, remain on an upward trajectory in the coming years. This will enable ODA to support a long-term recovery and provide impetus to LLDCs key development goals.

In light of this, the following recommendations are proposed:

- Development partners are encouraged to increase ODA to LLDCs and be attentive to support the COVID-19 response.
- Countries of the South should strive to increase financial and technical assistance to LLDCs, in the spirit of solidarity and South-South Cooperation.
- ODA should be leveraged to mobilize other financing resources, including additional private investment through blended finance, support to strengthen domestic resource mobilization, as well as to contribute to further reducing transfer costs of remittances.

Foreign Direct Investment

Foreign Direct Investment flows to LLDCs have been falling since the all-time high of $35.2 billion in 2011. According to UNCTAD, FDI flows to landlocked developing countries declined by 31 per cent from $22.3 billion in 2019 to $15.4 billion in 2020, the lowest level in 15 years. Only 5 LLDCs[5] accounted for more than half of FDI flows in 2020. This came against the backdrop of a 42 per cent decline in global FDI flows in 2020, compared to 2019 levels. UNCTAD also indicated that greenfield announcements of FDI, an indication of future FDI trends, fell by 52 per cent. One encouraging indicator, however, was the 28 per cent increase in the value of international project finance owing to deals in renewable energy and transport infrastructure.

In 2021 according to initial estimates by UNCTAD, global FDI flows showed a strong rebound, up 77% to an estimated $1.65 trillion, from $929 billion in 2020, surpassing their pre-COVID-19 level. However, the recovery has been unequal both in terms of recipient economies as well as types of investment. Firstly, FDI inflows have rebounded a lot more strongly in developed economies compared to developing economies. Secondly, high inflows are being driven more by mergers and acquisitions rather than productive greenfield investments in manufacturing industries or infrastructure.

[5] These five LLDCs in order of FDI inflows include: Kazakhstan, Ethiopia, Myanmar, Uzbekistan and Mongolia

FDI remains an important source of external finance for many LLDCs. Despite FDI recovering in 2021, significant more work needs to be done to attract higher levels of investment and use FDI as a lever for structural transformation and economic diversification. Policy responses by all governments to support their economies will also impact the trajectory of future FDI flow. The role and preparedness of national investment promotion agencies (IPAs) in LLDCs will be important in harnessing FDI for the post-pandemic development priorities.

In light of this, the following recommendations are proposed:

- Development partners should identify adequate means through which to support developing countries, particularly LLDCs, in attracting investment and creating additional incentives to retain investment.
- Donor and investment policy communities should coordinate to mitigate global value chain disruptions and support LLDCs in maintaining their firms' linkages with global and regional production networks and supply chains.
- LLDCs should employ relevant investment policies, as an important tool to cushion the impact of the COVID-19 crisis on FDI inflows.
- Development partners and relevant international organizations should urgently provide capacity building and technical support to IPAs in LLDCs on how best to digitalize investment platforms to reduce costs and time for investment licensing and other related procedures.

Remittances

Remittance flows to LLDCs decreased 6.1 per cent between 2019 and 2020. Travel restrictions and border closures imposed to halt COVID-19 have had an unprecedented impact on migrant labour. In 2021, according to initial estimates, the World Bank expects remittance flows to have increased by 7.3% globally compared to 2020 reaching $583 billion[6]. This would make remittances three times the size of ODA. Two LLDCs, Kyrgyzstan and Tajikistan are amongst the top 5 remittances receiving countries in the world in 2021, in terms of receipts as proportion of GDP. However, the cost of sending remittances globally remains high at 6.4 per cent, well above the SDG target of 3 per cent. While the global increase in remittances in 2021 is encouraging, there is significant potential to further increase flows and harness remittances for sustainable development in LLDCs.

In light of the above, the following recommendations are proposed:

- Governments of host countries and the broader international community should promote the use of digital transfers of remittances and reduce remittance transaction fees, and further consider waiving the transaction fees on remittances to LLDCs for low-income migrant workers indefinitely.
- Policymakers in developed and developing economies should ensure regulated remittance platforms are affordable and accessible to eliminate the use of unauthorized agents.

