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Improved assistance measures for graduated and graduating least developed countries for the achievement of agenda 2030

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1. Introduction

The category of the least developed countries (LDCs) was created by the General Assembly of the United Nations (GA) in 1971 in recognition of the substantial developmental gaps that existed between the poorest and the relatively more advanced developing countries. LDCs needed special measures—beyond what had been commonly available to all developing countries—to overcome their structural obstacles to development and close that gap. These special measures often fall in three main areas: international trade, development assistance, including development finance and technical cooperation, and general support (UN CDP, 2015).

Initially composed of 25 countries, the category increased in number reaching a peak of 51 countries in 2003. Currently, it is comprised of 47 countries. The Committee for Development Policy (CDP), an advisory body to the Economic and Social Council (ECOSOC), is mandated to make recommendations on countries' inclusion in and graduation from the category. CDP recommendations are to be endorsed and approved by ECOSOC and the GA.

Being partially the result of a political process, the graduation decision-making process has faced its own challenges. Different from other graduations (e.g., IDA, OECD-DAC, etc.), LDCs have a say in the process and can influence outcomes. As LDCs voice their reservations about their own graduation, negotiations do not always lead to consensus and graduation is stalled. At the same time, this resistance to graduation has contributed to a series of refinements of the LDC classification criteria and of the CDP procedures—most notably by the introduction of the economic vulnerability index (EVI), country consultations, the vulnerability profile and impact assessment reports. It has also led to the adoption of improved processes and measures by the concerned intergovernmental bodies, such as the two resolutions of the GA on the smooth transition strategy.[1]

LDC graduation has become an increasingly important issue in the international development agenda. Meeting graduation eligibility is a major goal of the Istanbul Plan of Action for the Least Developed Countries for the decade 201-2020 (IPoA). But as countries' concerns about graduation persist, the potential for additional tension has widened, particularly now that an increasing number of LDCs approach graduation. Currently, two countries are to be graduated in 2020-2021 (Angola and Vanuatu). At the 2018 triennial review of the list of LDCs, five other countries have been recommended to graduate and await the conclusion of the intergovernmental process (Bhutan, Kiribati, Sao Tome e Principe, Solomon Islands and Tuvalu)). Additionally, five other countries (Bangladesh, Lao PDR, Myanmar, Nepal and Timor-Leste) met the graduation eligibility and will be reviewed for a graduation recommendation in 2021.

Countries' reservations are centred on the potential negative impact that the withdrawal of LDC-specific measures can cause to their development and to the achievement of sustainable development goals as LDC-specific support is withdrawn. While this package of support measures is no silver bullet to address the structural challenges of the group, and while it is not clear whether such package has had a major role in countries' graduation so far, individual measures have proved to be beneficial in specific contexts. Another concern manifested by the LDCs is the absence of a clear road map to navigate through transition and graduation. Despite the guidelines issued by the GA, smooth transition recommendations have only been partially applied. Implementation has largely focused on the aspect of withdrawing and/or phasing-out of LDC-specific support rather than putting in place a renewed cooperation framework for supporting the country in its development efforts after graduation.

[1] General Assembly resolution 59/09 of 20 December 2004 and resolution 67/221 of 21 December 2012 on smooth transition strategy for countries graduating from the list of least developed countries.

In view of the above, the CDP decided to take further research and analysis on this matter and address some of the most pressing concerns related to graduation (CDP Secretariat, 2018). This paper is a contribution to that effort. It does not aim to be comprehensive given the vastness of the subject (the achievement of sustainable development at the country level) and the heterogeneity of the group which implies different development trajectories and needs (Cornia and Scognanillo, 2016). Similarly, it does not intend to create a new category or a subset of countries within the LDC category. Rather, the paper focuses on a set of suggestions that implies a more robust package of support to facilitate the graduation process and ease of some of the concerns of graduation-eligible countries. This set of suggestions has a strong emphasis on policy advice and technical cooperation for capacity building. It improves upon the existing framework by identifying areas where it could work better and detecting resources that may be potentially released by graduation.

Recommendations fall into three categories of measures: i) strengthening of the policy advice and technical cooperation framework for smooth transition policy design and implementation; ii) improved and more effective monitoring of the transition process; and, iii) additional support measures for graduating and graduated countries. These recommendations are presented and discussed after section II which introduces a very brief overview of the main features of the LDC category, including access and utilization of LDC-specific support measures, and graduated countries' outcomes.

2. Leaving the LDC category: the process and experiences so far

The CDP defines LDCs as low-income countries suffering from structural handicaps to sustainable development. The identification of the LDCs is based on three criteria: GNI per capita, which provides an indication of the overall level of resources available in the country, and two composite indices: the human asset index (HAI) and the economic vulnerability index (EVI). The HAI provides a proxy of the availability and quality of human capital, while the EVI gives an indication of the country's structural vulnerability to exogenous shocks.

To join the category, the country must satisfy all three criteria and have a population smaller than 75 million people. To be recommended for graduation, countries must satisfy two of the three criteria that classify countries as LDC at their respective graduation thresholds for at least three years. Graduation eligibility is also met when the GNI per capita is twice as high as the income graduation threshold (income-only criterion). Graduation rules were introduced in 1991 when the first triennial review of the LDC list took place.

In establishing a country's readiness to graduate, the CDP relies on two additional reports: an ex-ante impact assessment, prepared by UN DESA in consultation with the country and its development partners, and a vulnerability profile, prepared by UNCTAD. The impact assessment considers the possible implications of graduation due to the loss and/or phasing-out of LDC-specific support related to international trade, development finance and technical assistance. The vulnerability profile aims at giving an overall background of the country development situation. It also assesses country-specific vulnerabilities and structural features that are not captured by the LDC criteria but may be relevant for the graduation decision. These reports are available for the second review of the country's eligibility.

Graduation becomes effective following a three-year transitional period, which starts immediately after the GA takes note of the recommendation of the CDP. On occasion, either due to unforeseeable circumstances or at the country's request, the GA may postpone the date of graduation and grant the country a longer transition period (see Annex table A1). As a graduating country, it remains an LDC and continues to have access to the support measures that are exclusive to the category. The country is also expected to prepare a transition strategy in cooperation with its development partners. This strategy aims at ensuring that the eventual phasing-out of LDC-

specific support does not disrupt the country's sustainable development progress, and it identifies "actions by graduating country and its bilateral and multilateral development and trading partners to that end." (GA resolution A/59/209, para. 4)

2.1. Assessing the potential impact of graduation

One of the consequences of leaving the LDC category is the change in the package of support the country receives from its development partners. LDC-specific support can be grouped into three main areas: i) official development assistance (ODA), which includes grants and other financial flows provided under generous concessional terms, and technical cooperation; ii) measures related to international trade (preferential market access and other forms of special and differential treatment in World Trade Organization (WTO) and regional trade agreements); and, iii) general support, including support in preparation for graduation and after graduation from the LDC category. The role of the various international support measures is likely to differ among countries, as country conditions matter. Additionally, in most cases, it is difficult to disentangle LDC-specific support from other types of support (Cortez, Kinniburg and Mollerus, 2014). With these considerations in mind, the impact assessment report identifies those areas where potential changes in international support may impact on the development trajectory of the graduated country. Impact assessments became first available at the 2009 triennial review.

Although not an LDC-specific measure, development assistance is particularly important for LDCs. It provides both financial inflows, expertise and technical cooperation for capacity building. Graduation is not expected to affect technical assistance programmes as the programmatic allocation by specialized multilateral organizations is not necessarily guided by LDC status (Lanzi, 2017). However, access to LDC-dedicated funds will no longer be possible sometime after graduation. This applies to initiatives such the least developed country fund at the Global Environmental Facility (GEF-LDCF), the Enhanced Integrated Framework (EiF), the United Nations Capital Development Fund (UNCDF), the Investment Support Programme for LDCs (ISP/LDCs) and the Technology Bank for LDCs. Among these, losing access to the LDCF is a main concern for many graduating countries, particularly the small island developing States (SIDS), due to their considerable vulnerability to the impacts of climate change. It also implies that graduating countries will have to compete with other countries for funding from a disadvantaged position due to their relatively weaker administrative and technical capacity.

Turning to development finance, LDC status does not determine access to and lending terms of multilateral loans by the international financial institutions (IFIs) (see section V for further details). Consequently, these flows are not likely to be affected by graduation. However, the modalities of development finance extended by official bilateral donors may change after graduation. Currently, the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD-DAC) recommends member countries to offer an average grant element in ODA to LDCs at either 90 per cent of donor's annual commitments to all LDCs or at least 86 per cent of its commitment to individual countries over a period of 3 years. Furthermore, there is a commitment by donors to untie ODA going to LDCs and highly indebted countries (UN CDP, 2015). Thus, it is possible that grants may become less common and loan concessionality less generous in the financial assistance package extended to graduated countries.[2] The eventual change in ODA modalities needs to be duly considered and addressed by graduating countries in their smooth transition strategies.

[2] For example, in its communication to UN DESA, the EU indicated "there may be a reduction of grant-based aid for countries that are on a sustained growth path or are able to generate sufficient resources of their own, but that the countries graduating from LDC status are unlikely to be in this position immediately after graduation. Future programming cycles would consider specific situations and vulnerabilities." Summary of Impact Assessment, Note by the Secretariat. Committee for Development Policy, 20th plenary session, March 2018.

Preferential market access has been an effective measure adopted in favour of LDCs contributing to increased export revenues relative to countries that do not have access to such measures (Klasen et al, 2016). Naturally, such positive impact depends on existing productive capacities, types of products exported and the country's main export markets, main competitors in these markets and the level of preference granted. Exporters of agricultural products, clothing and textiles and other light manufactures have been the main beneficiaries in view of the relatively high level of tariffs still prevalent on these products in major importing markets. However, thus far, the loss of preferential access has not been a major issue identified by the IAs conducted during the period 2009-2015. This is either because exports have been negligible (Kiribati, Tuvalu) or incurred very low (except for Vanuatu's beef exports to Japan) or zero tariff under the most favoured nation treatment (Angola, Equatorial Guinea) or because countries belong to (or can negotiate access to) other preferential schemes (free trade agreements) whose access is not affected by the change of LDC status. Some graduated countries negotiated extensions and preferential agreements with their main trading partners (e.g., Cabo Verde, Maldives).

Notwithstanding the above, the loss of preferential treatment (not only with respect to tariffs but also with respect to rules of origin that are relatively less strict for LDCs in certain markets) is a relevant issue moving forward, particularly for LDCs that are manufacture exporters, such as Bangladesh and Cambodia. Additionally, LDCs that have joined the WTO in 1995 will lose policy space as they will no longer be exempted from some of the trade disciplines negotiated in that forum. Of these, the requirement to implement the agreement on trade-related aspects of intellectual property rights (TRIPs) may prove to be the most challenging.

While relevant in some contexts, the impact of losing access to LDC-specific support—which is ultimately contingent on how much the development of the country relies upon these measures—should not be exaggerated. Membership in the LDC category overlaps with membership in other categories to which LDCs will continue to belong after graduation and whose benefits they will continue to have access (see table 1). Moreover, no graduated country has reverted to LDC status thus far. Graduated countries have maintained and/or made further progress with respect to LDC indicators (see table 2).

Despite diversity of experiences and approaches, all graduated countries have been able to increase foreign direct investment (FDI) inflows and maintain growth of their export revenues after graduation (see table 3). However, economic growth outcomes have been less uniform across graduated countries. During the five-year period following graduation, Botswana could maintain its relatively high rates of growth, while Samoa succeeded in accelerating growth (based on a three-year period after graduation). Conversely, average growth decelerated both in Cabo Verde and the Maldives in the five-year period following graduation. It is not clear how much graduation has contributed to that deceleration. In the case of Cabo Verde, slower growth has been attributed to the impact of an adverse external environment, including economic difficulties in some key partners, delays in implementing the public investment programme, lower remittances from Cabo Verdeans abroad, and smaller ODA inflows (Mshimyumuremyi, 2018). In the case of the Maldives, deceleration of economic growth has been less sharp than in Cabo Verde, and largely attributed to the end of reconstruction following the tsunami of 2004, vulnerability to the external economic environment and its adverse impact on tourist arrivals, and fiscal consolidation needed to address chronic fiscal deficits (CDP Secretariat, 2018). As a share of GNI, net ODA flows declined in all four graduates (see table 3).

