



LDCs' Trade and Investment Challenges

A report and action plan of a group of NGOs in view of the Istanbul Summit of Least Developed Countries in May/June 2011

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Executive Summary

LDCs : a diverse group

Not all LDCs have the same opportunities and constraints to develop: a majority are medium-size countries with a small export base. Some have started to diversify into agro-processing and manufacturing, others into mining or modern services. Six oil producers are among the LDCs as well as a group of vulnerable small islands. Finally, a number of LDCs are in the throgs of civil strife and unresolved statehood.

Future development prospects

Many LDCs are in a good position today to move towards a sustainable high-growth path and reduce absolute poverty through employment, following the example of more advanced developing countries. We reach this conclusion after reviewing the LDCs' track record in the past decade and their reaction to the crises of the past years.

In the past decade development progress in many LDCs was remarkable. Before the financial crisis set in, growth of investment, GDP and exports was typically high, reaching Asian proportions. This was not only due to a price boom for agricultural and mineral commodities but also to foreign and domestic investment in infrastructure and productive sectors.

LDCs were struck first by a doubling of food prices (2007), then by a near-doubling of oil prices (2007-08) and, finally, by the financial crisis starting in September 2008. Confronting these challenges, many LDCs' policy stance was sound and revealed strong economic governance: Many lowered import tariffs on food, increased subsidies and reinforced safety net programs as a reaction to the food crisis. Oil importers absorbed the price hike of oil by increasing subsidies or lowering taxes on oil products. Most oil exporters saved the additional revenues in contrast to earlier oil booms.

When the financial crisis turned into an economic crisis, LDCs were severely affected, although on average less than other developing countries, owing to their low integration in the international economy. Investment inflows and remittances from diasporas slowed considerably. However, reduced commodity prices reversed the earlier shock for oil importers. Overall, LDCs recovered quite well from the financial crisis. In 2009, the GDP of African LDCs, without oil exporters, is estimated at 3.5 percent, and of Asian LDCs at 5.5 percent. Foreign direct investment picked up again starting in the second semester of 2009.

It is probable, therefore, that investment and growth will recover and that many LDCs will be able to pursue structural change towards more diverse production and exports. This is why we propose a development agenda for LDCs which focuses on trade competitiveness and investment. Such an outlook builds on the assumption that the recovery of the world

economy – including a driving role of emerging market economies – will continue on the present path. It also takes for granted that international cooperation is able to change from its earlier focus on social sectors and emergency aid to a strengthening of the business environment, trade and investment. Finally, it assumes that trade and investment policies of developed and advanced developing countries will support and not hinder the LDCs dynamic integration in the world economy.

A development agenda for LDCs

Opportunities for structural change and diversification are multifaceted and depend on the endowments and policies of each LDC. They may concern a broadening and increased processing of agricultural and mineral exports, finding niches in international manufacturing value chains and engaging in modern services.

As most LDC have small and shallow markets, a division of labor in productive investment with neighboring countries will in many cases allow for a scale of production which make output and exports internationally competitive and enhance trade. Therefore, stronger *regional economic communities* (REC) as well as *regional investment in economic infrastructure* are essential conditions for a successful diversification strategy.

Strategies for trade expansion and diversification have to be prepared. Their planning and monitoring should be inclusive, they have to be based on a sound analysis of the country's potential, and they should have an anchor in the government with considerable clout. A manageable group of policy reforms and projects should be selected to create and strengthen an enabling business environment, institutions to lower trade transaction costs, trade-related infrastructure, well informed trade policies, sustainable domestic and foreign investment, and a public-private partnership on trade promotion and information.

Sound investment governance is a must. Of particular concern are oil, gas and mining investments which are prone to non-transparent business practices. This is why LDC governments, involved in mineral investments, should adhere to the Extractive Industries Transparency Initiative which ensures that investments are properly appraised and then monitored, tracing payments made by extractive firms to host governments.

