# Graduating LDCs: Financing Challenges Ahead

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***Joint UN Workshop on Preparing for a Smooth Graduation from the LDC Category***



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# The Unfolding Graduation Scenario

- 12 (out of 47) LDCs to graduate by 2024

| Graduating countries | Recommended for graduation by the CDP, ECOSOC decision deferred to 2021 | Considered for graduation by the CDP in 2021 (deferred from 2018) | Considered for graduation by the CDP in 2021 (met criteria for the first time in 2018) |
|---|---|---|---|
| Vanuatu (2020)<br>Angola (2021)<br>Bhutan (2023)<br>Sao Tome and Principe (2024)<br>Solomon Islands (2024) | Tuvalu<br>Kiribati | Nepal<br>Timor-Leste | Bangladesh<br>Lao PDR<br>Myanmar |

Note: Year in bracket is the year of graduation from the LDC category

# The Unfolding Graduation Scenario

**Profile of 12 graduating (25%) LDCs**

- 6 SIDS
- 2 LLDC
- 11 LMICs, 1 LIC (Nepal)
- 2 oil exporting LDCs (Angola and Timor-Leste)
- 4 in World Bank's Harmonised list of Fragile States (Kiribati, Myanmar, Solomon Islands, Tuvalu)
- **All vulnerable to the impact of Climate Change!**

**Table: LDCs' share in World and Graduating LDCs' share in all LDCs in 2017/2018**

| Indicator | All LDCs (Share of world) | 12 Graduating LDCS (Share of all LDCs) |
|---|---|---|
| Population | 13.5% | 28.16% |
| GDP | 1.26% | **47.27%** |
| Merchandise export | .98% | **54.3%** |
| FDI | 1.84% | 12.74% |
| Remittance | 6.02% | **57.56%** |
| Gross ODA Disbursements | 22.25% | 17.81% |
| Net ODA Received | 29.91% | 16.57% |
| Private Philanthropy | 11.74% | 11.03% |
| Private finance mobilised by ODA (Annual Average over 2012-2017) | 6% | **34%** |

Source: UNCTADSTAT, OECDSTAT, IMF, WDI (2019)

# The Financial Concerns of Graduating LDCs

**Table: Snapshot of External Sector Dependence for Graduating LDCs**

| | Exports of Goods and Services (% of GDP) 2018 | Merchandise Exports (% of M. imports) 2018 | Current Account (% of GDP) 2017 | Balance of Payment (% of GDP) 2017 | Tax Revenue (% of GDP) 2017 |
|---|---|---|---|---|---|
| All LDCS | 19.69 | 70.63 | -4.52 | .. | 13.89 |
| Graduating LDCs | **32.72** | 57.70 | -3.11 | -6.04 | 14.90 |
| Graduating SIDS | **42.83** | **22.26** | 0.69 | **-18.76** | **15.89** |
| Graduating non-SIDS | 22.61 | **93.13** | **-6.92** | -4.94 | 13.72 |

Source: UNCTADSTAT, OECDSTAT, IMF, WDI (2019)

- Graduating LDCs can finance around **60 per cent** of their merchandise imports with merchandise exports. However, Non-SIDS (probably because of oil exporting Angola) can finance **93 per cent** of imports through export revenues.
- Exports contributed largely to GDP of SIDS most likely driven by their Tourism industry
- All graduating LDCs( except Kiribati and Tuvalu) had current account deficits in 2017.
- Graduating SIDs better at revenue mobilisation than LDCs, graduating LDCs and non-SIDS graduation LDCs on average.