Table 1: LDCs and graduated countries: membership in various initiative and in WTO

Country	SIDS	LLDC	LIC	LMIC	UMIC	HIPC	Fragile States	Access to IDA	Access to PRGT in 2017	WTO membership
Afghanistan							pb			new M
Benin										
Burkina Faso										
Burundi										
Cambodia										new M
Central African Republic							pb			
Chad						dec.p.				on-going
Comoros						dec.p				on-going
Djibouti										
Dem. Rep. of the Congo							pk			
Eritrea						pre.d.				
Ethiopia										on-going
Gambia							pk			
Guinea						dec.p				
Guinea-Bissau							pb			
Haiti							pk			
Lesotho										
Liberia							pk			new M
Madagascar										
Malawi										
Mali							pk			
Mauritania										
Mozambique										
Niger										
Rwanda										
Senegal										
Sierra Leone							pb			
Somalia						pre.d.	pb			on-going
South Sudan							pb			on-going
Sudan						pre.d	pb			on-going
Togo										
Uganda										
United Republic of Tanzania										
Yemen										new M
Zambia										
LDCs meeting eligibility criteria for graduation (5 countries)										
Bangladesh										
Lao PDR										new M
Myanmar										
Nepal										new M
Timor-Leste								blend		
LDCs recommended for graduation by the CDP (5 countries)										
Bhutan										on-going
Kiribati										
Sao Tome and Principe										on-going
Solomon Islands										
Tuvalu										
LDCs in transit to graduation (2 countries)										
Angola								IRBD		
Vanuatu										new M
Total (47 countries)	8	16	28	18	1	31	24	45	46	36
Memo item; graduated countries (5 countries)										
Botswana								IRBD		
Cabo Verde								blend		new M
Equatorial Guinea								IRBD		on-going
Maldives										
Samoa										new M

Notes:
Pre. d. = at pre-decision point in the HIPC process
Dec. p.= decision point in the HIPC process
Blend: country receives blend terms by the Work Bank and has access to both IDA and IBRD resources
IBRD = country only has access to non-concessional recourses from the World Bank.
New M = new member; acceded to WTO after 1995-1997
On-going= accession negations started but have not been completed yet.

Sources:
UN Committee for Development Policy
World Bank. Harmonized list of countries in fragile situations, FY 2019.
World Bank Country and Lending Groups available from https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups
WTO. Least developed countries. https://www.wto.org/english/thewto_e/whatis_e/tif_e/org7_e.htm
IMF, Eligibility to use the Fund's facilities for concessional financing, IMF Policy Paper, May 2017.

Table 2: Graduated, recommended and eligible countries and the LDC criteria

Country (year of recommendation)	At the time of recommendation			At 2018 triennial review		
	GNI	HAI	EVI	GNI	HAI	EVI
Graduated countries						
Botswana (1994)	Y	Y	N	2Y	Y	N
Maldives (2000)	Y	Y	N	2Y	Y	N
Cabo Verde (2003)	Y	Y	N	2Y	Y	N
Samoa (2006)	Y	Y	N	2Y	Y	N
Equatorial Guinea (2009)	2Y	N	N	2Y	N	Y
Recommended countries						
Vanuatu (2012)	2Y	Y	N	2Y	Y	N
Tuvalu (2012)	2Y	Y	N	2Y	Y	N
Angola (2015)	2Y	N	N	2Y	N	N
Kiribati (2018)	2Y	Y	N			
Bhutan (2018)	Y	Y	N			
Sao Tome and Principe (2018)	Y	Y	N			
Solomon Islands (2018)	Y	Y	N			
Memo: eligible countries						
Nepal				N	Y	Y
Timor-Leste				2Y	Y	N
Bhutan				Y	Y	Y
Lao PDR				Y	Y	N
Myanmar				Y	Y	Y

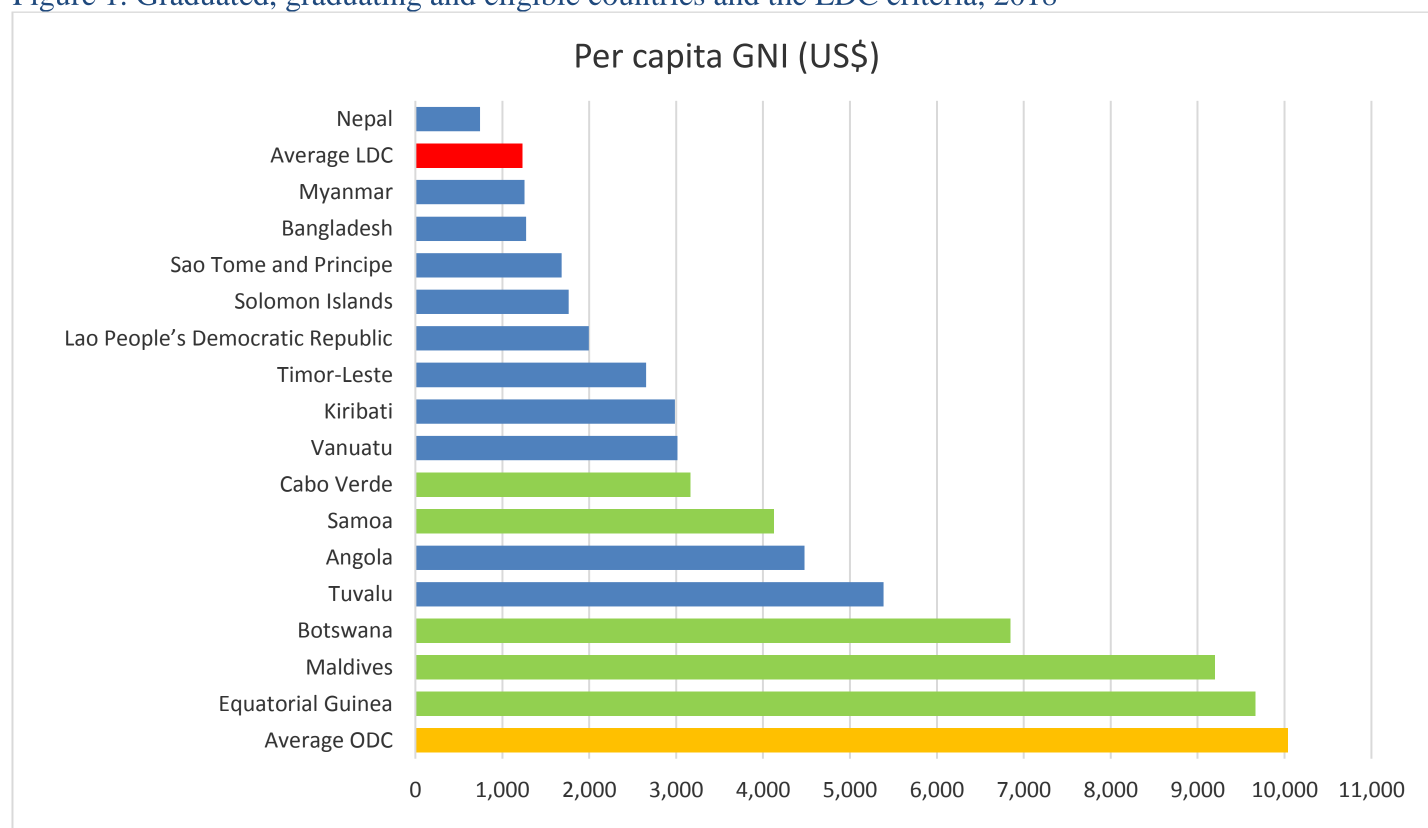
Source: CDP

2.2. Leaving the category, moving forward

It should be noted that none of the countries that graduated so far had explicit graduation policies. Graduation happened because of these countries' overall development strategies. All countries recommended to graduation met two of the three criteria, often the HAI and GNI, or the income-only criterion in the case of fuel exporters, Angola and Equatorial Guinea. EVI has proved to be a more challenging target to meet, even for countries that have left the category for some time (see figure 1 and table 2). Part of the problem has to do with fixed factors

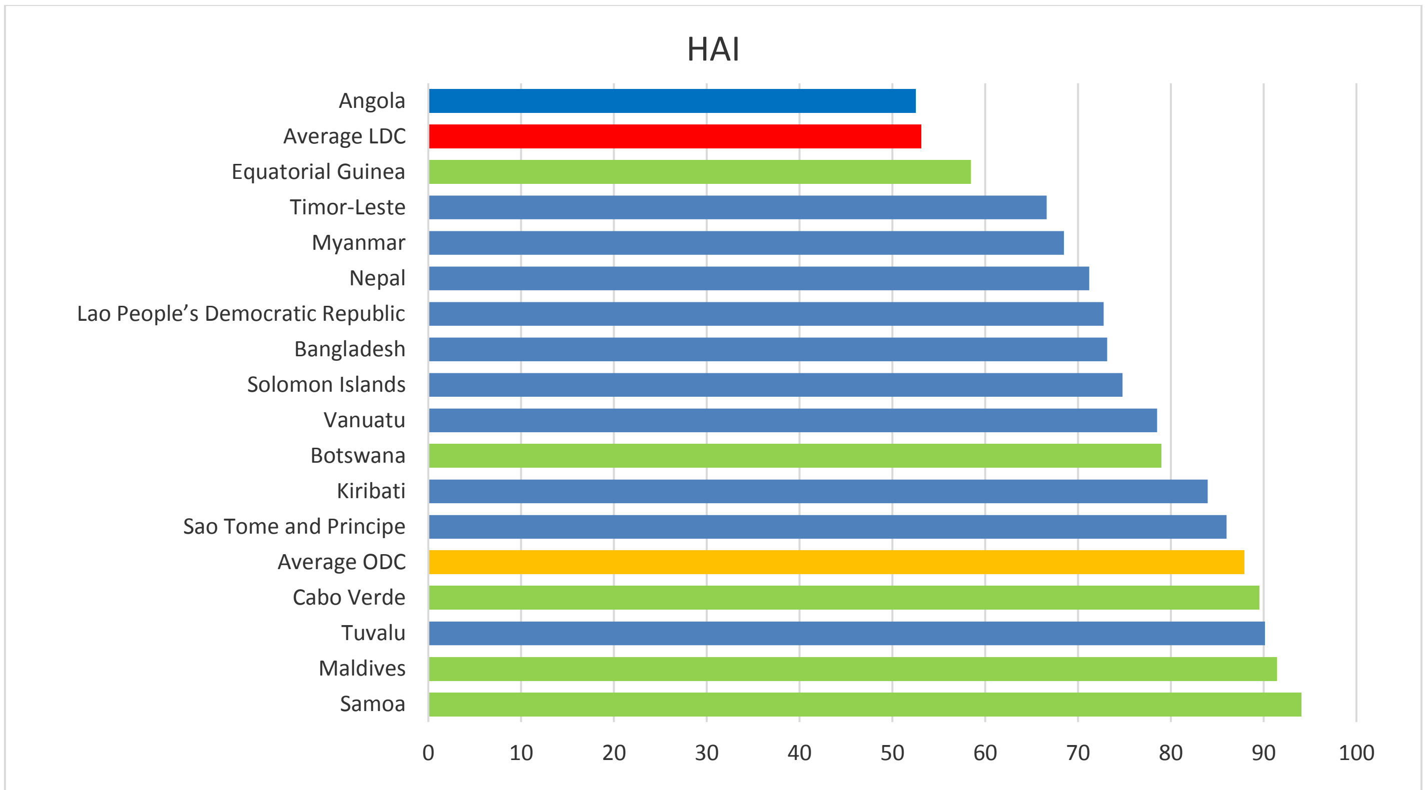
present in the composition of EVI (remoteness, size of population, etc.) which makes it more difficult to be impacted by policy interventions. Difficulty in improving EVI scores also derives from the increased frequency and severity of exogenous economic, financial and environmental shocks affecting these economies. These shocks often offset countries' attempts at reducing exposure and increasing resilience. In fact, the various vulnerability profiles prepared over the years have highlighted the remaining vulnerabilities of graduating countries, particularly those related to dependence on external finance (be it ODA or labour remittances), climatic and other natural shocks, limited structural transformation of the economy and insipient technological upgrading.

