



**Committee for Development Policy**

United Nations Department of Economic and Social Affairs

Development Policy and Analysis Division

**Lessons learned in developing productive capacity  
from graduating LDCs:  
Small island developing states**

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# Context is queen

Three pathways to graduation with different forms of expanding productive capacity for sustainable development:

1. Investing in human assets and in structural transformation away from agriculture into manufacturing and modern services, leading to diversification: eg. **Bangladesh, Ethiopia, Rwanda**
2. Investment in human assets and structural transformation, but economic specialization in a single or very few sectors: **Botswana, Bhutan, Cape Verde, Maldives, Samoa, Vanuatu and Solomon Islands**
3. Rapid economic growth through exploitation of natural resources, which does not require broad investments in human assets. **Angola and Equatorial Guinea.**

# Some lessons

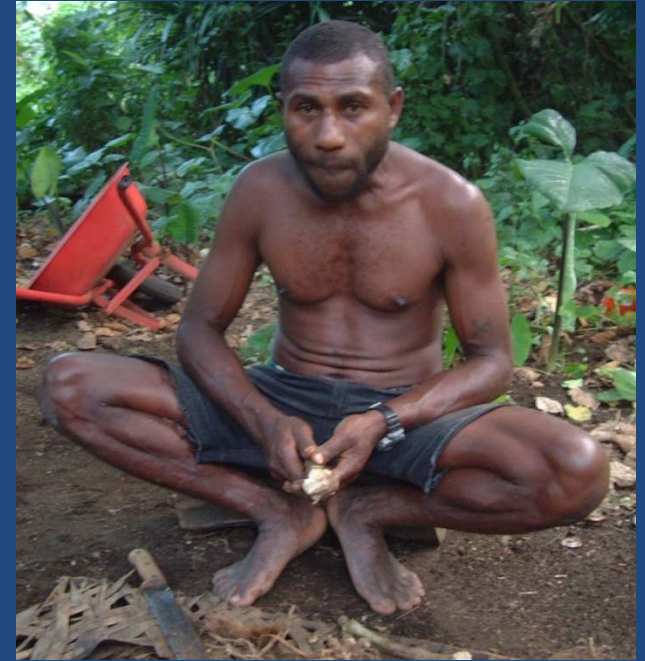
**1.** In most LDCs, particularly those which are culturally or geographically fragmented, **state legitimation** is vital.

- Max Weber: something is "a 'state' if and insofar as its administrative staff successfully upholds a claim on the 'monopoly of the legitimate use of physical force'
- John Locke: the government is not legitimate unless it is carried on with the consent of the governed.
- Vanuatu and Solomon Islands have very different state legitimation