# Lessons from Graduated Countries

## Changes in Key Indicators of former LDCs

| Graduated County | CABO VERDE | | MALDIVES | | SAMOA | |
|---|---|---|---|---|---|---|
| **Indicator** | **Before Grad (4-5 years)** | **After Grad ( 4-5 years)** | **Before Grad (4-5 years)** | **After Grad ( 4-5 years)** | **Before Grad (4-5 years)** | **After Grad (4-5 years)** |
| **Real GDP growth (%)** | 7.22% | **2.30%** | 6.25% | **5.96%** | 0.42% | **2.52%** |
| **Current Account (% of GDP)** | -8.71% | **-10.44%** | -14.24% | **-13.18%** | -5.63% | **-3.09%** |
| **Merchandise exports (% of GDP)** | 1.68% | **3.05%** | 12.08% | **8.53%** | 9.00% | **6.45%** |
| **FDI (% of GDP)** | 5.49% | **8.78%** | 2.36% | **10.18%** | 1.59% | **1.90%** |
| **Remittances (% of GDP)** | 12.22% | **9.88%** | 0.23% | **0.10%** | 20.83% | **17.69%** |
| **Tax revenue (% of GDP)** | 17.38% | **19.41%** | 10.78% | **17.87%** | 20.72% | **23.55%** |
| **Net ODA in USD million** | 158.522 | **200.068** | 46.62 | **33.04** | 97.44 | **101.63** |
| **Net ODA (% of GNI)** | 18.32% | **12.89%** | 2.99% | **1.15%** | 15.59% | **12.86%** |
| **Net OOF (% of GNI)** | 5.31% | **2.30%** | 2.03% | **0.46%** | 0.67% | **0.39%** |
| **External Debt Stock (% of GNI)** | 54.01% | **67.41%** | 42.26% | **34.29%** | 52.72% | **54.73%** |

Source: UNCTADSTAT, OECDSTAT, IMF, WDI (2019)

# Lessons from Graduated Countries

**(Based on three country experiences)**

## Obvious Increases in Indicators after Graduation

- FDI percentage of GDP
- Tax revenue as a percentage of GDP

## Obvious decreases in Indicators after Graduation

- Net ODA as a percentage of GNI
- Net OOF as a percentage of GNI
- Remittance as a percentage of GDP

## Mixed Trends

- GDP Growth improved for two, declined for one
- Current Account (% of GDP) improved for two, deteriorated for one
- Merchandise exports (% of GDP) increased for one, decreased for two
- External Debt Stock (% of GNI) increased for two, decreased for one

# The Financial Flashpoints of Graduating LDCs

**Table: External Finance Flows**

| | ODA per capita (USD) 2017 | Net ODA (% of GNI) 2017 | OOF (% of GNI) 2017 | Private Philant-hropy (% of GNI) 2017 | Private finance mobilised by ODA (% of GNI) Annual avg. of 2012-2017 | Aid for Trade ( % of GNI) 2017 | FDI (% of GDP) 2018 | Remittance (% of GDP) 2017 |
|---|---|---|---|---|---|---|---|---|
| Graduating LDCs | 379.66 | 11.19 | 0.24 | 0.02 | 0.07 | 5.41 | 1.73 | 5.76 |
| Graduating SIDS | 706.11 | 19.52 | 0.17 | 0.01 | 0.02 | 9.22 | 1.89 | 5.40 |
| Graduating non-SIDS | 53.21 | 2.87 | 0.31 | 0.02 | 0.13 | 1.61 | 1.56 | 6.11 |

Source: UNCTADSTAT, OECDSTAT, IMF, WDI (2019)

- Dependence on ODA is greater for SIDS whereas dependence on OOF is greater for non-SIDS graduating LDCs. SIDS get significantly higher ODA per capita compared to non-SIDS graduating LDCs.
- Graduating SIDS receive minimal private philanthropy compared to their non-SIDS counterparts
- Graduating SIDS also have minimal private finance mobilised through blended finance operations.
- Graduating SIDS get a higher share of their GNI as Aid for Trade compared to non-SIDS

