The 2021 magic deadline: To be or not to be an LDC

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Bangladesh's least developed country (LDC) status has come under scrutiny by policymakers and development practitioners alike. In a Policy Research Institute (PRI) analysis titled Bangladesh in LDC status, published in the FE on January 02 last, Dr. Sadiq Ahmed argued that given the current state of economic progress, social and human development, Bangladesh hardly belongs to the group of LDCs listed by UN Committee for Development Policy (CDP). That list is dominated by a litany of under-developed African countries, and a few vulnerable landlocked or island states.
Being a predominant exporter of manufactures with a gross domestic product (GDP) of $225 billion, Bangladesh economy is unlike any of these countries. The problem perhaps lies in the selected criteria formulated for graduation out of LDC status that leaves Bangladesh languishing in the LDC group while an island economy like the Maldives (relying singularly on tourism and fishing activities and threatened with extinction due to sea level rise under climate change) graduates in 2011. This write-up seeks to delve a bit deeper into the pros and cons of being an LDC, while assessing the prospects for, and the potential resistance to, graduation out of LDC status.

For the record, only a handful of LDCs have graduated out of LDC status since the United Nations (UN) adopted this categorisation for several developing countries in the grip of abject poverty, low income, and constrained by other physical and economic vulnerabilities. Thus graduation has proved to be a long and arduous process taking several decades of social and economic progress. Once out of LDC status, the country loses the benefits available under the rubric of International Support Measures (ISMs) offered by the international community ranging from trade preferences to concessional finance and technical assistance. Appealing as they are one wonders if the existence of these benefits become a drag on some LDCs preventing them from growing rapidly out of under-development.

In 1971 when Bangladesh emerged as an independent country, it was in the company of Nepal, Chad, Rwanda and Burundi, countries with per capita income of US$100 or less. The same year, the UN introduced the notion of least developed countries with a list of 25 LDCs that included Bangladesh – countries that were recognized to have vulnerable economies suffering from low income poverty trap and facing particularly serious obstacles to achieving the structural transformation needed to advance economically and socially. The objective was to direct development resources and adopt international policies and special measures aimed at expanding their trade and improving their economic and social development to help accelerate their move out of LDC status. Instead, the list got longer over time reaching a total of 48 countries as of 2016. The vast majority of LDCs are in Africa (34), many are landlocked (e.g. Afghanistan, Bhutan, Nepal), and some are small island economies.

Only four LDCs have graduated in the 45 years since the establishment of the category: Botswana (1994), Cape Verde (2007), the Maldives (2011), and Samoa (2014). This prompted the international community to redirect attention on sustainable development of LDCs via the Istanbul Programme of Action (IPoA) in 2011, which set a goal of graduating at least one-half of LDCs by 2020. As it turns out, that is unlikely to happen and recently the United Nations Conference on Trade and Development (UNCTAD) has projected that only 16 LDCs are expected to graduate by 2025.

The good news is that Bangladesh has come close to meeting the graduation threshold and is on the UNCTAD's list of the 16 countries. The bad news is that it will have taken Bangladesh over 50 years to reach that milestone. The fact is that if the first 25 years had registered the kind of dynamism experienced in the second 25 years, Bangladesh would have graduated by now, to be counted among the "other developing countries" that are not LDCs.

To be sure, inclusion in the list of LDCs requires an endorsement of the UN's Committee on Development Policy and acceptance of the status by the government concerned. But any national government reserves the right to opt out of being considered an LDC and be excluded from the special dispensation accorded to them under the variety of ISMs favouring LDCs. It may be argued that by 2021, Bangladesh's 50th anniversary of independence, the country could well be facing that choice. Let us explain.

THREE CRITERIA: The CDP uses three criteria for classifying a country as LDC: (a) Income criteria (Gross National Income or GNI per capita); (b) Human assets (based on nutrition; child mortality ratio, school enrolment, adult literacy ratio); and (c) Economic Vulnerability originating from natural or trade-related shocks (e.g. from export concentration in primary goods), from smallness or remoteness. Apart from the income criteria (threshold of $1242 GNI per capita), human assets and economic vulnerability criteria are based on composite indices of various component features, each having a certain weight in the index.