**2. National vision** is extremely important. *It almost doesn't matter what this national vision actually is.*

### Vanuatu

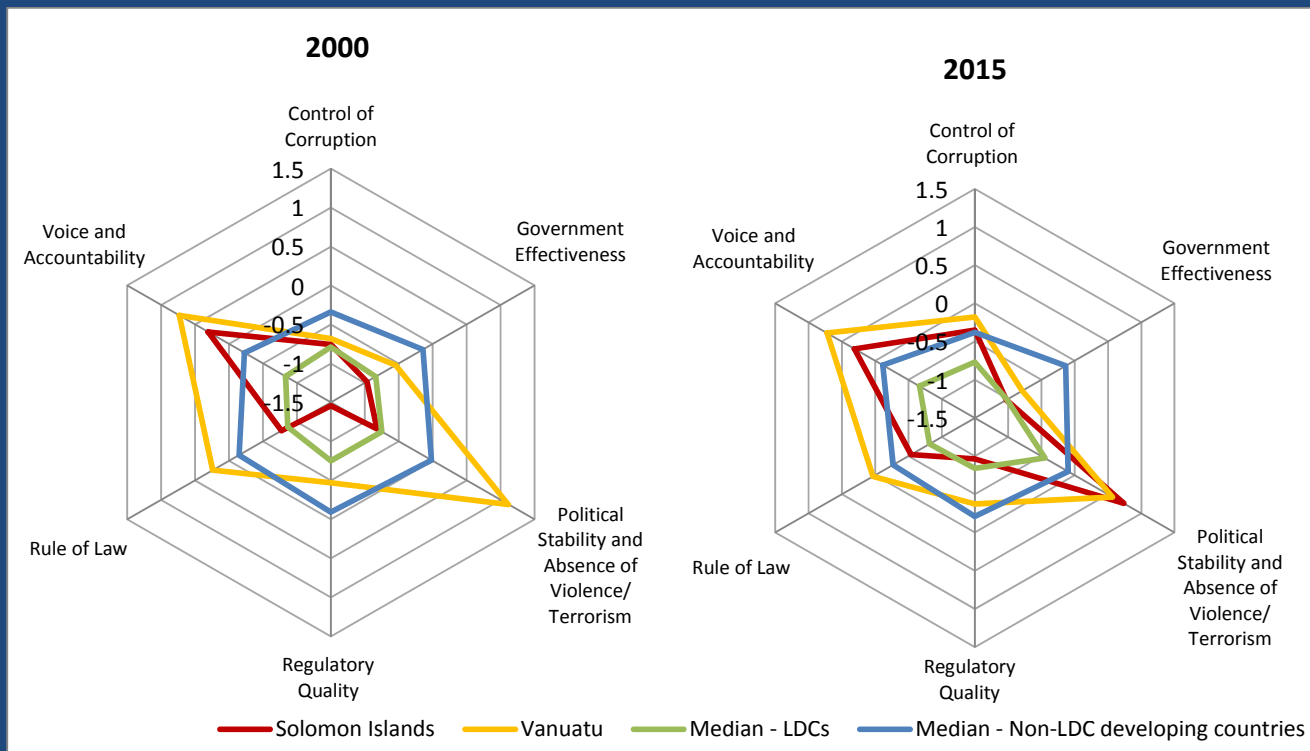
- promotion of 'kastom'.
- 'Happiest' country in the world.
- Strong sense of national identity – membership of non-aligned movement, anti-nuclear stance, etc.
- Rejection, in some cases, of materialist values.



**Bhutan** - Gross National Happiness: “maximize the happiness of all Bhutanese and to enable them to achieve their full and innate potential as human beings.”

- Defines the policy space to channel development in the chosen direction, within limits set by the international context
- Econ. growth is a means to an end, not an end in itself
- Intrinsic environmental benefits, but also strong planning.
- Helps create political legitimacy
- Ensures ‘no-one is left behind’ – equality is central.