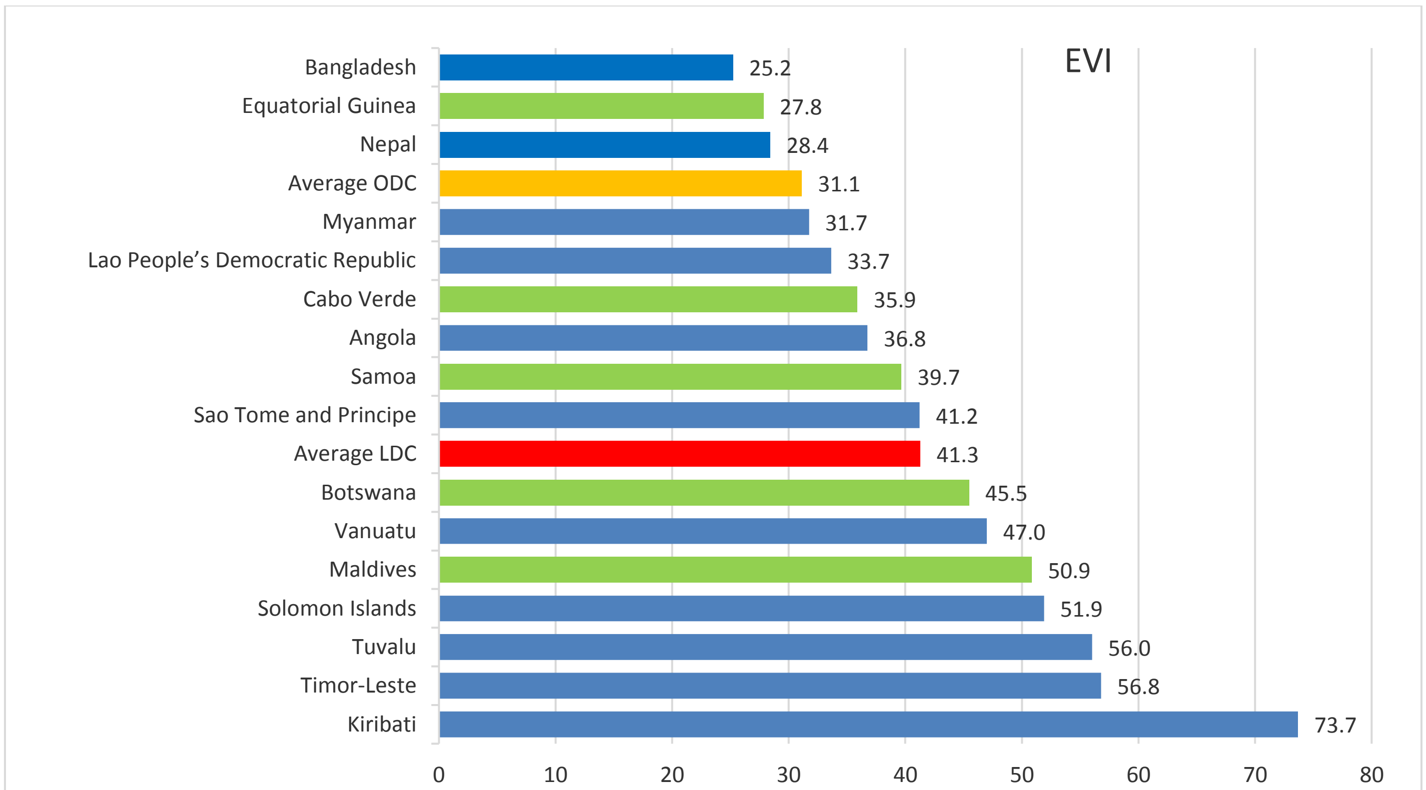
Figure 1. Graduated, graduating and eligible countries and the LDC criteria, 2018



Source: CDP

Country meeting graduation eligibility or graduating from LDC category
Graduated country





Thus, while belonging to the LDC category is a binary condition (a country is or is not LDC), the achievement of sustainable development is an evolving process. Graduation “[…] marks the end of a *political and*

administrative process, but not the completion of an *economic or developmental process*." (UNCTAD, LDC Report 2016, p. 39). Accordingly, reaching graduation only signals that some of the countries' most pressing structural constraints have been lessened, but the development process is far from over.

Table 3: Selected indicators of graduated countries, LDCs and low- and middle-income countries

	Botswana (1994)		LDCs		Low and middle income	
	Before	After	1989-1993	1995-1999	1989-1993	1995-1999
GDP growth (annual %)	6.4	6.3	0.8	4.9	2.2	2.4
Exports of goods and services (5 of GDP)	52.5	54.0	16.0	17.3	19.1	20.6
Gross fixed capital formation (5 od GDP)	30.3	26.2	14.8	..	24.8	25.7
Tax revenue	26.1	15.9	..	..	..	..
Net ODA received (% of GNI)	3.7	1.9	11.6	8.3	1.5	1.5
Foreign direct investment, net inflows (% of GDP)	-0.6	1.5	0.8	1.9	1.0	1.5
Personal remittances, received (% of GDP)	2.0	0.8	3.9	3.7	1.2	1.2
	Cabo Verde (2007)		LDCs		Low and middle income	
	Before	After	2002-2006	2008-2012	2002-2006	2008-2012
GDP growth (annual %)	6.9	2.4	6.9	5.6	6.6	5.4
Exports of goods and services (5 of GDP)	35.8	35.3	26.7	26.7	30.3	28.1
Gross fixed capital formation (5 od GDP)	..	41.6	20.2	22.4	26.9	30.3
Tax revenue	21.9	19.2	..	..	12.5	12.6
Net ODA received (% of GNI)	15.9	14.8	8.9	6.5	1.0	0.7
Foreign direct investment, net inflows (% of GDP)	6.9	7.8	2.9	2.9	2.8	3.0
Personal remittances, received (% of GDP)	13.1	8.8	4.8	4.1	1.8	1.5
	Maldives (2011)		LDCs		Low and middle income	
	Before	After	2006-2010	2011-2015	2006-2010	2011-2015
GDP growth (annual %)	8.7	5.1	7.2	4.9	6.5	4.6
Exports of goods and services (5 of GDP)	76.6	83.3	27.4	24.1	29.8	25.8
Gross fixed capital formation (5 od GDP)	..	..	21.7	24.0	29.4	30.2
Tax revenue	10.7	19.5	..	..	12.8	12.2
Net ODA received (% of GNI)	2.8	1.0	7.3	5.1	0.8	0.6
Foreign direct investment, net inflows (% of GDP)	6.8	9.2	2.7	3.2	3.3	2.5
Personal remittances, received (% of GDP)	0.2	0.1	4.3	4.3	1.7	1.5
	Samoa (2014)		LDCs		Low and middle income	
	Before	After	2009-2013	2015-2017	2009-2013	2015-2017
GDP growth (annual %)	0.0	3.8	5.3	4.2	5.3	4.3
Exports of goods and services (5 of GDP)	28.7	28.4	26.0	21.7	27.2	24.2
Gross fixed capital formation (5 od GDP)	..	..	22.9	23.8	30.6	29.4
Tax revenue	20.7	23.7	..	..	12.5	12.0
Net ODA received (% of GNI)	16.3	11.7	6.2	4.7	0.6	0.6
Foreign direct investment, net inflows (% of GDP)	1.2	1.8	2.8	3.8	2.8	2.2
Personal remittances, received (% of GDP)	21.4	17.3	4.1	4.1	1.5	1.6

Source: World Development Indicators Database

Graduated countries should maintain, if not accelerate, their efforts to improve upon graduation outcomes, advance their structural transformation and enhance their productive and institutional capacities. To offset the loss of preferential treatment, graduating countries, like any other developing country, will need to improve competitiveness and increase productivity in the affected sectors/industries by upgrading processes, adding value, improving skills, etc. This requires resources, both financial and technical. Concessional finance will remain accessible but perhaps costlier. Access to capital markets may not be an option available to all graduating countries (and in any case excessive dependence on foreign savings and unsustainable levels of indebtedness should also be avoided). Thus, countries could take graduation as an opportunity to improve upon the mobilization of domestic finance, which implies having not only an efficient tax system and introducing reforms to combat tax evasion and tax avoidance and further developing and strengthening the domestic financial system, but also reversing the informalization of the economy. FDI and other private flows may contribute to the continued transformation of the economy, and the importance of an enabling business climate and stable political conditions and a sound policy environment cannot be overemphasized. More important, however, is the type of association the country should aim to have with foreign investors. That association should contribute to generate durable forward and backward links with the domestic economy and avoid the creation of enclaves with shallow links.

In this regard, a smooth transition strategy can be understood as an element of the country's sustainable development plan; it indicates those policy interventions that may be necessary to be introduced in that overall policy due to changes in the cooperation framework resulting from the country's change of status. And in designing and implementing their transition strategy, graduating countries will need the continued support of their development partners, but this assistance needs to be adjusted and tailored to the countries' specific and evolving needs.

Currently, the framework of support for transition is not well structured despite two GA resolutions on the issue. While the resolutions indicate that successful transitions need to be based on smooth transitions elaborated "as a priority by each graduating country", there is very little guidance on how countries could proceed. Thus, after meeting eligibility to graduation, LDCs are uncertain about which actions to take and the extent of support they will receive. And this lack of clarity on how to move forward and what to expect makes it more difficult for countries to accept the recommendation to graduate.

Additional support is necessary to continue to strengthen institutional capacities as graduating countries will need to elaborate an effective transition strategy to adjust to their new status. Stronger institutional capacities will also be required to navigate their new development cooperation landscape, effectively compete for finance (particularly climate finance), expertise and market shares as well as for implementing international conventions and agreements (for example, TRIPs) and conducting development-effective negotiations with official and private partners (FDI, free trade agreements).

A better graduation support framework is necessary. Its main elements are already in place but need to be energized, reformed and complemented by additional measures. The new graduation support framework—to be discussed in the next sections—would require action by several actors: graduating countries, ECOSOC and GA, the United Nations development system, other multilateral organizations, bilateral official donors and the CDP. It encompasses action in three main areas: i) strengthening of the policy advice and better targeting of capacity building support for smooth transition policy design and implementation; ii) improved and more effective monitoring of the transition process; and, iii) additional support measures for graduating and graduated countries.

3. Strengthening policy advice and technical cooperation for smooth transition policy design and implementation

As seen above, an ex-ante impact assessment is prepared when a country meets eligibility for graduation for the first time. The assessment is expected to be prepared during the year preceding the following triennial review (second finding) to assist the CDP in its decision-making process. The impact assessment identifies the LDC-specific measures used by the country and the smooth transition provisions these measures carry, if available or known. It also identifies the country's main trading and development partners and the possible changes in partners' attitudes and policies vis-à-vis the country should it be recommended to graduate. As such, the impact assessment highlights issues that need to be addressed as the country moves forward. But the report is silent in terms of an initial policy advice on possible options to offset potential losses and to capitalize on potential gains from graduation.