Foreign investment in agriculture has the potential to raise productivity and welfare but only if it respects the rights of existing users of land, water and other resources, associates local communities and improves their livelihoods, and does not harm the environment. All sizable investments in a country should be screened beforehand to ensure their sustainability. Such appraisal techniques should find their way into international investment treaties and host State-investor agreements, and LDC governments should acquire the skills to appraise and screen projects.

Another essential aspect of governance concerns *trade and financial relations*. LDC governments should partner with business associations, think-tanks and civil society groups not only for the development and monitoring of trade strategies but also for the preparation of specific reforms, for instance in trade facilitation. They should take into account the importance of exchange rate policies in the competitiveness of exports. Also they should better mobilize domestic revenues and other financial resources. This is a particularly important aspect in the selection of foreign investments but concerns more generally tax collection, the fight against tax fraud, mispricing and smuggling of traded goods, and international tax agreements to fight tax evasion.

At WTO the LDC Group has emerged as a negotiating partner with a single and strong voice over the last years. This role has now to be strengthened to deal with new challenges in the trade agenda. Therefore, *a small permanent Secretariat* will be required which will be able to organize meetings, inform members of the group, and prepare analytical inputs for LDC governments and international negotiations. LDC countries should come up with the core funding for the Secretariat themselves but get support for policy studies from development partners. Advice should extend to LDCs role in regional economic communities and trade and investment agreements.

Given the diversity in the LDC group, *trade and investment strategies will have to be adapted to each case*. Oil and mineral producing countries will be concerned particularly with avoiding a negative incidence of high revenues and prices on other sectors of the economy (“Dutch disease”) and will seek to create the fundamentals of a more diversified range of exports. Small islands will want to reduce their vulnerability to climate change and external economic shocks hitting their mainstay sectors. Finally, fragile States will often not be in a position to focus on trade and investment but should strive to maintain and create jobs wherever possible.

International community: trade and investment policies

Even more important than development cooperation are *trade, investment and technology policies of developed and advanced developing countries that give strong production and export incentives to LDCs*. In trade that means that the coverage of duty-free and quota-free preferences should be expanded to all products and all LDCs and even other small market low-income countries. Rules of origin should promote trade and investment and allow for inputs to LDC production to come from all developing countries. It also means concluding new-style trade agreements which maximize the positive effects on regional integration and market access of LDCs. These agreements should have as a companion aid for trade measures that are enabling, comprehensive and practical.

Industrialized and emerging market countries should put an end to the stalemate of the Doha Round and *agree to conclude the negotiations* which, with all their limitations, are to the benefit of LDCs. If this is impossible, at least an immediate “early harvest” should include the commitment to duty-free and quota-free preferences, the agreement on trade facilitation, and the more than proportional reduction of cotton subsidies.

A new type of North-South and East-South investment agreement should replace the thousands of old style investment agreements which have proved to be of little use. Besides a legitimate protection of investors this would imply giving support to a screening mechanism for important investments to ensure that investment projects follow sound practice and take into account also the interests of other stakeholders than the invested enterprise. Such agreements could give official support to proven voluntary guidelines for investors. Dispute settlement modalities also have to become more transparent, predictable and independent. A model agreement for sustainable investment was prepared in 2005 by the International Institute for Sustainable Development.

These recommendations are particularly appropriate for advanced developing countries which have become important trading and investment partners of LDCs. LDC trade with China, India and other advanced developing countries is highly imbalanced. In fact, there are cases where cheap imports from these countries displace local production in LDCs sometimes built up earlier by investors from the same Asian countries. Market access for LDC exports is still limited for many products by tariffs and, in some countries, complex product standards. Also, Asian countries have made substantial investments in mineral resources and infrastructure in LDCs. As a consequence, the risk of making unsustainable investments is considerable.