### 3. Political stability and peace are prerequisites for sustainable development

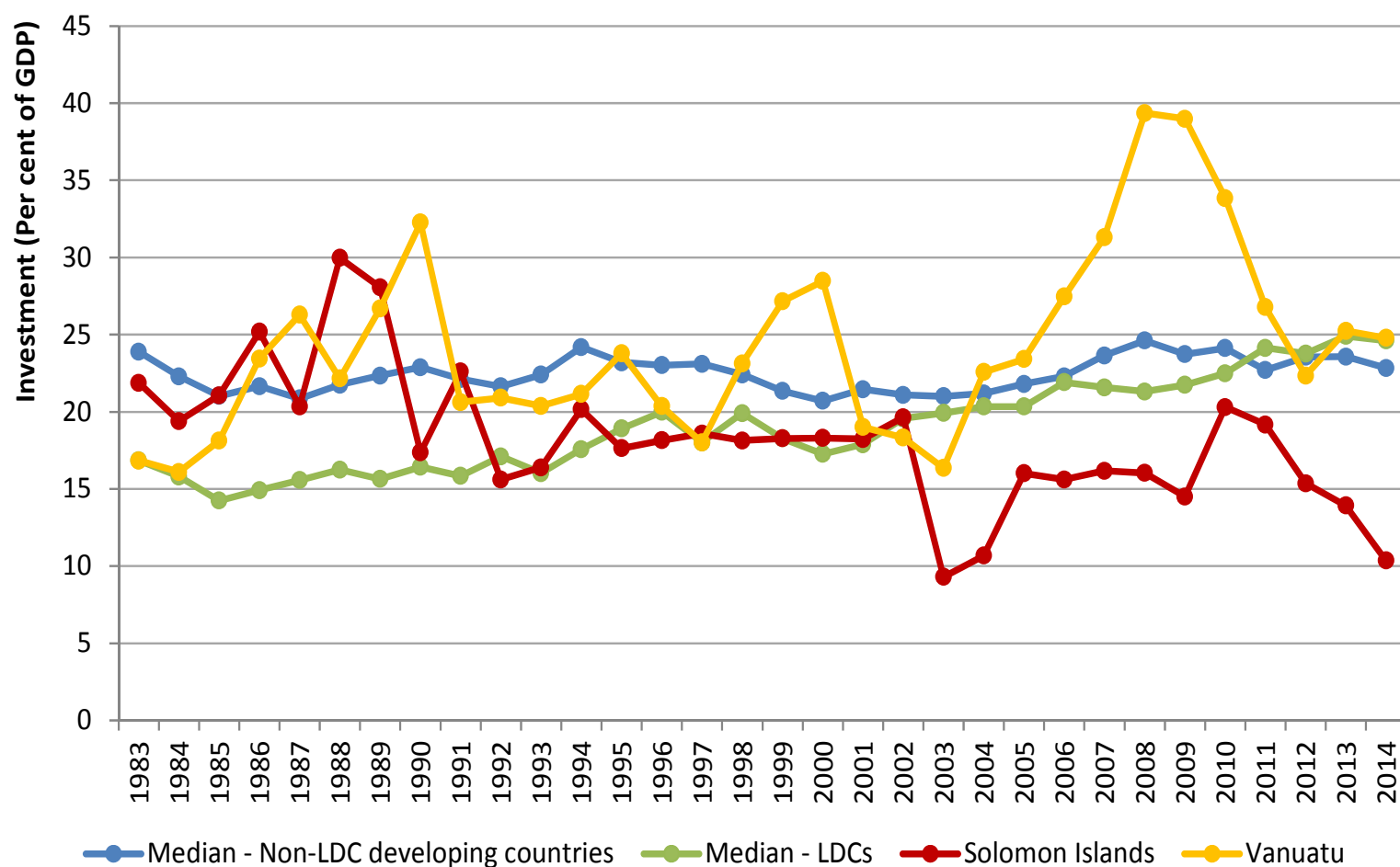


4. In **Vanuatu**, economic transformation is/was underpinned by a high rate of investment, particularly in services for Vanuatu – in the various forms: FDI, aid and domestic public and private financing.

**Vanuatu** - 85 per cent of FDI by value was in the services sector, mostly tourism

- Tax revenues hit 31% of GDP by 2015.
- Solomons in effect was subject to austerity: low debt, fiscal surplus
- In Vanuatu, infrastructure investment in next 5 years is worth half of 2014 GDP. It's a form of soft industrial policy.
- Aid among highest in world, at \$458 per capita in 2010. Considerable aid went to infrastructure.