For all three criteria, different thresholds are used for identifying cases of addition to the list of LDCs, and cases of graduation from LDC status. The CDP holds triennial reviews to determine if an LDC has met the graduation criteria. Applying these criteria, Bangladesh's standing as of 2015 is presented in Table 1.

In the 2015 triennial review Bangladesh did not meet the GNI and Human Assets Index (HAI) thresholds, but projections for 2018 based on current data indicate that Bangladesh will comfortably meet GNI and Economic Vulnerability Index (EVI) thresholds, as well as HAI (since it was only 2.2 short in 2015) in the 2018 review, and maintain that position for the 2021 review. A country will normally qualify for graduation from LDC status if it has met graduation thresholds under at least two of the three criteria, in at least two consecutive triennial reviews.

Under this rule Bangladesh would qualify for graduation in 2021. However, after CDP recommendation has been endorsed by Economic and Social Council (ECOSOC) and the UN General Assembly (UNGA), Bangladesh would benefit from a grace period (normally three years) before graduation effectively takes place (2024).The grace period is designed to enable a graduating country experience a "smooth-transition", so that the planned loss of LDC status does not disrupt the socio-economic progress of the country. Bangladesh has the prerogative to opt out of the grace period or even argue to extend it based on adverse developments, should that happen.

It is reasonable to argue that the CDP methodology is too mechanical and does not reflect reality. Reviewing Bangladesh's development progress noted by various other global assessments would show that it is very much an outlier among the group of LDC economies that is dominated by African countries, and some landlocked and island economies. In the context of progress with economic and social policies and institutions, World Economic

Forum’s Global Competitiveness Index (GCI) provides an indication of the maturity of an economy and its capability to address its development challenges. The 2016-17 GCI rankings put Bangladesh at 106 out of 138 countries included in the list, which is better than for such non-LDCs as Ghana (114), Cameroon (119), Pakistan (122), Zimbabwe (126) and Nigeria (127). In the area of Human Development, the United Nations Development Programme (UNDP) ranks Bangladesh 142 out of 188 countries and is grouped under “Medium Human Development”. Whereas countries like Kenya (146), Pakistan (147), Nigeria (152), Cameroon (153), Zimbabwe (155) and Cote’d’ Ivore (172) all belong to the “Low Human Development” (LHD) category of the UNDP but are not a part of the LDC group.

BENEFITS OF LDC STATUS: Regardless of these global assessments, Bangladeshi policymakers can hardly ignore the benefits arising out of LDC status. As an LDC, Bangladesh is the beneficiary of at least three significant support measures which have strategic development implications for its economy and society: (a) trade preferences, (b) Trade-Related Aspects of Intellectual Property Rights (TRIPS) exemption, and (c) concessional aid.

When it comes to trade rules and preferences under the World Trade Organisation (WTO), LDCs may deviate from the Most Favoured Nation (MFN) principle being entitled to special and differential treatment (S&DT). The LDCs have benefited from deeper tariff concessions under WTO’s Generalized System of Preferences (GSP), such as duty-free and quota-free (DFQF) market access. Bangladesh is among the leading beneficiaries of this arrangement as it exploited its comparative advantage in labour-intensive manufacturing exports. Though its exports into US market is subject to tariff peaks (e.g. on readymade garment or RMG), much of its exports to European Union (EU), Japan, Canada, India, and even China, enjoy DFQF market access, with concessional benefits running into billions of dollars. Clearly, without the LDC regime in these markets, competition would be tougher, and exports lower than they have been.

Next, when it comes to the Intellectual Property system, the WTO members recognized the special requirements of the LDCs, and the need for flexibility in the TRIPS agreement so that they could help create a viable technological base in these countries. In particular, TRIPS ‘flexibilities’ were applied to address public health problems in LDCs giving legal effect to a system which gives governments compulsory licensing authority to allow low-cost generic medicines (of patented drugs) to be domestically produced and also exported exclusively for the purpose of serving the needs of countries that cannot manufacture those products themselves. This TRIPS provision, supported with indigenous drug policies, has been a boon to Bangladesh's nascent pharmaceutical industry which now meets some 97 per cent of domestic drug requirements while exports approach $100 million. The provision, which expired in 2016, has now been extended to 2033, for all the LDCs.