Development cooperation

The time has come to give priority in LDCs to trade competitiveness and economic diversification. *Governments and cooperation agencies should focus more decisively on these reforms than in the past.* Aid requirements are considerable. Only a small number of LDCs has been able to obtain adequate support so far to pursue this new agenda. And now additional demands will have to be addressed on the account of climate mitigation and adaptation in order to reach climate-resilient development.

The donor community should help each LDC to plan and implement a trade and investment strategy. This is not yet the case today. For instance, most bilateral donors in Africa have chosen only a few partners, and often these are the same for many donors. Multilateral agencies like the World Bank and the African Development Bank are able to give some counterweight to this aid concentration but are limited themselves by tight resource

constraints in their field presence in a number of LDCs. Strong technical representation in LDCs by donors is a must for an enhanced dialogue which will lead to effective assistance.

The Enhanced Integrated Framework is a good framework for aid alignment and harmonization to the extent that it becomes operational and down-to-earth. Yet, in many LDCs strengthened investment, trade policy and private sector development are still in the starting blocks. This has good reasons and cannot be by-passed by donors. But non-controversial reforms, capacity-building and trade infrastructure should make progress even if ideal institutional arrangements have not yet been sorted out. Donors and LDC stakeholders have a shared responsibility to make the Enhanced Integrated Framework work and accelerate its implementation. They should jointly report on progress and difficulties annually, country by country.

Support to this agenda requires an *expertise and presence in LDCs of cooperation agencies* which often goes beyond their resources and skills. Bilateral agencies should make an effort to train and upgrade their staff to become familiar with trade and investment policies of developing countries and particularly LDCs.

Finally, *monitoring and evaluation of projects and country programs* are essential tools but serve only their purpose if institutions learn by heeding recommendations made. Not many cooperation agencies have established reliable feed-back into new programs they finance. Both cooperation agencies and LDC governments should give more weight to monitoring and evaluation. Particular care has to be taken to ensure a rigorous feed-back of the track record into new operations, a function which the Enhanced Integrated Framework could coordinate.

Examples of initiatives in investment and trade cooperation

Regional cooperation and integration. The most important task now is to take stock of trends and develop policy prescriptions. This is best done in common with LDC researchers and policy makers in a combination of research studies and dissemination workshops. Based on this analysis cooperation agencies should give support to LDCs in their regional integration policies. Regional economic communities should run parallel to regional partnerships around a single common cause, for example in economic infrastructure.

Aid should enhance investment initiatives by LDCs. Diversification requires strong investment by the domestic private and public sectors as well as by foreign companies. Tools have to be found which enable higher investment and technology absorption as well as a sustainable choice and management of investment with high benefits to the society as a whole. Specialized equity funds, often funded by public resources because of the high risk involved, have been a preferred tool used in advanced developing countries in the past.

Other investment enabling tools are a one-stop shop for foreign investors and local investors looking for technical and marketing partners, regulation and incentives for backbone and business services, best-practice investment codes, and technical assistance to domestic public-private partnerships for investment projects.

A science and technology culture to facilitate technology transfer. Academic and vocational training as well as technological adaptive research should be attended to and reinforced in close cooperation with private enterprise. An essential element is literacy in information technology which has to be tied to improved access to telecommunications and information infrastructure. Adaptive research and development centers should be established in the main productive sectors helping to disseminate good practice. LDCs should explore and build-up capacity in intellectual property rights focusing on those rights which correspond to the country's present interests.

Agricultural exports and food security. Aid agencies have to focus much more than in the past on giving support to LDC agriculture. Particularly African LDCs have to invest in technologies and irrigation to use the sizable untapped potential and produce higher yields, following the lead of other developing countries. Higher production and exports, particularly to neighbors and the region, are essential for small countries as food security will improve if it is organized at the regional level. Agricultural research should also be considered a cooperative undertaking of the region.

Processing of commodities. Concrete proposals are to engage in research and development and market research of commodity-based products for instance through partnerships of research institutes and universities, provide credit and technical assistance to build up domestic processing capacity, encourage direct investments by international food retailers, and promote equity investments of domestic enterprises.