[6] World Bank (2021) *Migration and Development Brief 35,* World Bank: Washington D.C

- Host countries should prioritize those migrant workers that lost jobs during the pandemic in upcoming employment opportunities when possible.
- Development partners and international financial institutions have a role to play in supporting LLDCs in ensuring that remittances stay stable in case of future crises by proactive planning and risk mitigation.

Debt

Debt levels in LLDCs, which had been on an upwards trajectory until the pandemic struck, rose further in the last two years. External debt increased from an average of 58.1% of GDP in 2019 to 64% of GDP in 2020[7]. 9 LLDCs are classified as being at high risk of debt distress whereas one is characterized as debt distressed[8]. The average total debt servicing came down significantly in 2020, to 17.4% of exports revenues compared to 28% of the export revenues of LLDCs in 2019. However, this sharp reduction was due to temporary debt repayment suspension schemes enacted in response to the pandemic. If LLDCs' debt is not restructured on a long-term basis, the lifting of debt repayment suspension would undoubtedly increase fiscal and balance of payment burdens, which would in-turn threaten both their immediate recovery as well as the attainment of long-term development objectives.

The reliance of the majority of LLDCs on primary commodities for exports means that tepid global economic growth levels may lead to further exacerbation of resource constraints. Exports from LLDCs also continue to be impacted due to the emergence of new COVID-19 variants, on account of periodic movement and transportation restrictions. The resumption of debt repayments coupled with a lacklustre recovery in exports may result in currency devaluations in many LLDCs. With rising spending needs unmatched with commensurate increases in revenue, public debt is likely to increase further and sizably in many countries. High debt servicing can also have indirect costs across many dimensions. For example, an unstable macroeconomic climate may deter much needed investment flows.

To make progress on debt sustainability, the following recommendations are proposed:

- Extend debt moratorium for LLDCs that are in debt.
- Address multilateral debt, specifically for low-income countries and LLDCs.
- Cancel, exchange or reprofile debt for the most vulnerable highly indebted LLDCs.
- Official creditors should consider debt swaps to enhance social investments and address the impact of COVID-19.
- Private and commercial creditors should join debt cancellation and debt moratorium to avoid the public sector bailing out private creditors. Encourage them to improve private sector participation in debt moratoria and alternatives for LLDCs.
- There is need for a more coordinated effort from development finance partners on how to address the emerging debt crisis, through fairer and more effective mechanisms for debt crisis resolution, as well as more responsible borrowing and lending.

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[7] World Bank (2022) *World Development Indicators,* Online, available at: https://databank.worldbank.org/source/world-development-indicators

[8] LLDCs at high risk of debt distress include: Afghanistan, Central African Republic, Chad, Ethiopia, Lao PDR, Malawi, South Sudan, Tajikistan and Zambia. Zimbabwe is characterized as being in debt distress.

International Trade as an engine for development

According to the WTO[9], LLDCs' merchandise exports decreased by about 11% from $190 billion to $167.5 billion in 2020. In comparison, global merchandise exports decreased by about 7.4%. This demonstrates the disproportionate impact of the pandemic on LLDCs. LLDCs' share of the global trade remains below 1% and decreased further in 2020. Although according to initial estimates, global merchandise exports volume grew by 10.8% in 2021, this recovery was highly uneven. Based on regional trade growth trends, it is extremely likely that growth in exports in LLDCs lagged the global average in 2021. This threatens LLDCs of being left behind during the recovery phase, in addition to long-term structural imbalances.