## Gross fixed capital formation, Solomon Islands and Vanuatu

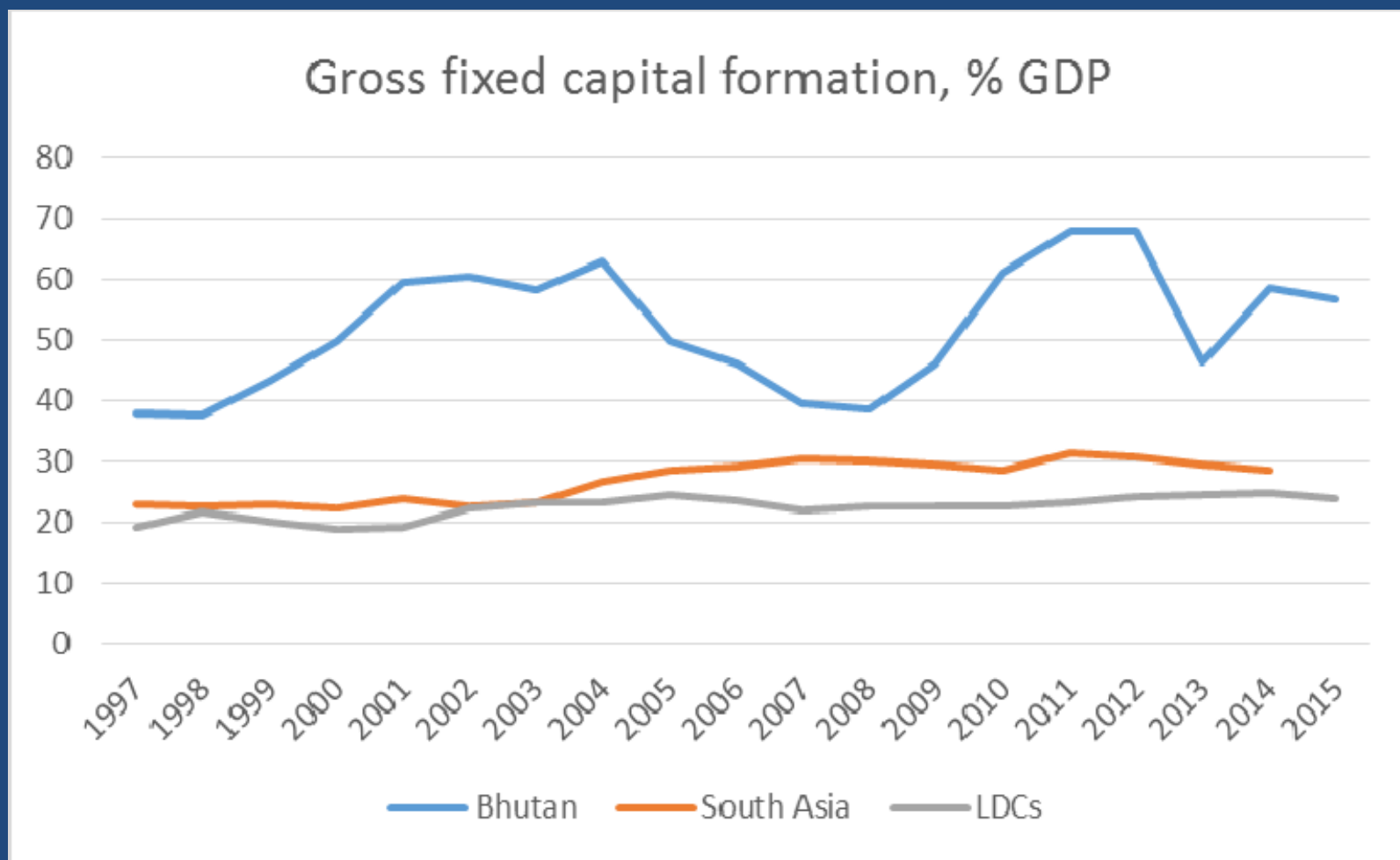




**Bhutan** – currently the highest rate of investment in the world. GFCF 56-58%. Hydropower.

- Also success in attracting aid, both official and unofficial.

## Gross fixed capital formation, Bhutan



**5.** Economic growth and **environmental sustainability** tend to be linked. Unsustainable resource use damages not only the environment, but ultimately also economic development.

- Logging in Solomon islands hindered development and caused social problems
- Vanuatu is, perhaps paradoxically, somewhat fortunate in not having resources.

## 6. Trade policy

- Comparatively more emphasis might be placed on fostering sustainable productive capacity than on domestic or international liberalisation. Eg. Solomons.
  - This requires agency
- Or at least the interaction between the international economic environment and national sustainable productivity capacity should be considered.
- Remittances are increasingly important – Samoa & Cape Verde. Need active trade policies to use them well.
- Limited human resources mean that time, travel costs and emphasis devoted to trade negotiations can detract from efforts to build productive capacity.

**7. There are risks associated with services-based structural transformation**, with its inevitably low levels of productivity and the associated difficulties of creating large-scale employment.

- Vanuatu, Maldives and Cape Verde's development almost all based on tourism and associated services. Remittances increasing.
- But tourism linkages and employment are low
  - You don't make a haircut better by doing it faster.
  - Beethoven's 9<sup>th</sup> can only be played at a certain speed.

# Summary

For these LDCs, and others, the following lessons hold (& probably more):

- 1. Political legitimacy matters.**
- 2. National vision is critical.**
- 3. Political stability and peace are vital.**
- 4. Successful LDCs in this category seem to be characterised by high levels of investment.**
- 5. Economic growth and environmental sustainability are linked.**
- 6. Active trade policies consider the relationship between liberalisation, market access and productive capacity.**
- 7. There are risks associated with services-based structural transformation.**

- **These features are linked** – legitimacy underpins vision and stability.
- Vision and stability help facilitate investment – FDI, public and private.
- Fragmented or illegitimate states tend not to develop sustainably.
- States without legitimacy, vision and stability often don't generate the agency for domestic policies and trade policy aimed at structural transformation.

Thank you