Modern services. LDCs should develop strategies to get services on their development map. They should then implement the action and reform program resulting from the strategy. LDCs would then be in a position to include trade in services in international agreements taking into account the country's interest and priorities.

Trade facilitation. It is uncontested today that a combination of thorough reform of Customs and other border agencies, more efficient trade logistics services and regulation, and improved infrastructure have a good potential to lower export and import costs, often more than reducing tariffs. The positive impact on land-locked LDCs is greater, if efficient trade corridors to ports are organized.

Lowering business costs by improving business procedures and management. In the last years, cooperation agencies have increased their support to the business sector in low-income countries. One vector has been complex business procedures, that is the time required to establish enterprises, and the cost of public intervention in their management and their trade.

The international and domestic private sector

Dynamic pre-crisis investment is expected to recover. Besides major investment in extractive industry, private investment in LDCs is increasing again. LDC governments have to gear up to engage with investors, be they foreign or domestic. While developed countries remain the main source of foreign direct investment in many LDCs, the field has increased not only to some emerging market countries such as China, India, Malaysia, and Russia but to many others including African countries.

Contracts between host States and investors. It will be essential for foreign investors and financiers to follow sound investment criteria which have been anchored in voluntary investment codes and international agreements. Also, LDCs should now lay down the criteria which they will use in screening foreign investment and make them public so that investors know the rules. Recently, the International Bar Association took the initiative to develop a model mining development agreement to serve as a negotiation template for investor-State agreements in the mining sector in developing countries.

Foreign direct investment has to be beneficial for LDC stakeholders and has to draw in local investors. Investments have to be profitable also for workers, suppliers, service providers, and the government. Local producers and investors should be associated through joint ventures or supplies and services. The investment has to be environmentally and socially sound. Finally, in the case of sizable and intrusive investments, local communities have to be consulted.

Domestic investment is essential, independently from FDI. In many cases investment grows out of domestic trading activities, SMEs and microenterprises, be it in agriculture, manufacturing or services. Governments have to create a level playing field for these new entrepreneurs and strengthen the local business culture through good training opportunities.

Remittances for investment of the diasporas. Some emigrates would like to invest in their country of origin but not as direct investors. They have to be able to rely on sound investment agencies (investment companies or operational entrepreneurial NGOs) which are willing to submit projects, report on investments transparently and fully, and know how to cope with domestic administrative rules.

Main Report

A. Background

1. This document is an input to the UN Istanbul Summit of LDCs which will take place from May 30 to June 3, 2011. It is addressed to governments of the North and the South as well as international agencies who participate in the Summit. It also examines the role of private corporations, particularly international ones. It is the result of “brainstorming” of experts from a number of NGOs and other institutions active in trade and investment from June to October 2010. The preparation of this report benefitted from a grant of the Swiss Agency for Development and Cooperation.

2. The action plan focuses on trade and investment because the authors are of the view that many LDCs are in a position to diversify their production and exports and embark on a phase of sustainable development. The international community should support LDCs in this drive. Recommendations are therefore directed at LDCs first, because they are in the driver’s seat. But then governments of developed countries, advanced developing countries and multilateral agencies are asked to pursue more determined and comprehensive support strategies to LDCs. Finally some suggestions are made also to international and national enterprises.