# The Financial Flashpoints of Graduating LDCs

**Table: Share of Net ODA Received**

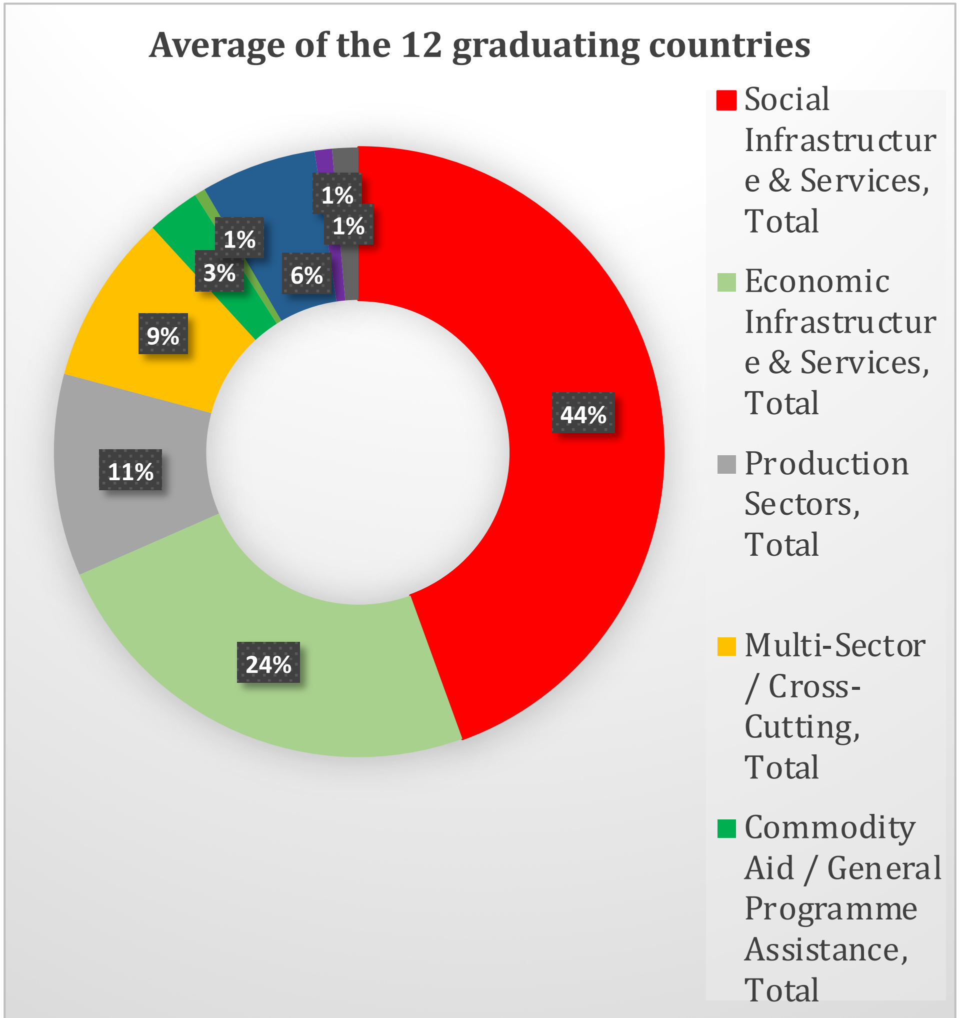
| | 2010 | 2015 | 2016 | 2017 |
|---|---|---|---|---|
| LDCs' share in World | 33.86 | 28.22 | 27.46 | 29.91 |
| Graduating LDCs' share in World | 3.02 | 4.38 | 4.04 | 4.96 |
| Graduating LDCs' share in All LDCs | 8.93 | 15.53 | 14.71 | 16.57 |
| Graduating SIDS' share in All LDCs | 1.82 | 1.81 | 1.55 | 1.42 |
| Graduating non-SIDS LDCs' share in All LDCs | 7.11 | 13.72 | 13.16 | 15.14 |

Source: OECDSTAT (2019)

- LDCs' share in total net ODA received by all developing countries have declined since 2008, only picking up slightly since 2015
- However, graduating LDCs share in total net ODA received by LDCs have improved over the years implying ODA may have played an important part in pushing LDCs towards graduation.
- This increase has been mostly due to the higher share of ODA received by non-SIDS graduating LDCs.

# The Financial Flashpoints of Graduating LDCs

**Figure: Sectoral composition of ODA as a share of total of all sectors (2017)**




- Highest share of ODA is allocated for **Social Infrastructure and services**- **44.91%.**
  - The exceptions, **Bhutan**, **Tuvalu** and **Vanuatu**
  - These have highest share of ODA allocated for **Economic Infrastructure and services** (27.47%, 36.50%, 40.34% respectively).
- For Social Infrastructure and services: (average of **SIDS-44.99%**; **Non-SIDS-44.82%**); for Economic Infrastructure and services: (average of **SIDS-26.79%**, **Non-SIDS-21.61%)**
  - In contrast, for Humanitarian Aid, **Non-SIDS' average allocation is 9.57% as opposed to SIDS' allocation of 2.81%.**
  - **Bhutan** has the highest allocation for Humanitarian Aid followed by **Myanmar & Nepal**(18.52%, 12.89%, 10.61% respectively)

Source: OECDSTAT (2019)