Finally, a large portion of the official development assistance (ODA) disbursed by multilateral agencies (e.g. World Bank, Asian Development Bank) and bilateral assistance offered by the Organisation for Economic Cooperation and Development (OECD) countries (e.g. Japan, UKaid) are directed towards the LDCs. The World Bank uses its own income criteria whereby countries are classified as Low Income Countries (LIC), Lower and Upper Middle Income Countries (LMIC, UMIC), and High Income Countries (HIC). The World Bank's Atlas method is used to compute income per capita and determine country classification.

After being an LIC since inception, Bangladesh was placed in 2015 in the LMIC category, though its LDC status remained unchanged. As an LIC for over 40 years Bangladesh has been the recipient of a large quantum (estimated at $32 billion as of 2016 including recent commitments) of the World Bank's low-interest concessional loan doled out by its concessional arm IDA (International Development Agency). While Bangladesh approaches LDC graduation and moves up the World Bank's country classification, it stands to lose out on its receipts of concessional aid as it begins to access international capital at commercial rates.

Thus it might be argued that Bangladesh is faced with two mutually exclusive milestones in its socio-economic progress: becoming an Upper Middle-Income Country, and graduation from LDC status. If the economy remains in its current growth path, Bangladesh could be classified as UMIC around 2030 by which time it will have lost all access to IDA concessional loans. LDC graduation, on the other hand, involves a coordinated decision by the CDP/UN and acceptance by the Bangladesh government. Taking the three-year "grace period" into account, 2024 has become the graduation year to note. Does Bangladesh have an option to bring that date forward?

Graduation out of LDC status comes with its own charm – the absence of the stigma of LDC with connotations of poverty and under-development. It is a confirmation of broad-based development of productive capacities, diversification and structural economic transformation. Economic rewards could be significant as well. Bangladesh's credit rating by S&P or Moody's, which currently stands at BB- or Ba3 (non-investment grade), could rise a couple of notches, and foreign direct investment (FDI) inflows could get a boost so that Bangladesh could compete with Vietnam and Myanmar in mobilizing FDI resources for transport and energy infrastructure, as well as manufacturing. Available resources from multilateral agencies and global capital would be significantly higher.

What is notable is that the actual decision on graduation need not follow mechanically from the satisfaction of graduation criteria but would depend on the specific circumstances of Bangladesh, which would have to evaluate the likely impact of the ensuing loss of LDC treatment following graduation. An economy approaching graduation must make years of preparation to withstand the loss of ISMs. Loss of trade preferences will have to be countered by raising productivity and competitiveness in export sectors.

Given its success in RMG exports, one could make the case that the loss of trade preferences in another three to four-year period would not have a catastrophic impact on the Bangladesh economy. But TRIPS exemption will have to be met with quality improvements plus skill- and technology-intensive investments via FDI together with massive increase in research and development (R&D). Though the pharmaceutical industry has grown to meet practically all the domestic requirement for drugs with only modest export success, it cannot be said that the industry has reached the maturity to produce anything beyond generic drugs. LDC graduation will cause WTO MFN rules to kick in without S&D privileges. The costs from loss of trade preferences and TRIPS exemption could be substantial as to create resistance from losers. That gives rise to significant political economy considerations that must be factored into the approach to graduation. Finally, greater access to global commercial capital calls for maintaining sound and prudent macroeconomic management which Bangladesh has done so far.

LDC graduation is part of a system formulated by the UN's CDP to accommodate a smooth transition into the group of "other developing countries". If a country, in its own assessment, feels that it is no longer an LDC and has enough development momentum not to suffer economic disruption from losing ISM benefits, it has the prerogative to opt out of the LDC regime. Graduation will then be irrelevant. But the historical record shows that no listed LDC has done that. Should Bangladesh be the first? With all the promise of 7.0 per cent+ growth, rapid poverty reduction, and becoming a middle income country, should Bangladesh continue to remain an LDC? 2021, the 50th year of independence, could be a watershed in Bangladesh's socio-economic development process if it chooses to step out of the LDC community in that year. That would mean abandoning the three-year grace period. That would be a first since no LDC has done something like that. LDCs have been known to argue for remaining in that status rather than moving out. Can Bangladesh make history?

Bangladesh is left with two options: to graduate out of LDC in 2024 within the existing UN framework, or opt out of the LDC group on its own volition at a time of its own choosing. Rest assured, Bangladesh's LDC status could become a hot topic of discussion in the coming days.