B. The LDC group today

A diverse group

3. Since its creation in the early 1970s the countries of the LDC category have evolved in a way that make an analysis of their development status as a group difficult. A separation into five sub-groups is useful, even if frequently countries participate in more than one sub-group:

- A majority of LDCs are countries, mostly African, with a small to medium-size population and a narrow range of production and exports, mostly limited to the primary sector; part of them are land-locked, which reinforces their vulnerability;
- A few LDCs, mostly Asian (Bangladesh and Cambodia are the most prominent ones) but also some African countries and Haiti have expanded into textiles and garments, other manufacturing and agro-processing, and occasionally modern services;
- The economy and exports of several countries are driven by the oil sector: Angola, Chad, Equatorial Guinea, Sudan, and to a lesser degree Timor-Leste and Yemen. These countries are prone to “Dutch disease”;

- A group of LDCs are small islands or continental mini-States; while their per capita income is typically rather high, they are more vulnerable to external shocks hitting their mainstay sectors.
- Finally, another group of LDCs may be considered fragile States because of volatile governance and civil strife, often owing to unresolved issues of statehood and treatment of minorities. Traditional economic cooperation often is a limited part of a cooperation package which assists mainly in preventing conflicts or stabilizing governance.

Development prospects before the financial crisis¹

4. In the 2000 decade development progress in many LDCs was remarkable before the international financial crisis set in: for the LDC group, investment, GDP and export growth rates were very high, 7.1% per year for 2001 to 2009 with the highest rates from 2006 to 2008. In many cases external debt was reduced substantially, often thanks to the HIPC initiative, and inflation rates dropped to safe levels.

5. Several factors explain this progress. Export prices were high both for agricultural and mineral commodities; some LDCs profited particularly from the oil boom in 2007-2008. Especially Chinese and other Asian companies invested not only in oil and mining but also in infrastructure, manufacturing and services. Foreign aid and remittances increased substantially. As a result of this favorable external environment and a substantial increase of domestic investment, production started to recover and diversify in many LDCs. Not only mineral products were concerned but also their processing, non-traditional agricultural products, agro-business, manufacturing, infrastructure and services.² Better economic governance in many LDCs definitely helped to improve the investment climate. Since the mid-1990s, many LDCs have undertaken macroeconomic and fiscal reforms which are starting to pay off (World Bank 2010).

6. UNCTAD 2010 points to the risk that this high growth period might not have led to “structural progress” in LDC economies but might rather have made them more vulnerable as the share of commodity exports in GDP has increased in many cases. Yet, higher savings from the commodity boom may well lead to higher investments and structural change. Also, even if manufacturing shares of GDP, in the case of African LDCs, have remained stable over

¹ This and the following paragraphs in section B. have two main UNCTAD sources: The recent report (May 12, 2010) on key challenges facing the LDCs (TD/B/EX(49)/2), henceforth called **UNCTAD 2010**, and the **World Investment Report 2010** (published July 22, 2010) which comprises a sub-chapter on LDCs, pages 60 to 63. It also refers to a chapter of a just published World Bank report (end September 2010): Devarajan Shantayanan and Shetty Sudhir, Africa: Leveraging Crisis Response to Tackle Economic Challenges, in Canuto Octaviano and Giugale Marcelo, eds., *The Day After Tomorrow*, The World Bank, Washington DC, 2010 (henceforth **World Bank 2010**).

² The UNCTAD 2010 report mentions that considerable FDI took place in food, beverages and tobacco as well as in services like transport, storage, communications, hotels and restaurants.

the period, this still meant considerable growth in manufacturing product and exports, given the high overall GDP increase.³ High-value investment, mainly in oil and mining, was concentrated in a few mineral-rich countries while a high number of small foreign investment ventures in manufacturing and services spread over many countries: from 2003 to 2009 over 1200 green-field projects were registered in LDCs, of which 470 in manufacturing and 530 in services (World Investment Report 2010).

7. Although Chinese investment has been oriented towards extractive industries in Africa, it appears that private Chinese and Indian enterprises are increasingly investing in apparel, food processing, retail ventures, fisheries and seafood farming, commercial real estate and transport, tourism, power plants and telecommunications.⁴ Furthermore, intra-regional African investment is starting to make a dent, if one looks at recent investments of South-African, Nigerian and Kenyan companies in other African countries (World Investment Report 2010).⁵

8. Also, for some LDCs the best option has been to diversify into a broader group of traditional and non-traditional agricultural products and to expand exports through productivity increases in farming. This may lead to new diversification options in a second stage.