Improved impact assessment for initial policy guidance and advice: The impact assessment was conceived as a decision-making tool for the CDP and should be kept as such, but at the country's request, it could be complemented by an Addendum, which would contain initial policy advice and guidance on the very first steps and possible actions graduating countries would need to consider based on the impact assessment findings. For example, the Addendum would:

i) include some initial suggestions on possible institutional arrangements that would be useful to oversee the transition process;

ii) indicate priority areas where attention will be needed to prepare the country for designing its transition strategy (for example, preferential market access, phasing out of GEF-LDCF, or increased FDI inflows);

iii) identify issues and/or provide guiding questions regarding areas where additional information needs to be collected and analysed to have a better understanding of the extent of the impact and to inform policy-making (for example, supposing the loss of preferential treatment is identified as one main area of concern, possible additional information needed includes: extent of the sector(s) reliance on preferential treatment; importance of the sector for the country's generation of foreign currency—which may affect the country's capacity to import and the servicing of its external obligations— employment and fiscal revenues; identification of domestic suppliers to the sector, etc.). *The Addendum will not collect or analyse this data*; it will simply indicate the areas and types of information that need to be made available for policy-making moving forward; and,

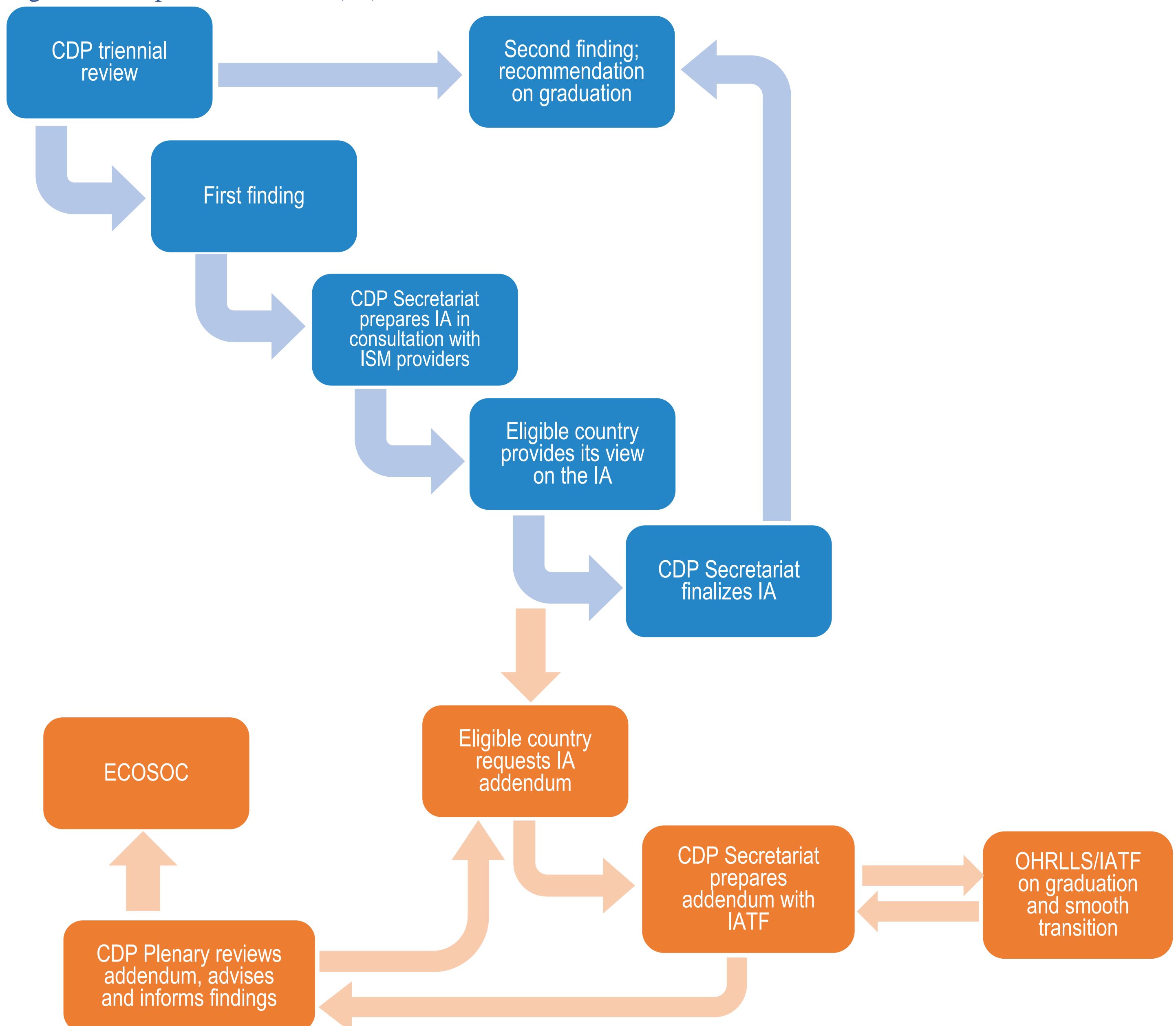
iv) propose possible *broad* policy *options* (emphasis on broad and on options) the country could contemplate to address such impacts (for example, explore alternative markets, negotiate extensions of preferential treatment, upgrade the affected sector productive capacity, industrial policy options for other sectors with potential for growth, apply to GSP+ or other preferential schemes, enter in free trade negotiations with main partners, etc.).

The Addendum would be prepared by the CDP Secretariat in collaboration with the members of the Inter-Agency Task Force on Graduation and Smooth Transition (IATF), which would also indicate which specific and target areas that their respective agencies could provide advisory services for the implementation of the transition strategy. As the organizer of the IATF, UN-OHRLLS would coordinate and consolidate these inputs and forward them to the CDP Secretariat. The involvement of the IATF would help activate the United Nations development system to consider imminent changes in the country status as well as the possible implications for the country's

development and the system's operations at the country level in a more effective way. This would also contribute to better coordination with and support from the United Nations agencies present in the country (see below).

The Addendum could then be reviewed and discussed at the plenary meeting of the CDP sometime preceding the next triennial review. The CDP will then provide the country with some initial thoughts about the road (or possible avenues) towards graduation and report to the ECOSOC on its main findings. To move forward with this suggestion, the impact assessments need to be prepared during the first year after the country meets graduation eligibility for the first time (instead of for the subsequent triennial review, three years later), to give eligible countries additional time to get ready for the second eligibility finding. The Addendum, in turn, would be prepared and made available for the second CDP plenary after the triennial review which indicated the country's first eligibility to graduation (see figure 2a).

Figure 2.a: Impact Assessment (IA) and its Addendum



It should be emphasized that the Addendum is NOT the country smooth transition strategy. That strategy should be initiated, led and prepared by the country itself. Equally important, no graduation recommendation has been made at that point by the CDP. Thus, the Addendum should be understood as a rough exploratory guide, an additional planning tool that could be made available at the country's request as it embraces graduation. It aims to support the country in getting better prepared to design its smooth transition strategy and approach its development partners by providing the country with a better understanding of issues at stake, identifying areas that will be potentially impacted by graduation, pointing to basic additional information that needs to be collected to establish priorities for policymaking, and outlining possible general policy alternatives.

To further improve the usefulness of these preliminary assessments as a policy tool and to enhance the country's capacity to plan for its transition, sometime during the first year after the GA takes note of the CDP recommendation, preferably at the start of the country's preparatory period, a panel discussion could be organized as a side event at one of the High-level segments of ECOSOC. The panel would review the country's path to graduation, possible actions moving forward and the role of development partners in providing support. The panel discussion could be composed of a country representative who would introduce the issues, a bilateral donor-designated representative, and a multilateral donor/partner representative (preferably someone linked to the country's UNADF (see below), a trading partner (if relevant), a representative of the private sector and/or civil society, and a CDP member. Basically, this is a discussion in a wider forum of the findings of the impact assessment and its Addendum plus the graduating country's initial thoughts about its transition plans. The panel discussion could be a useful exercise to keep momentum in the preparation of the smooth transition strategy, alert partners of changes ahead and gather additional support and inputs. The main findings of the panel discussion could be forwarded to the intergovernmental process overseeing the implementation of the IPoA [this suggestion requires consultation with UN-OHRLLS as per the operationalization of this suggestion. The idea is that any concern related to impacts of graduation could be expressed in a resolution and/or considered in the IPoA follow-up].

Formal and more effective United Nations Development Assistance Framework (UNDAF) engagement for smooth transition support: While the Addendum is indicative in nature, it can help graduating countries to bridge the gap between the CDP process and actions required at the country level. Accordingly, for the United Nations system to be better aligned in providing policy advice and capacity building to graduating countries, the findings and conclusions of the impact assessment and its addendum need to be fully reflected in the country's UNDAF, not as a separate exercise, but as part of the UNDAF exercise (see figure 2b).

The UNDAF is currently oriented towards the implementation of the 2030 Agenda at the country level. Thus, the mainstreaming of smooth transition into UNDAF would guarantee that the adjustment to graduation conditions would be compatible with and contribute to the achievement of broader sustainable development goals. Moreover, this mainstreaming could provide a better and easily identifiable anchor to the establishment of the consultative group (which may also involve entities beyond UNDAF: organizations that do not belong to the United Nations system such as WTO, certain IFIs, trading partners and bilateral official donors) as the country advances with the planning of its policy environment post-graduation.

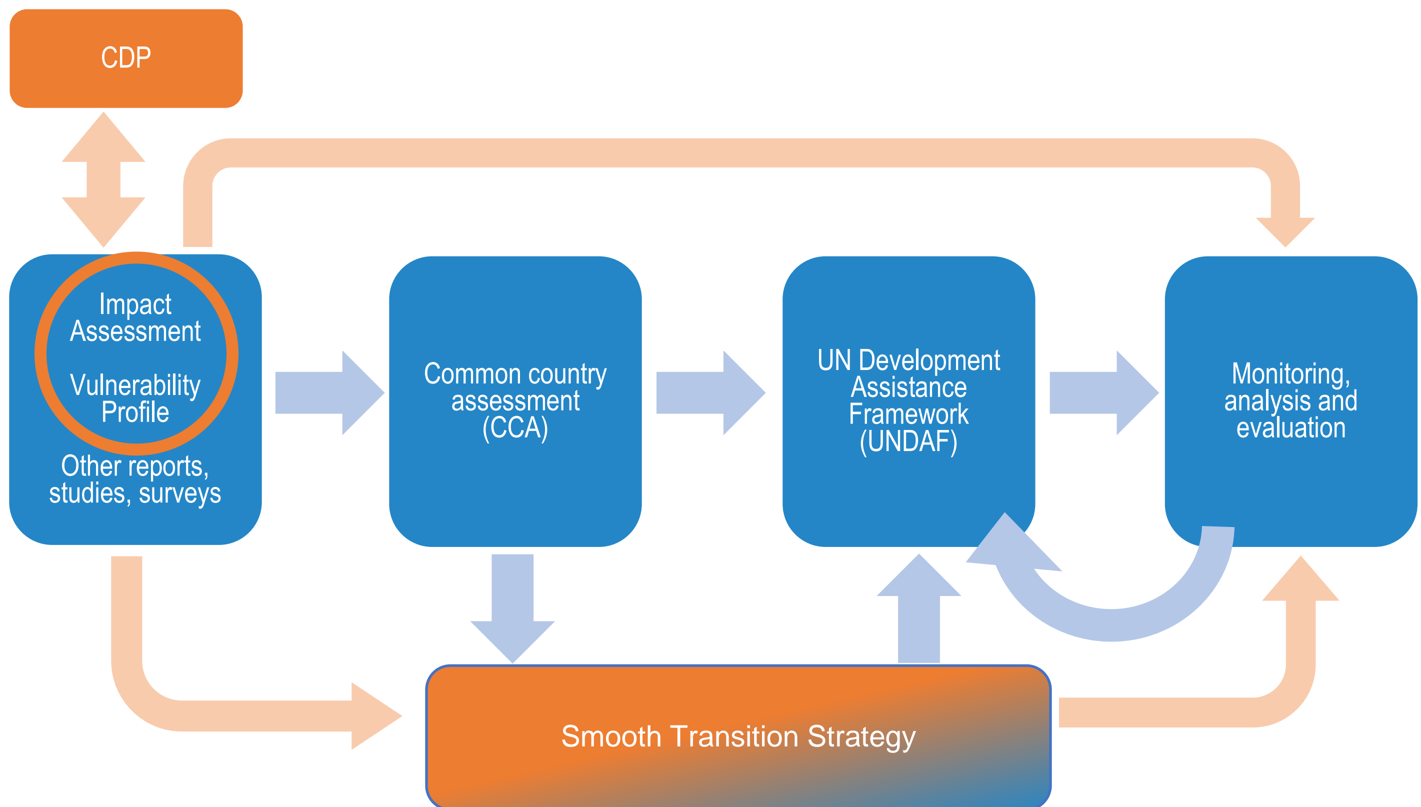
The UNDAF provides a system-wide overview of key United Nations activities at the country level in support of national priorities and policies. But it needs to be attuned to become more responsive to the graduation process thus providing graduating countries with the necessary advisory services and technical assistance to adjust their development strategy during the transition period and after graduation. Action in this direction would also contribute to improved coherence between the normative and operational arms of the United Nations.