# The Financial Flashpoints of Graduating LDCs

**Table: ODA/ OOF Flow & Composition**

| | ODA & OOF share of the total flow | | Technical cooperation as a share of ODA | Share of ODA disbursed by multilateral and bilaterals (2017) | | Share of OOF disbursed by multilateral and bilaterals (2017) | |
|---|---|---|---|---|---|---|---|
| Recipients | ODA (%) | OOF (%) | Technical Cooperation(%) | Multilateral (%) | Bilateral (%) | Multilateral( %) | Bilateral (%) |
| Average of the 12 Countries | 87.84 | 12.16 | 18.61 | 44.66 | 55.34 | 23.34 | 76.66 |
| Average of SIDs | 98.51 | 1.49 | 25.65 | 39.10 | 60.90 | 15.19 | 84.81 |
| Average of Non-SIDS | 77.16 | 22.84 | 11.56 | 50.22 | 49.78 | 30.12 | 69.88 |

Source: OECDSTAT(2019)

- Except for Angola, all **11 countries have higher share of ODA compared to OOF** in total official flow.
  - ➢ Among **SIDS** this difference between **ODA and OOF (98.51% & 1.49%)** is **more prominent** than **Non-SIDS (77.16% & 22.84%)**
- of the total ODA disbursement, on an average **18.61%** is allocated for technical cooperation. Technical cooperation is more prominent among **SIDS (25.65%)** than **Non-SIDS (11.56%).**
- For **SIDS** highest share of ODA comes from **bilateral sources (60.90%)**. In contrast, **Non-SIDS have a balanced share of ODA source**; 50.22% from multilaterals and 49.78% from bilaterals.
- For OOF, both SIDS and Non-SIDS are mostly reliant on Bilateral Sources.
  - ➢ **Non-SIDS** reliance on **multilaterals** for OOF **(30.12%)** is double than that of **SIDS (15.19%)**

# The Financial Flashpoints of Graduating LDCs

| External debt stocks (% of GNI) | | | | | |
|---|---|---|---|---|---|
| **Country Name** | **2010** | **2015** | **2016** | **2017** | **2018** |
| **Graduating Countries** | | | | | |
| **Bangladesh** | 21.57 | 17.48 | 16.58 | 18.11 | 18.19 |
| **Bhutan** | 62.41 | 104.91 | 112.56 | 112.65 | 109.24 |
| **Solomon Islands** | 46.47 | 18.51 | 22.73 | 30.79 | 29.08 |
| **Graduated Countries** | | | | | |
| **Cabo Verde** | 56.09 | 100.31 | 96.20 | 103.01 | 89.30 |
| **Maldives** | 40.26 | 26.71 | 29.45 | 32.70 | 47.98 |
| **Samoa** | N/A | N/A | N/A | N/A | N/A |

WDI, 2019

- Both Bangladesh and Solomon Islands show **declining trends**.
- Whereas, Bhutan shows **increasing trend**

# The Financial Flashpoints of Graduating LDCs

| Short-term debt (% of total external debt) | | | | | |
|---|---|---|---|---|---|
| **Country Name** | **2010** | **2015** | **2016** | **2017** | **2018** |
| **Graduating countries** | | | | | |
| **Bangladesh** | 10.97 | 18.27 | 20.18 | 22.83 | 17.33 |
| **Bhutan** | 0.64 | 0.00 | 0.00 | 0.12 | 0.17 |
| **Solomon Islands** | 1.74 | 10.47 | 13.16 | 7.40 | 11.08 |
| **Graduated Countries** | | | | | |
| **Cabo Verde** | 0.17 | 0.10 | 0.10 | 0.09 | 0.09 |
| **Maldives** | 15.92 | 15.60 | 10.86 | 7.63 | 11.27 |
| **Samoa** | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |

WDI, 2019

Both Bangladesh and Solomon Islands show **increasing trends**.

Whereas, Bhutan shows slightly **declining trend**

For Solomon Islands, Central government debt (as a share of GDP) **dropped** from **15.89%** in **2011** to **7.63%** and **7.00%** in **2015** and **2016** respectively.