According to a recent study by the WTO, LLDCs' trade costs are 1.4 times higher than those of developing countries with a coastline. These costs were and continue to be further compounded by the COVID-19 pandemic. LLDCs' export revenues are also vulnerable due to a high reliance on natural resources and commodities. On average, the price of all commodities dropped by 21.5% in 2020. In 2021, however, commodity prices rebounded strongly largely driven by energy commodities. After reaching all-time highs in 2021, natural gas and coal prices are expected to decline in 2022 as demand growth slows and supply constraints ease (World Bank, 2022[10]). Crude oil prices are projected to reach $74/bbl in 2022, up from a projected $70/bbl in 2021. The World Bank expects agricultural commodities to broadly stabilize in 2022. Although higher energy prices may increase exports from oil and gas exporting LLDCs, they may add result in balance of payments imbalances in others.

The COVID-19 pandemic has also made it more difficult for LLDCs to integrate in global and regional value chains. Global value chains (GVCs) are highly sensitive to trade inefficiencies both in terms of costs and transportation time. According to UN-OHRLLS[11] estimates, before the COVID-19 pandemic, LLDCs' participation in total GVC trade was only 0.45%, and this has likely gone down further in the last two years. LLDCs need multifaceted support to increase their participation in GVCs as a key part of their efforts to build back better due to the effect that this can have on reducing resource dependency and promoting economic diversification.

The digital economy and e-commerce have great potential in integrating the LLDCs particularly their Small and Medium Enterprises into global trade especially during COVID-19 pandemic. LLDCs are however confronted with challenges in accessing benefits from the increasing digitalization of the global economy. These include, inadequate ICT infrastructure, unreliable and costly power supply, underdeveloped financial systems, weak legal frameworks and low levels of information and communications technology (ICT) literacy. It is important that these challenges are addressed to ensure that the LLDCs are able to fully utilize domestic and cross-border e-commerce and tap into the benefits offered by emerging technology intensive industries.

[9] WTO (2021) *International Trade and Tariff Data,* Online, available at: https://www.wto.org/english/res_e/statis_e/statis_e.htm
[10] World Bank (2021) Commodity Markets Outlook October 2021, World Bank: Washington D.C.
[11] UN-OHRLLS (forthcoming) *Harnessing Global and Regional Value Chains to Promote Development in LLDCs,* UN-OHRLLS: New York

The integration of the LLDCs in the global trade is vital for the achievement of the 2030 Agenda. Whereas it is the responsibility of the LLDCs to adopt enabling national trade policies, the enabling global trading environment is an essential element to facilitate the integration of the LLDCs. There is need to pursue an inclusive and developmental multilateralism in line with the 2030 Agenda to enable vulnerable countries like the LLDCs to benefit from international trade.

In light of this, the following recommendations are suggested:

- Development partners, the United Nations, the International Financial Institutions, and other international organizations should support LLDCs to build their productive capacities, promote value-addition and diversify their economies. Building dynamic productive capacity should involve shifting focus from narrow specialization to the expansion of manufacturing bases.
- Address the high trade costs faced by LLDCs through increased investment into all forms of connectivity – transport, digital and energy is critical for trade facilitation and increased trade potential. Efforts must be stepped up to bridge the enormous connectivity gaps between LLDCs and the developed world and between urban and rural areas.
- The pandemic has underscored the importance of a strong rules-based multilateralism, including a commitment to maintain open and free trade; a commitment to keep borders opens, with restrictions only for legitimate reasons. Emergency measures designed to tackle COVID-19 and any future crises must be temporary, transparent, targeted, proportionate, and be consistent with WTO rules.
- Address supply chain disruptions through targeted international support for LLDCs.
- Enhance support to LLDCs, including towards enhanced use of ICT at the borders, towards the implementation of the WTO Trade Facilitation Agreement by transit countries and LLDCs is fundamental and there is therefore a need.
- Ensure enhanced transparency and efficient information.
- Support LLDCs to build capacities needed for them to take advantage of the opportunities of the digital economy and e-commerce.
- In the long-term, while implementing methods for structural economic transformation, LLDCs need to consider methods to diversify their exports and drive down the product concentration index value.

The WTO's 12th Ministerial Conference should deliver favorable outcomes for marginalized countries Members of the Organization including the LLDCs.