Currently, these two processes—graduation and UNDAF—are not communicating well with one another. For example, the current UNDAF for Angola (2015–2019) has only one activity related to graduation (the conduction of a study) but no follow up is mentioned. There is no reference to graduation in Equatorial Guinea's UNDAF for the period 2013–2017 (the country's graduation was endorsed by the ECOSOC in 2009, see Annex table A1). For countries approaching graduation, Bhutan's (2014–2018) and Bangladesh's (2017–2020), the word LDC is not even mentioned in their respective UNDAF reports. Communication channels need to be strengthened among main actors involved. As a suggestion, the CDP Secretariat should send a communication to the entities of the United Nations System present in the field, as identified by the United Nations Development Group (www.undg.org), on the outcome of its triennial review, thus directly alerting them on eventual future changes to the country status as LDC. Moreover, the country itself must have a much more active role towards that end by flagging to its development partners the anticipated changes to its status or to the conditions it faces.

Preparing the impact assessment and the vulnerability profile in the first year after the first finding should give enough time to coordinate the UNDAF cycle with the graduation cycle. Ideally, the findings of the impact assessment and vulnerability profile should also feed into the preparation of the Common Country Assessment (CCA). The CCA aims to identify immediate underlying national structural development challenges and informs the design of United Nations policies and programmes at the country level. It also identifies key risks that that could impact the development trajectory of the country, including economic and financial shocks. In its guidelines, the United Nations Development Group states that "[t]he CCA provides an opportunity for United Nations agencies to come together with key national and international stakeholders to discuss national development challenges and common approaches in the beginning of the UNDAF cycle. It thus holds the potential for ensuring that support provided by United Nations agencies as a whole in a country is coherent and complementary, drawing from each agency's expertise, resources and mandate."(UNDG, 2017, p. 3) In this regard, the UNDAF seems to be the most feasible and suitable locus for a graduating country to request guidance on how to prioritize actions in preparation for graduation and to identify available support to carry those priority actions.

In case graduation eligibility occurs after the CCA is finalized and an UNDAF cycle is launched, UNDAF has a monitoring component (implementation monitoring reports) which provides an opportunity to revise or adjust existing programmes (see figure 2). Thus, United Nations agencies already working in the country can properly consider the graduation impact on their programmes and activities at the local level. Having the participation of IATF in the preparation of the Addendum can contribute to this end as well, as most IATF members are also present in the UNDAF system.

Figure 2b: Mainstreaming LDC graduation and smooth transition strategy into the United Nations Development Assistance Framework



Designation of supporting advisors for negotiations with trading partners and official donors: An additional measure of support could be the designation, again at the country's request, of supporting negotiators from a specialized United Nations agency. The supporting negotiators would assist the graduating country in preparing for its discussions with its main bilateral and trading partners and attend these meetings. The idea is based on UNCTAD's role in external debt negotiations with the Paris Club of creditor countries, where the Organization has helped debtors to present their case to creditors.[3] In the case of graduating countries and, depending on specific country's needs and specificities as indicated by the impact assessment, the Addendum and subsequent work by the country and UNDAF, supporting advisors or advocates could be designated, for example, in the areas of trade and development finance. This measure would strengthen country's capacity to better articulate their smooth transition goals and secure the necessary inputs from key partners not participating in UNDAF.

4. Towards a more effective monitoring of the transition process

The current reporting cycle on graduating and graduated countries is a long one. First, graduating countries are invited to submit reports on the preparation of their smooth transition strategy and are to be monitored yearly by the CDP during the transition period before graduation. Based on the experience thus far, this implies between

[3] Additional information on UNCTAD's original mandate available from: http://unctad.org/divs/gds/dmfas/who/Pages/DMFAS-History.aspx

three to six annual monitoring reports. The monitoring report aims to assess any sign of deterioration in the development progress of the countries concerned and to review the country's progress report on the preparation of its smooth transition, if such information is made available to the Committee. Then, after graduation, the CDP will continue to monitor countries, annually during the first three years after graduation and triennially after that for two triennial reviews. This implies five additional reports. Graduated countries are currently invited to provide the CDP with concise reports on the implementation of their smooth transition strategy (UN CDP, 2015).

The usefulness of this exercise is unclear. First, country participation is far from optimal. Among the five countries monitored in 2018, only Samoa provided detailed information on its transition from LDC status. Second, the timing of some of these reports are ill conceived. In some instances, the reports are due right after the decision of the GA on graduation to provide sufficient time for country action or to generate new relevant information and data to be collected, analysed and reported to the CDP. Third, findings of the monitoring get buried in the CDP report and are not sufficiently acknowledged or discussed at the relevant intergovernmental processes. Greater visibility and impact are needed to provide the country with additional insights and policy options as well as to alert the international development partnership of the specific issues confronted by graduating and graduated countries. Fourth, there are numerous other reports prepared by international organizations that already conduct a thorough examination of recent trends in these economies and their prospects (some of them with dedicated individual country analysis) on a regular basis providing a wealth of information on these countries.[4] Finally, the growing number of countries reaching graduation and graduating also points to the need to rationalize the monitoring process due to capacity limits at the CDP and its secretariat. The following is suggested:

Midpoint monitoring review: Midpoint in the transition period (between the GA decision and the anticipated date of graduation), there should be one monitoring report on the stage of preparation of the transition strategy. The monitoring report is to be prepared by the country. It could include a concise summary of actions leading to the mainstreaming of the transition strategy process into UNDAF, the setting up and composition of the country's consultative mechanisms, identification of special negotiators or advocates if applicable, prioritization of areas and actions to be taken, challenges that require further consideration and further assistance, main risks to the implementation of the strategy, the role of bilateral and private donors as well as multilateral donors not participating in UNDAF. The report is to be submitted to the CDP. A parallel event to the CDP plenary with the participation of CDP members, a country representative and IATF members would be organized to discuss the report and provide feedback, further engaging the UN system in supporting the country. The recommendations from the parallel event are to be reverted to the country and the members of the consultative mechanism. Recommendations by the CDP are to be forwarded to ECOSOC as part of the CDP annual report to the Council and to other relevant intergovernmental processes.

Presentation of the Smooth Transition Strategy: In the year of graduation, the country would make a presentation on the main contours of its transition strategy prepared with the assistance of UNDAF and other partners of the consultative mechanism. Preferably, this exercise should be combined with the National Voluntary Review Process of the Agenda 2030, thus linking smooth transition from the LDC category with the implementation of the 2030 Agenda.

[4] To name a few: UNCTAD's *The Least Developed Country Report*, UN-OHRLLS's *State of Least Developed Countries*, ECA's *Economic Report on Africa*, ESCAP's *Asia-Pacific Countries with Special Needs Report*, ECLAC's *Balance Preliminar para las Economias de America Latina y el Caribe*, African Development Bank's *African Economic Outlook*, Asian Development Bank's *Asian Development Outlook*, IMF's *Regional Outlook* (Asia and the Pacific, Sub-Saharan Africa); and the World Bank's *Global Economic Prospects* (regional outlooks).

Implementation monitoring reviews: Subsequently, the first monitoring review could take place two years after graduation. It would highlight the country's experience during the first years of smooth transition including its main accomplishments and challenges. It could also indicate areas where additional attention may be needed, either to address unforeseeable issues and/or to further facilitate implementation. The first monitoring review would be followed by a second and last implementation review three years later. This review would be prepared by the country and forwarded for consideration, analysis and feedback by the CDP. Recommendations of the CDP are to be forwarded to the country and its consultative mechanism. Findings would also be recorded in the CDP report and forwarded to ECOSOC and to the GA process overseeing the implementation of the IPoA. Thus, any concern related to impacts of graduation could be expressed in a resolution and/or considered in the IPoA follow-up. The idea is that any concern (and necessary policy actions) related to impacts of graduation could be expressed in a resolution and/or considered in the IPoA follow-up.

Triennial Review monitoring: The CDP would continue to monitor the LDC-indicators of graduated countries at its triennial reviews, highlighting their performance in a dedicated table (see figure 3).

To sum up, *at the country level*, besides the country's own national monitoring mechanisms, the implementation of the smooth transition strategy would also be monitored by the UNDAF as it is mainstreamed and becomes an integral part of it and/or is reflected in that framework (see again figure 2). *At the international level*, monitoring and follow-up would take place at the relevant intergovernmental meetings as suggested above. In any case, it would be important to undertake consultations with LDC representatives to assess their interest and ideas on how this process can be more effective and useful for the implementation of the smooth transition strategy. Similarly, consultations with the secretariats of the relevant intergovernmental processes will also be necessary to ascertain the feasibility of these suggestions. But fewer and more meaningful monitoring reviews are a necessary component of the new package of support for graduation.

Figure 3: Graduation and monitoring reviews

5. Additional smooth transition measures: capitalizing on graduation

As seen in section II, LDC-specific ODA modalities, preferential market treatment, and access to LDC-specific climate funds are the most relevant forms of LDC-specific support, on average. Other important forms of support are technical cooperation (no reason to anticipate change in access), and policy space at WTO (although not all LDCs have the same policy space there, as recently acceded countries often have less policy space than original members). This section will explore and propose new measures that could not only offset some of the potential negative impact the phasing out this support but also contribute to the country's achievement of its long-term sustainable development goals.

Table 4 provides information on the relative importance of specific financial flows to LDCs over the period 1999–2016. The composition of such flows has been changing over the recent years. Overall, the relative importance of net ODA flows (grants, in particular) has declined while FDI and loans (both concessional and non-concessional) increased. While the share of FDI and portfolio net flows almost doubled during the period, these flows are highly concentrated in a few countries, most of them exporters of natural resources. In fact, the ten largest recipients absorbed four-fifths of FDI flows during the period 2011–2013 (Mallapali and Sauvant, 2015).

Table 4. Net flows of financial resources to LDCs, 1999–2016 (period average), US$ millions.

LDCs, period averages	1999-2001	% share	2014-2016	% share
Total Grants	13,409.0	54.6	40,887.7	34.4
Technical cooperation grants	2,650.3	10.8	4,273.3	3.6
ODA grants	10,758.6	43.8	36,614.3	30.8
Total loans (net flows)	2,191.2	8.9	20,478.6	17.2
Concessional loans	2,367.5	9.6	15,710.7	13.2
Non concessional loans	-176.3	-0.7	4,767.9	4.0
Remittances	6,101.0	24.8	31,613.0	26.6
FDI + portfolio (net flows)	2,870.4	11.7	25,868.8	21.8
Total above	24,571.6	100.0	118,848.0	100.0
Memo items:				
Inflows (% of GNI)	13.2		13.1	
ODA (net Million USD)	12,919.5		43,349.9	

Source: OECD Statistics, GeoBook: Graphical flows to developing countries; World Bank International Debt Statistics Database and Remittances outflows and inflows (April 2018).

LDC access to international capital markets has somewhat improved lately particularly since debt burdens have been reduced in several countries with the completion of Heavily Indebted Poor Country and Multilateral Debt

Relief Initiatives (see again table 1). Some LDCs had successful bond issuance in these markets (Angola, Ethiopia, Lao PDR, Mozambique, Rwanda, Senegal, United Republic of Tanzania, and Zambia). Yet, at the time of writing, sovereign credit ratings—which are necessary for international bond issuance—are available for only 14 LDCs (ten by Standard & Poor's and additional four by Moody's) while only nine LDCs are assessed by the IMF at a low risk of debt distress (see table 5). Issuers of financial securities often engage the services of a credit rating agency to assign a rating to the security to be placed in the market. Ratings reflect the perceived willingness and ability of sovereign issuers to service their financial obligations to nonofficial creditors on time and in full. That ability is often conditioned by the institutional, economic, external, fiscal and monetary features of the country (S&P 2017). And the lower the credit rating, the higher the compensation the issuer will have to pay to attract investors. This once again stresses the importance of prudential macro management of the economy and the quality of its institutions as well as the limits of increased external indebtedness as a sustainable tool of finance.