# The Financial Flashpoints of Graduating LDCs

| World Bank's country Classification | | | |
|---|---|---|---|
| IDA Only (unless Creditworthy) | Blend (unless not creditworthy) | IBRD (after successful IDA graduation) | Donor (after successful IBRD graduation) |
| < $1025 | $1185 - $1945 | $1945 - $7025 | $12475< |

Source: modified after (Centre for Global Development (cgdev), 2016)

| | |
|---|---|
| IDA only | Eritrea, Somalia, Sudan, Syrian Arab republic, Afghanistan, Benin, Burkina Faso, Burundi, Cambodia, Central African republic, Chad, Comoros, Congo Dem. Rep., Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Kyrgyz Republic, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Nepal, Niger, Rwanda, Senegal, Sierra Leon, South Sudan, Tajikistan, Tanzania, Togo, Uganda, Yemen Rep. |
| Gap | **Myanmar**, Nicaragua, **Zambia**, **Bangladesh**, **Djibouti**, **Bhutan**, Guyana |
| Blend | Cameroon, Congo Rep., Kenya, Moldova, Mongolia, Nigeria, Pakistan, Papua New Guinea, Uzbekistan, **Timor-leste**, St. Lucia, St. Vincent and the Grenadines, Cape Verde, Dominica, Grenada, Zimbabwe |
| IBRD | Bolivia, Sri Lanka, Vietnam |

(World Bank, 2018)

# The Financial Flashpoints of Graduating LDCs

| | |
|---|---|
| **IDA only** | Eritrea, Somalia, Sudan, Syrian Arab republic, Afghanistan, Benin, Burkina Faso, Burundi, Cambodia, Central African republic, Chad, Comoros, Congo Dem. Rep., Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Kyrgyz Republic, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Nepal, Niger, Rwanda, Senegal, Sierra Leon, South Sudan, Tajikistan, Tanzania, Togo, Uganda, Yemen Rep. |
| **Gap** | **Myanmar**, Nicaragua, **Zambia**, **Bangladesh**, **Djibouti**, **Bhutan**, Guyana |
| **Blend** | Cameroon, Congo Rep., Kenya, Moldova, Mongolia, Nigeria, Pakistan, Papua New Guinea, Uzbekistan, **Timor-leste**, St. Lucia, St. Vincent and the Grenadines, Cape Verde, Dominica, Grenada, Zimbabwe |
| **IBRD** | Bolivia, Sri Lanka, Vietnam |

(World Bank, 2018)

**Solomon Islands is categorized separately as Small Island**.

# The Financial Flashpoints of Graduating LDCs

The IDA graduation process involves multiple stages, offering countries an opportunity to gradually adjust to tighter terms of financing as they move from
**IDA-only non-gap → IDA-only gap → IDA-blend →then graduate to IBRD-only status**

- an LIC becomes an LMIC when its income crosses what's known as the "civil works preference" threshold, currently **$1,025** (FY17)
- IDA graduation process is not triggered until countries cross the "operational cutoff," currently **$1,185** (FY17)
- The IBRD only lends to countries it finds creditworthy.
- Although IBRD's credit worthiness assessment is more lenient than market assessment, still several countries fail to meet this standard. These are **Gap countries**. They continue receiving loans from IDA, although they are expected to take steps to improve their creditworthiness.
- Sometimes the Bank recommends or discourages a country's IDA graduation due to factors such as political instability, poverty, debt sustainability.

# The Financial Flashpoints of Graduating LDCs

**Asian Development Bank (ADB):** ADB divides countries in 3 categories depending on their creditworthiness (UN, CDP, n.d.).

- LDCs that are no longer low-income countries and that “lack” creditworthiness are provided concessional assistance only (as opposed to blended finance for countries of similar income that are not LDCs)
- countries that are no longer low-income countries but that have “adequate” creditworthiness have access to blended finance (as opposed to ordinary capital resources only countries with a similar level of income that are not LDCs)
- For countries considered of “limited” creditworthiness, whether or not the country is an LDC does not change the terms of loans.

# The Financial Flashpoints of Graduating LDCs

**ADB's Classification of Developing Member countries**:

| | |
|---|---|
| **Group A (Concessional assistance-only)** | Afghanistan, Bhutan, Cambodia, Kiribati, Kyrgyz Republic, Federated States of Micronesia, Lao People's Democratic Republic, Maldives, Marshall Islands, Myanmar, Nauru, Nepal, Samoa, Solomon Islands, Tajikistan, Tonga, Tuvalu, Vanuatu. |
| **Group B (Ordinary Capital Resources Blend)** | Bangladesh, India, Mongolia, Pakistan, Palau, Papua New Guinea, Timor-Leste, Uzbekistan. |
| **Group C (Regular Ordinary Capital Resources-only)** | Armenia, Azerbaijan, People's Republic of China, Cook Islands, Fiji, Georgia, Indonesia, Kazakhstan, Malaysia, Philippines, Sri Lanka, Thailand, Turkmenistan, Viet Nam. |