Table 5: LDCs: risk of debt stress, credit ratings and fragility

Country	Fragile state	Risk of debt (IMF assessment 2017)	S&P credit rating (May 2018)
Afghanistan	Y	high	-
Benin	N	low	-
Burkina Faso	N	moderate	B
Burundi	Y	high	-
Cambodia	N	low	B2*
Central African Republic	Y	high	-
Chad	Y	high	-
Comoros	Y	moderate	-
Dem. Rep. of the Congo	Y	moderate	CCC+
Djibouti	Y	high	-
Eritrea	Y	in distress	-
Ethiopia	N	moderate	B
Gambia	Y	moderate	-
Guinea	N	moderate	-
Guinea-Bissau	Y	moderate	-
Haiti	Y	high	-
Lesotho	N	moderate	-
Liberia	Y	moderate	-
Madagascar	N	moderate	-
Malawi	N	moderate	-
Mali	Y	moderate	-
Mauritania	N	high	-
Mozambique	Y	moderate	Caa3*
Niger	N	moderate	-
Rwanda	N	low	B
Senegal	N	low	B+
Sierra Leone	Y	moderate	-
Somalia	Y	…	-
South Sudan	Y	moderate	-
Sudan	Y	in distress	-
Togo	Y	moderate	-
Uganda	N	low	B
U. R. of Tanzania	N	low	B1*
Yemen	Y	high	-
Zambia	N	moderate	B
Countries meeting graduation eligibility			
Bangladesh	N	low	BB-
Lao PDR	N	high	-
Myanmar	Y	low	-
Nepal	N	low	-
Timor-Leste	Y	moderate	-
Countries recommended for graduation			
Bhutan	N	moderate	-
Kiribati	Y	high	-
Sao Tome and Principe	N	high	-
Solomon Islands	Y	moderate	B3*
Tuvalu	Y	high	-
Countries in transition to graduation			
Angola	N	n.a.	B-
Vanuatu	N	moderate	-
Graduated countries			
Botswana	N	n.a.	A-
Cabo Verde	N	high	B
Equatorial Guinea	N	n.a.	-
Maldives	N	high	B2*
Samoa	N	moderate	-

Source: IMF 2017 op. cit., World Bank Harmonized list of Fragile States for fiscal year 2019 and Standard and Poor: Sovereign Rating History, June 2016 and Trading Economics available at https://tradingeconomics.com/country-list/rating
* Moody's

In all, notwithstanding the increasing importance of private and commercial inflows for development finance in LDCs, ODA will remain vital for these countries as they leave the category. As discussed earlier, graduated countries will not be cut from concessional ODA, but the amount of grants and the level of concessionality may decrease, depending on the donor. In the case of the World Bank, access to and graduation from its concessional window, the International Development Association (IDA), depends upon the country's income level and financial ability to borrow from the International Bank of Reconstruction and Development (IBRD), its non-concessional window. Countries often receive blend terms—access to both IDA and IBRD resources—before losing access to IDA and gaining full IRBD access.

To be classified as blend, the country needs to satisfy the creditworthiness criteria, which is based on eight components (political risk, external debt and liquidity, fiscal policy and public debt burden, balance of payment risks, economic structure and growth prospects, monetary and exchange rate policy, financial sector risks, and corporate sector debt). Assessment of creditworthiness by the Bank may differ from market perceptions as the Bank does not charge an individual risk premium and its loans have much longer maturity than commercial loans (World Bank-IDA, 2016). During fiscal year 2019 all LDCs, except Angola (IBRD since fiscal year 2014) and Timor-Leste (blend terms), received IDA terms. Among graduated LDCs, Botswana and Equatorial Guinea are under IBRD terms, while Cabo Verde receives blend terms. Maldives and Samoa receive IDA terms under the small island exception rule (see table 1).[5]

Access to and graduation from concessional funds available in other multilateral financial institutions are often guided by IDA terms. Graduation from the IMF's concessional window, the Poverty Reduction and Growth Trust (PRGT), depends upon the level of the country's GNI per capita or whether countries have the "capacity to access international markets on a durable and substantial basis, provided that they do not face serious short-term vulnerabilities access" (IMF 2017, p.5). As in the case of IDA, Angola is currently the only LDC without access to the PRGT. At the most recent eligibility review (2015) Bhutan, Lao PDR, and Zambia were eligible to graduate from the PRGT under the market access criterion but were not recommended due to high risk of debt distress and/or were confronting serious short-term vulnerabilities (IMF, 2017).

Turning to official bilateral donors, countries graduate from OECD-DAC eligibility only after they have exceeded the World Bank's high-income threshold for three consecutive years at the time of the triennial DAC review. Thus, access to ODA funds is not contingent on LDC status either. However, flows from bilateral donors may become more expensive, pending donors' attitude towards graduating countries as discussed in section II. For example, Japan and Germany are among the major bilateral donors that offer concessional loans. In the case of Germany, the Federal Ministry for Economic Cooperation and Development (BMZ) offers funds to LDCs in the form of grants, while IDA-only countries are offered loans at the same terms of IDA's: 0.75 per cent interest rate over a 40-year period, including 10-year grace period. Other countries are offered loans at 2 per cent interest rate over a 30-year period and 10-year grace period. In the case of Japan, effective October 2017, the terms applied for low-income LDCs (GNI per capita lower than US$1,005 in 2017) are: 0.01% interest rate and 40-year repayment period including 10-year grace period, irrespective of sectors and fields. A three-year transition period will be granted to recipient countries that move from the category of low-income LDCs, and, during the period, the terms and conditions for low-income LDCs will be applied to the projects of these countries. Several options (floating or fixed interest rates, varying repayment and grace periods) exist for lower-middle-income countries (LMICs) depending on the type of the project. Less expensive options under fixed rate terms range from 0.1 to 0.25%.[6] Policies followed by other donors that are not members of the OECD-DAC, including

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[5] Population smaller than 1.5 million, significant vulnerability due to size and geography and very limited creditworthiness.

[6] Information obtained from the BMZ and JICA websites, accessed on 8 August 2018 and 1 August 2018, respectively.

providers from the South, do not follow a standard pattern as far as their financial cooperation with LDCs is concerned. It is not clear how much the change of status by recipient countries will influence the terms of such cooperation.

Looking at the—admittedly not long-- experience of graduated countries, one notices that the share of ODA loans by the members of OECD-DAC tended to increase, at least initially, following graduation. This is particularly true in the case of Cabo Verde, but subsequently it declined (see annex figure A1). At the same time, the three graduates (except for the Maldives in 2015–2016) continued to receive loans with greater concessionality (measured by the grant element) than the average of LDCs and LMICs (see again annex figure A1). Thus, although the recent experience indicates an increase in the share of loans in ODA flows by OECD-DAC members, that increase is not necessarily permanent. Moreover, the degree of loan concessionality does not seem to change much after graduation.

Effective use of LDC indicators in ODA allocation: One way to avoid declines in ODA flows, and direct flows where needed the most, is to incorporate indicators of the LDC criteria, particularly those of EVI in their allocation criteria of ODA. This measure has already been recommended by the GA (resolution 67/221), but there is little evidence that it has been implemented. In the same vein, multilateral and bilateral donors could adopt an index of physical vulnerability to climate change to guide allocation decisions of concessional finance for adaptation.[7] LDCs are among the most climate vulnerable countries and would lose access to dedicated funds for climate adaptation sometime after graduation (see below). *The incorporation of measures of physical vulnerability to climate change for the allocation of climate finance* would keep vulnerable graduated LDCs among priority countries. This measure further addresses LDCs' concerns and de facto support graduated countries in their adaptation efforts without excluding other vulnerable countries in need.

While complying with the GA recommendation on the incorporation of the LDC criteria for the purposes of ODA allocation could contribute to maintain levels of ODA to graduated countries, it does not address possible changes in the terms these flows are to be extended. There are no directives or guidelines on the share of grants in ODA flows to LMICs beyond the minimum amount of grant equivalent a flow must have for that flow to qualify as ODA. To qualify as ODA, loans to LMICs must have a grant equivalent of at least 15 per cent. The corresponding figure for LDCs is 45 per cent (UNCDP, 2015). Thus, loans to LMICs can be classified as ODA at a much lower level of concessionality when compared to loans extended to LDCs. Additionally, as seen above, some donors have slightly more stringent terms on loans to LMIC when compared to loans LDCs (higher interest rates, shorter maturity and grace periods).

A moratorium to upgrading to LMIC ODA modalities: While it is not clear how donors will proceed, loans have a greater share in total ODA extended to LMICs than to LDCs (23 per cent for LMIC compared to 17 per cent for LDCs of net ODA flows in 2016). Additionally, lending terms to LMICs are often less generous than those extended to LDCs. Thus, one could make the case for a moratorium of the application of observed ODA modalities for LMICs (greater share of loans, higher costs) for graduating countries. The moratorium would provide graduated countries with a (financial) breathing space to tackle the adjustments required by graduation. The moratorium should last while the country receives IDA terms only. The ODA terms could then be modified as the country is graduated to blend terms by the World Bank. The moratorium provision would also enhance coherence in the international development finance architecture by better aligning the Bank and the OECD-DAC processes.

[7] See for instance proposal by P. Guillaumont, Measuring vulnerability to climate change to allocate funds for adaptation, FERDI Documents de Travail, No 136, 2015.

Cost differential targeted for enhancing capacity to use blended finance: Should donors decide to no longer apply LDC guidelines to graduated countries, the cost differential—the difference between the LMIC terms being paid by the graduated country and what the donor would be receiving should the country still be treated as LDC—could be channelled to a fund to be reverted as grants to the country to enhance its capacity to access blended finance arrangements in the future. The resources generated will reflect the difference in levels of concessionality and may not be significant but sufficient for the enhancement of local capacities to better understand, negotiate and structure new types financing arrangements, to strengthen the local investment promotion agencies, to prepare initial studies and project proposals, identify projects to be financed by private investors to achieve sustainable development goals, etc.

For example, let's assume for illustration purposes only, that a $1,000 concessional loan would carry a $600 grant element if extended to an LDC but only $300 if extended to a graduated LDC that is now classified as LMIC for ODA calculation purposes but still is limited to IDA and PRGF funds. The graduated country would service the loan at the LMIC terms, but the difference in concessionality ($600-$300 = $300) would go to a fund as a grant to finance activities and programmes in graduated countries.

While there has been a great deal of enthusiasm for blended finance, one should proceed with caution so that grants and highly concessional resources aiming at development outcomes do not end up as subsidies for activities of the private sector that would take place in any case and/or end up generating perverse distributive effects and limited social returns (Alonso, 2018). Information asymmetries between national authorities and international investors can lead to biased results in favour of the latter. Thus, "conditions need to be put in place to support LDCs to negotiate appropriate deals, and continuously invest in capacity to enable them to negotiate, monitor and expand these arrangements." (Agence Française de Développement, 2016, p.37). Reverting funds generated from the servicing of less concessional loans back to graduated countries would contribute to that end to some extent and constitute a new measure of support for these countries. Currently, the United Nations Capital Development Fund (UNCDF) is investigating how suitable blended finance is for LDCs and how to address the challenges these countries face in tapping these resources. This research should provide solid guidance on how to develop this proposal further.[8]

Advisory services for promoting FDI and negotiating with the foreign investor: FDI inflows to LDCs have increased lately. Despite its concentration in extractive industries recent trends indicate foreign investor's interest in other sectors for investment in LDCs such as manufacturing (not only garments due to the abundance of relatively cheap labour, but also food, beverages and tobacco in the larger LDCs) and services (transportation, electricity, financial services, tourism). In general, countries' attractiveness as locations for FDI, depends not only on the availability of natural resources, the cost and skills of the labour force and market size but also on "the institutional and policy framework governing FDI, the overall climate for business or economic activities and the effectiveness with which such investment is promoted." (Mallampally and Sauvant 2015, p. 4).