Source: (ADB, 2019)

# Exposure to Non-Conventional Financing instruments

- **Blended finance:** is broadly understood as the strategic combination of public and/or private development finance flows (e.g. aid and philanthropic funds) with other public or private capital to enhance resources for investment in key areas such as infrastructure (UNDP and AFD, 2016).
  - Only **6%** of the private finance mobilised by ODA (through different blended finance instruments) in all developing countries are in LDCs. Of this, Graduating LDCs mobilise around **34%** of private finance.
- **Counter-cyclical lending contracts (CCLs):** Under CCLs, it is agreed ex-ante that debt service will automatically be allowed to fall, or become zero, in periods when external shocks hit a country. The instrument has wider applicability to LDCs as a tool to reduce risk and vulnerability (UNDP and AFD, 2016).

# Exposure to Non-Conventional Financing instruments

- **Catastrophe-linked ("CAT-linked") securities:** provide a mechanism for the transfer of catastrophe risks to capital markets, and may provide an additional layer of protection to traditional insurance and reinsurance arrangements or serve to reduce reliance on these arrangements (OECD, 2009).
- **GDP-indexed Bonds:** is a debt security or derivative security in which the authorized issuer (a country) promises to pay a return, in addition to amortization, that varies with the behavior of GDP (UNDESA, 2006).

# Exposure to Non-Conventional Financing instruments – Climate Finance

**Total climate-specific financial flow** during 2015-2016 was **USD 58 billion** of which, only around **20%** went to LDCs (UNFCCC, 2018). There are several funding schemes available which are applicable for LDCs. Some examples-

- ***Global Environment Facility Trust Fund (GEF):*** was established in the **IBRD or World Bank** as a pilot program in order to assist in the protection of the global environment and promote thereby environmentally sound and sustainable economic development.

- ***The Least Developed Countries Fund (LDCF):*** The LDCF, managed by the **Global Environmental Facility (GEF),** was designed to address the special needs of the Least Developed Countries under the UNFCCC. As part of its mandate, the LDCF helps countries prepare and implement National Adaptation Programs of Action (NAPAs).

# Exposure to Non-Conventional Financing instruments – Climate Finance

- ***Adaptation Fund:*** created under the **UNFCCC**. The fund is designed to finance climate change adaptation projects and programs based on the priorities of eligible developing countries.

- ***Special Climate Change Fund (SCCF):*** was established under the **UNFCCC** to finance activities, programs and measures relating to climate change that are complementary to those funded by the resources allocated to the climate change focal area of the Global Environment Facility Trust Fund

# Areas of In-Country Capacity Building Support for Graduating LDCs

**Capacity needs to be built in two phases:**

**1. Pre graduation Phase:**

More "**defensive approach**" to counter-act the possible financial shocks due to graduation

- Support to improve **effective access to concessional finance**
- Support to strengthen **domestic resource mobilisation** (capacity building of tax administrations)
- Support to capacity related to **disaster management** and risk reduction
- Support to capacity development for **enhanced policy and administrative management**
- Support to **statistical capacity building**
- Support to enhance **capacity to negotiate with development and trading partners**

# Areas of In-Country Capacity Building Support for Graduating LDCs

**Capacity needs to be built in two phases:**

**2. Post graduation Phase:**

More "**offensive approach"** to inclusive and sustained economic growth and development

- Most of **pre-graduation phase interventions** to continue
- Support to enable more **access to various finance mix**
- Support to enable **access climate finance**
- Capacity development for **reducing cost of doing business** for promoting private investment
- Capacity development for **improving economic competitiveness** for export promotion

# Need for a Political Strategy

1. To operationalise technical solutions one would need to **broaden the awareness** about the challenges of the graduating LDCs in the **area of finance**
2. **Secure engagement** of the concerned agencies (funders and interlocutors)
3. Creation of an **alliance** in favour of the graduating LDCs
4. Generating **political momentum** through inter-governmental process.

# Need for a Political Strategy

Below are the events/meetings/forums where this issue can be discussed:

- 12th WTO Ministerial Conference
- Aid for Trade review 2021
- the Fifth UN Conference on the LDCs in 2021
- CHOGM 2020, Rwanda

***Thank You***

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