As the association with the foreign investor will likely play a greater role in the attainment of sustainable development goals of the country moving forward, additional advisory services may be needed to strengthen local capacities to develop the appropriate framework to attract FDI and to ensure that association will generate the desired benefits for the country. In this regard, graduating countries could consider requesting the conduction

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[8] On April 13, 2018 the UNCDF organized an expert group meeting on blended finance in the least developed countries. One of the objectives of the EGM was to generate knowledge products to "a) contribute to the policy debate on blended finance by developing empirical evidence and original research on how blended finance is being and can be used in LDCs, and b) create a community of practice that can help shape the actions of governments, investors and practitioners with regard to applying blended finance in LDCs." (http://www.uncdf.org/expert-meeting-on-blended-finance-in-the-least-developed-countries)

(or an update, if applicable) of an Investment Policy Review (IPR) by UNCTAD, one of the United Nations entities with considerable expertise in this area. The IPRs provide an evaluation of the country's legal, regulatory and institutional framework to increase FDI inflows and how to maximize the benefits from it. The review produces action-oriented recommendations which often form the base for subsequent technical assistance and capacity building provided by UNCTAD.[9] Graduating countries should have access to these advisory services on a priority basis. Currently, among graduating countries and countries meeting eligibility for graduation, only Bangladesh and Nepal have conducted IPRs (in 2013 and 2003, respectively).

Equally important is support and capacity building for the negotiation, implementation and monitoring of investment contracts with the foreign investor. Several initiatives are available, most of them related to the extractive and energy industries.[10] A new addition to this support framework is the Investment Support Programme for Least Developed Countries (ISP/LDCs), a partnership initiative by UN-OHRLLS and the International Development Law Organisation (IDLO). Launched in 2017, ISP/LDCs is intended to provide legal and technical advice and assistance to requesting LDCs on investment-related negotiations and dispute settlement. The Programme will also arrange complementary training and capacity building activities on demand. Graduated countries will access the programme for at least 5 years after graduation. As it will be proposed further below, an exit training/capacity building component should be added and offered to graduating countries benefiting from the programme to facilitate their transition into other sources of support available in this area.

Graduated country investment guarantee facility: depending on the country situation, FDI flows could be encouraged if guarantees covering for political risks (currency inconvertibility and transfer restriction, war terrorisms, civil disturbances, expropriation, etc.) are more readily available. Among others, the Multilateral Investment Guaranty Agency (MIGA) of the World Bank offers political risk insurance for member countries for investment projects that comply with a comprehensive set of environmental, developmental and social standards. During the period 2010–2016, MIGA offered political risk insurance for 41 projects in LDCs at an average exposure of $46 million per project (UN-OHRLLS 2017, table 2.4, p.44). A special fund to be financed by voluntary contributions could be established within MIGA to provide political risk guarantees for FDI projects in graduated countries in a dedicated fashion. Having to qualify to MIGA's standards and approval would ensure the developmental orientation of the projects. This special measure of support could potentially unlock valuable additional resources for graduating and graduated countries.

Capacity building to access climate funds: While funds currently available for climate change adaptation are clearly insufficient, the loss of both access to the GEF-LDCF and priority professed in favour of the category to access other funds is a major concern among graduation-eligible LDCs.[11] The Least Developed Country Expert Group (LEG) of the UNFCCC, in collaboration with the Green Climate Fund (GCF) secretariat, already provides

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[9] According to information available from UNCTAD's website, "out of 32 countries for which the IPR was published more than three years ago, 29 have experienced an increase in FDI inflows in the following years. And for 19 of them, such increases have been dramatic, with FDI inflows having more than doubled.".

[10] For a compilation of such initiatives see www.NegotiationSupport.org and Matrix of Major Negotiation Support Initiatives, prepared by Vale Columbia Centre on Sustainable International Investment (VCC) and HUMBOLDT-VIADRINA School of Governance (HVSG) available from http://ccsi.columbia.edu/files/2013/11/VCC-Compilation-of-NSIs-April-2014.pdf.

[11] As of 30 May 2018, the Fund had approved around US$1.2 billion for adaptation projects and programmes in 51 countries and leveraged another $5 billion in co-funding from partners. The LDCF's operational guidelines include a cumulative maximum amount that each LDC can access from the LDCF. Up to June 2018 the ceiling stood at $40 million, raised from $30 million in June 2016. As of April 2018, eight of the 47 LDCs have reached or nearly reached the current funding ceiling, including approved and pipelined projects. Additional 16 countries have accessed $30 million or more in LDCF funding. For GEF-7 (2018–2022), the resource allocation ceiling will be raised to $50million, with a cap of $10 million per country (GEF 2018, p. 41).

technical guidance on accessing funding from the GCF for the process to formulate and implement national adaptation plans (UNFCCC-BIS, 2018). Graduated countries may not have access to this support once they leave the category. Moreover, several other initiatives are available and dispersed throughout the climate change finance and assistance framework making support fragmented and difficult to locate and access. Therefore, LEG could devise an exit training component/programme to provide graduating countries with information on available resources and actions necessary to tap these initiatives including how to get assistance to prepare project proposals, understand requirements, strengthen local capacities, etc. This is particularly important for graduating SIDS with low lying coastal areas and other LDCs situated in regions prone to adverse climatic phenomena. In fact, three out of the seven graduating and graduated countries had the effective date of their graduation postponed due to the occurrence of natural disasters (Maldives, Samoa and Vanuatu).

Exit programmes from LDC-specific capacity building initiatives: Like the proposal above, the development and supply of country-specific graduation workshops and/or exit training exercises/programmes for the capacity-building initiatives that are LDC-specific should be an integral part of the new framework for graduation support. This will enable graduating countries to have a better understanding of the relevant issues and be empowered with the tools to effectively access support available to them as non-LDCs. In some cases, the exit programme by LDC-specific initiative could focus on issues the graduating country would need to address due to the change of status from LDC to non-LDC, where applicable. For example, the Enhanced Integrated Framework (EiF), in collaboration with the WTO and UNCTAD, could take the leadership in coordinating country-specific capacity building programmes, at the graduating countries' request, on how to approach the implementation of WTO disciplines they were exempted from as LDCs. Additionally, the United Nations Institute for Training and Research (UNITAR) offers training activities in the field of public finance, trade and intellectual property, upon request by partner institutions and donors, and could contribute to this end as well.

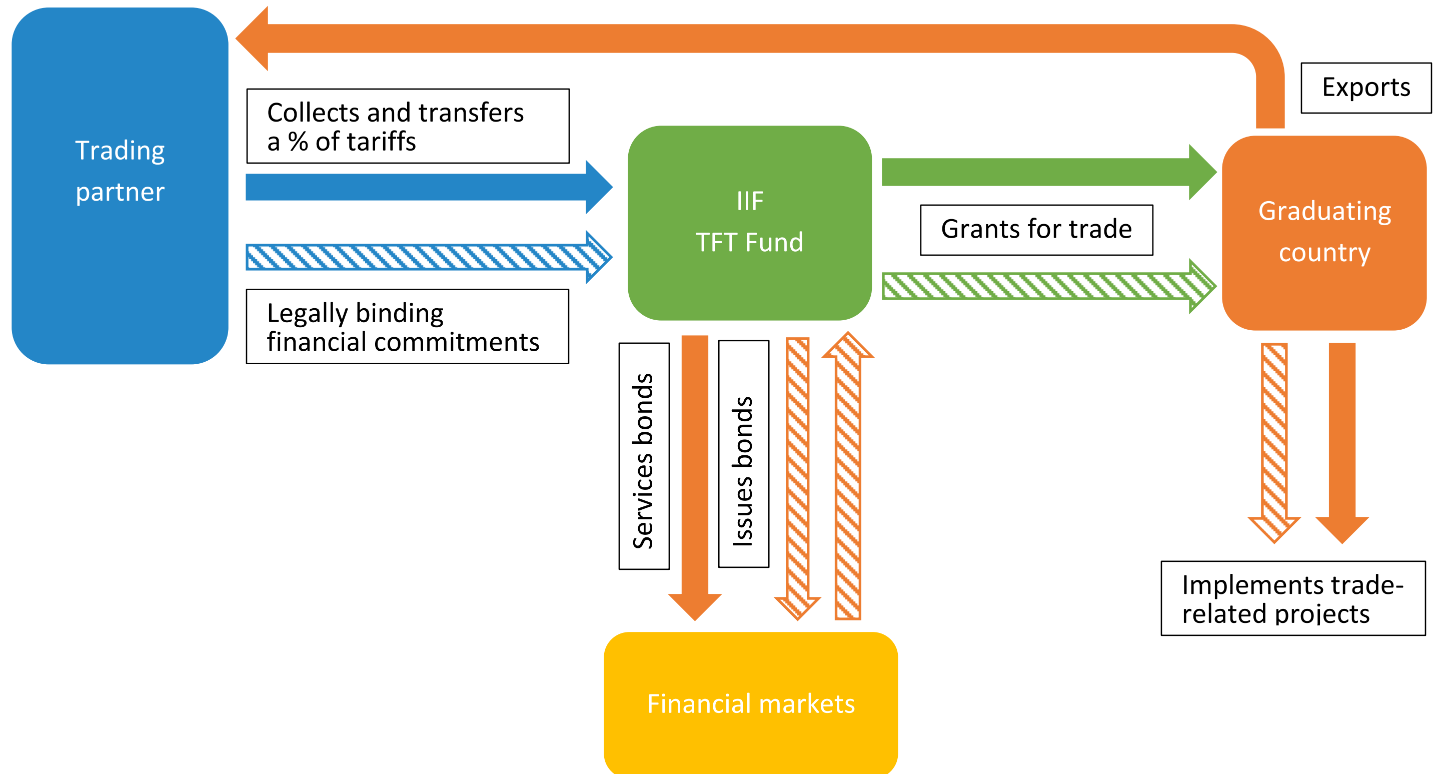
Tariffs for development initiative: While preferential treatment can be extended beyond graduation in some DFQF schemes (for example, the Everything but Arms Initiative of the European Union), the eventual loss of preferential access may have a potential negative impact for producers in graduating countries (loss of market share and export revenues) as well as consumers in importing countries (higher prices).[12] Upgrading of trade productive capacities for increased productivity will be needed. These activities could be financed in part with tariff revenues (or a dedicated share of such revenues) that will be eventually collected on the graduated countries' exports. A given amount of such revenues could be forwarded to a dedicated fund and used to finance projects to improve graduated country's competitiveness and/or other trade-related activities needed in the country to offset the negative impact of the loss of preferences. Timing may be a problem here, as tariff revenues will be generated only sometime after graduation while interventions aiming at increases in productivity would be needed before graduation to avoid disruptions.

Bridging financing would be necessary to front load resources. The proposal is similar to and inspired by the International Financial Facility for Immunisation (IFFIm, details available at www.iffim.org). An international financial institution (such as the World Bank) or a regional development bank (African Development Bank or Asian Development Bank) would take long-term legally binding financial commitments from donors (graduated country's trading partners that were granting LDC preferential market access). These financial commitments will be based on and backed up by a certain percentage of tariff revenues trading partners expect to collect from graduated countries. The financial institution will use donors' guarantees as collateral against which they issue

[12] Currently, the European Union is the main importer of LDC products. In 2009, LDC preferential imports by the EU reached €6.2 billion, corresponding to about €730 million in foregone tariffs. EU preferential imports under EBA reached €23.5 billion in 2016 (WTO 2017, EC 2018, EC 2011).

bonds (tariff-for-trade bonds) in international financial markets. Bonds could be designed in such a way that their servicing (payment of interests) would start after tariffs start to be collected on graduated countries. The proceeds of TFT bonds would go to a dedicated fund (the Tariff-for-Trade Fund, TFTF) to be managed by the IFI. Funds would then be released as grants to front load spending in trade-related projects and programmes in graduating countries. Once tariffs are applied to graduated countries' exports, trading partners would transfer the tariff revenues (or a share) to the TFTF. These resources would be used to service the tariff-for-trade bond, initially. After this initial period, as tariffs are collected and the FTF accumulates resources above the needs of bond servicing, bond issuance may no longer be necessary (see figure 4).

Figure 4: Tariffs-for-Trade: a proposal



Note: shaded arrows indicate flows at TFTF's initial phase when tariff revenues on graduated country's exports are not yet being generated.

The proposal is contingent on the collection of tariffs, which may not happen if graduating countries either negotiate FTAs with their major trading partners or participate in other preference granting arrangements (such as the GSP+ of the European Union). In some cases, tariff revenue collection may be small depending on the volume and composition of the export basket of the graduating country. The proposal requires further development. There is a great deal of experience and expertise in the IFIs that the United Nations could capitalize upon should it decide to give the proposal further consideration. Overall, the proposal is based on the concept that graduation may release resources that could be still used in support of graduating countries thus further signalling trading partners' continuous commitment towards these countries.

6. Summing up

The paper discusses a series of measures to strengthen the current framework of support for graduation and address some of the concerns LDCs have expressed when contemplating graduation from the category. It does not attempt at being complete or comprehensive in view of the heterogeneity of the category and the need to consider countries' context and specificities.

The recommendations include measures to push forward and kick start the preparation of the country's smooth transition strategy from the LDC category, with greater provision of advisory services and capacity building activities from the UN system, including improved links and greater synergies with the UNDAF process at the country level. It also envisages a more active role by the recently created Inter-Agency Task Force on Graduation. The paper recommends a revamp of the monitoring of graduating and graduated countries with fewer but more productive reviews of the preparatory and smooth transition processes. Lastly, it proposes additional measures and complementary inititatives that could further support the graduating countries in their transition effort.

Most of the proposals presented here either build upon existing initiatives or make use of resources that can be made potentially available with graduation. The paper understands these recommendations are preliminary and require further development. Yet, these suggestions provide a solid starting point for discussions with main stakeholders, in particular with the LDCs which need to have a more active role in the taking of decisions affecting their future.

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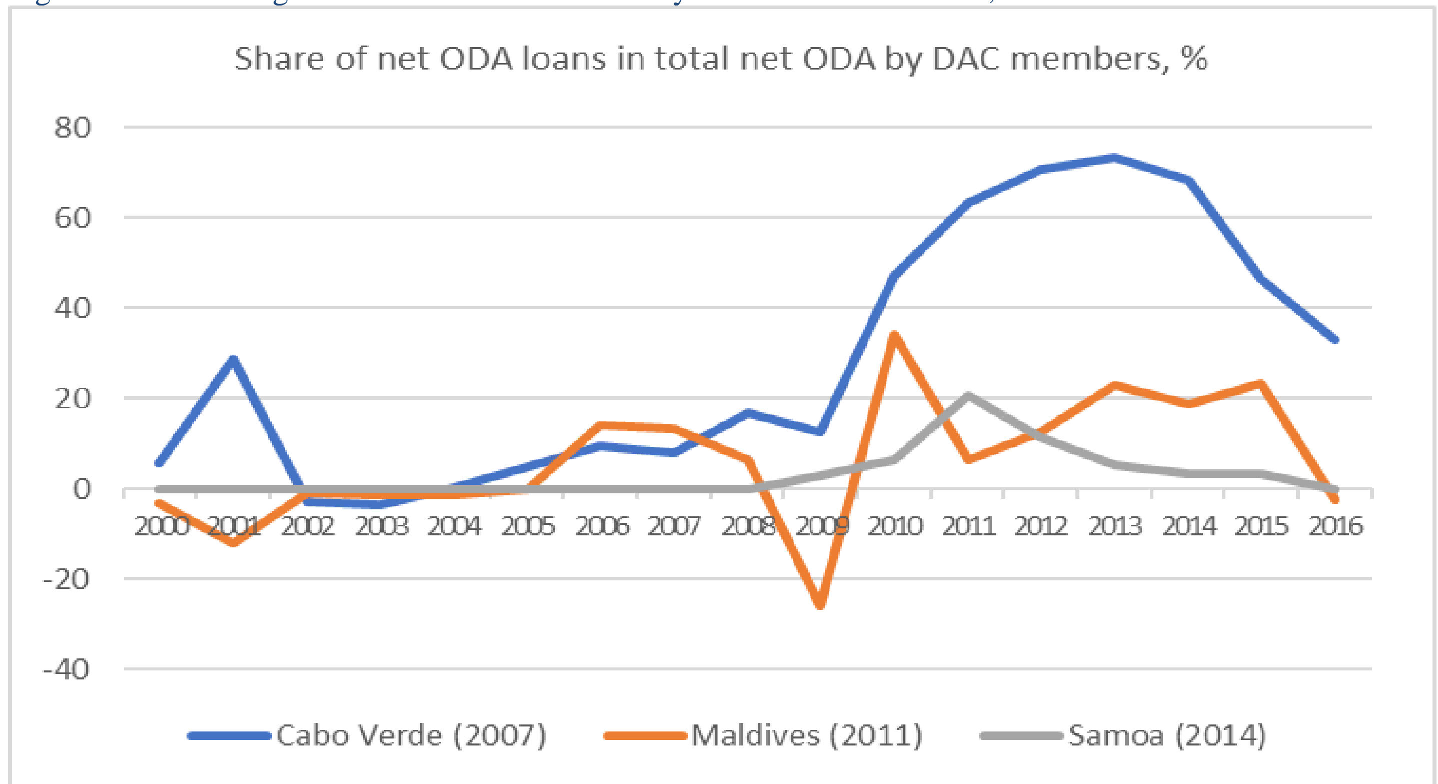
Annex

Table A1: The LDC category: evolution of graduation and graduation decisions, 1971-2018

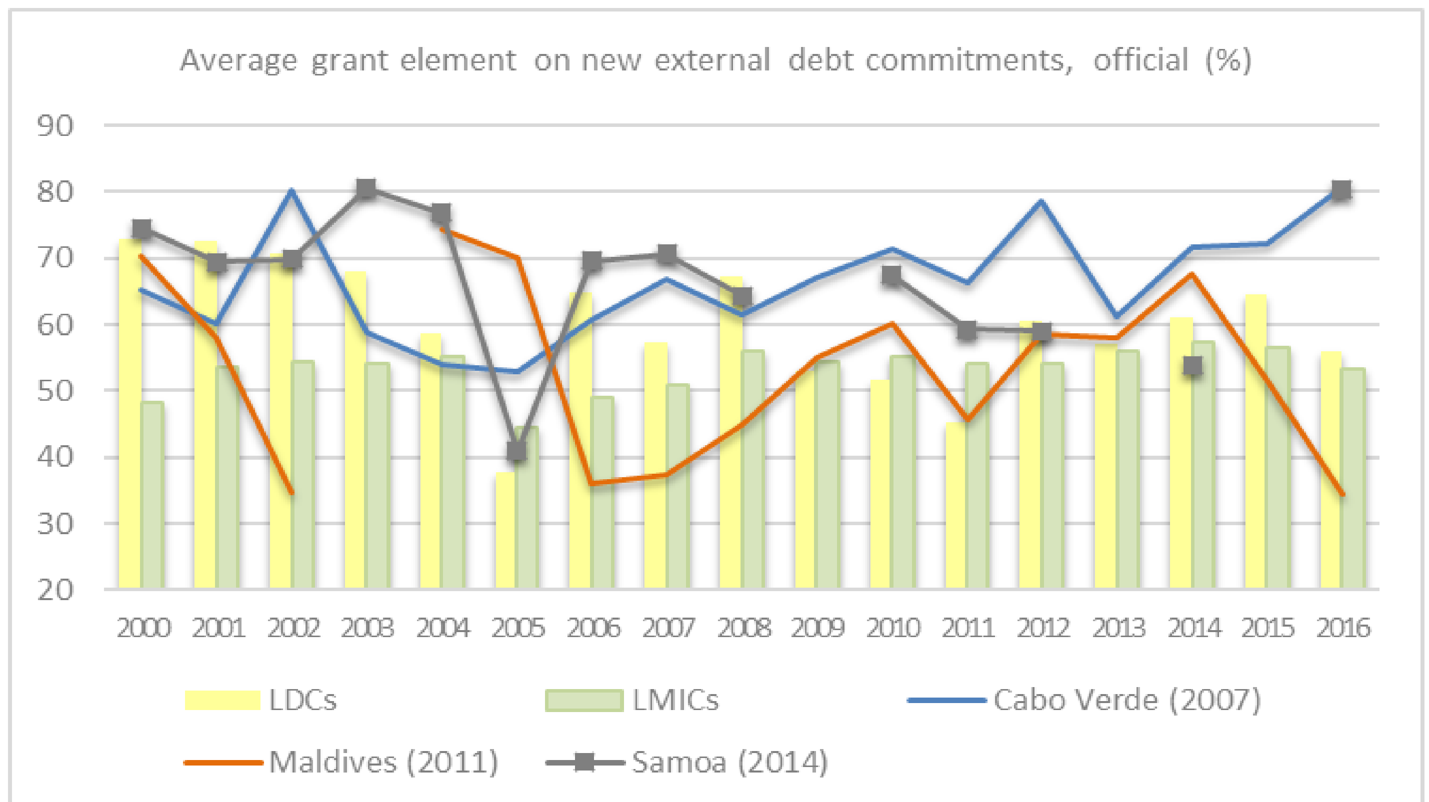
Year	Category/ graduation rules and process	CDP recommendation/finding		ECOSOC endorsement	GA takes note of CDP recommendation
		Eligibility	Graduation		
1971	Creation of the LDC category				
1991	Introduction of triennial reviews, inclusion and graduation rules; criteria updated		Botswana		Botswana *(3-year transition)*
1994	Triennial review	Vanuatu			
1997	Triennial review; A/RES/52/210 on assessing of an economic vulnerability index	Cabo Verde Maldives Samoa **Vanuatu**	Vanuatu	deferred	
1998					
1999	Introduction of vulnerability profiles; criteria updated				
2000	Triennial review	Cabo Verde **Maldives**	Maldives	deferred	
2001					
2002	Criteria updated				
2003	Triennial review	**Cabo Verde** Samoa	Cabo Verde	deferred	
2004	A/59/209 on Smooth transition provisions and triennial monitoring reports			Cabo Verde Maldives	Cabo Verde *(3-year transition)* Maldives *(6-year transition)*
2005	Criteria updated				
2006	Triennial review	Equatorial Guinea Kiribati **Samoa** Tuvalu Vanuatu	Samoa	deferred	
2007	Introduction of impact assessments			Samoa	Samoa *(3-year transition)*
2008					
2009	Triennial review	**Equatorial Guinea** Tuvalu Vanuatu	Equatorial Guinea	Equatorial Guinea	
2010					
2011	Criteria updated; IPoA: meeting graduation criteria as a goal; working group on smooth transition				

2012	Triennial review; A/67/221 on annual and triennial monitoring reports, use of LDC indicators for ODA allocation	Angola Kiribati **Tuvalu** **Vanuatu**	Vanuatu Tuvalu	Vanuatu Tuvalu deferred	
2013					Equatorial Guinea *(3.5-year transition)* Vanuatu *(4-year transition)*
2014					
2015	Triennial review	**Angola** Bhutan Kiribati Nepal Sao Tome and Principe Solomon Islands Timor-Leste	Angola	Angola Tuvalu deferred	
2016					Angola *(5-year transition)*
2017	Criteria updated				
2018	Triennial review	Bangladesh **Bhutan** **Kiribati** Lao PDR Myanmar Nepal **Sao Tome and Principe** **Solomon Islands** Timor-Leste	Bhutan Kiribati Sao Tome and Principe Solomon Islands	Bhutan Kiribati deferred Sao Tome and Principe Solomon Islands Tuvalu deferred	Bhutan *(5-year transition)* Sao Tome and Principe *(6-year transition)* Solomon Islands *(6-year transition)*

Figure A1: Selected graduated LDCs: ODA terms by OECD-DAC members, 2000-2016.



Source of data: Dataset: Aid (ODA) disbursements to countries and regions [DAC2a]



Source of data: World Bank, International Debt Statistics