Impact of the triple crises

9. LDCs were struck first by a doubling of food prices (2007), then by a near-doubling of oil prices (2007-08) and, finally, by the financial crisis starting in September 2008. The reaction to the food crisis of African LDCs was sound. Only a few introduced price controls. Many lowered import tariffs on food, increased subsidies and reinforced safety net programs. Yet, these safety nets for the poor happened to be effective only in a few cases, for instance in Ethiopia.

10. Oil importers absorbed the price hike of oil by increasing subsidies or lowering taxes on oil products. Most oil exporters among the LDCs saved the additional revenues in contrast to earlier oil booms.

11. When the financial crisis turned into an economic crisis, LDCs were severely affected, although on average less than other developing countries owing to their low integration in

³ This does not exclude important instances where the closing of firms, e.g. in textile production (which started in the 1980s in Africa) has continued as a result of cheap imports for instance from China. A Nigerian example is mentioned in paragraph 84.

⁴ Broadman Harry G., *Africa's Silk Road*, The World Bank, 2007.

⁵ Indications in the World Investment Report 2010 are confirmed by anecdotal evidence collected by the author in talks with officials and experts in African countries.

the international economy. Investment inflows declined by 14 percent (to USD 28 billion) in 2009 while remittances from diasporas slowed considerably. However, reduced commodity prices reversed the earlier shock for oil importers; they tightened foreign exchange income of heavy oil exporters considerably and led to stagnation in some countries in 2009. This explains that, overall, LDCs recovered quite well from the financial crisis. In 2009, the GDP of African LDCs, without oil exporters, is estimated at 3.5 percent, and of Asian LDCs at 5.5%. Yet this still meant that 270 foreign-invested projects were started, often in financial and business services. Sixty percent of these originated from developing and transition countries (World Investment Report 2010).

12. Prospects for 2010 and the years afterwards are for GDP rates to rise but not quite to the 2006 to 2008 levels. Foreign direct investment picked up again in the second semester of 2009 and particularly in the first quarter of 2010. This does not yet make LDCs a preferred investment destination as market size is often small and investment conditions are still judged to be weak in international reference publications. But it points to a dynamic upward trend and the growing role of new investors. It also reminds us of the important role of regional integration and development cooperation to help LDCs overcome some of the remaining investment barriers.

Future prospects

13. It is probable, therefore, that investment and growth will recover and that many LDCs will be able to pursue “structural change” towards more diverse production and exports in the five directions mentioned in the next section. During more difficult times for LDCs in the 1980s and 1990s international cooperation focused increasingly on support of social services and infrastructure to make progress in poverty reduction. In a period of low growth or stagnation leading to increasing poverty rates in many countries, this was an urgent investment to limit the scourge of absolute poverty. Yet this meant fighting the symptoms and – through better access to education and health services – creating the fundament for future growth and diversification.

14. Times have changed: many LDCs are in a position now to move towards a sustainable high-growth path and reduce absolute poverty through employment, following the example of more advanced developing countries, including some direct neighbors. Now the support of industrialized and emerging development partners alike has to include production diversification and trade competitiveness.

15. Obviously, this does not mean that the past emphasis in international aid was wrong or has now to be abandoned. It should continue and complement the investment and production focus but with a new goal: to prepare LDC (often very young) citizens to cope with more diverse and demanding jobs, become entrepreneurs and skilled workers, staff of

increasingly modern and efficient public institutions, and experts of research and education institutes.

16. This outlook is based upon optimistic but realistic assumptions on the main factors which will enable LDCs to recover from the triple crises of the last years and engage again on a high-growth path. The main external enabling factor will be a recovery of the world economy with emerging market economies as strong front-runners and more hesitating developed countries, which is at this time the most likely scenario. The latter will take longer to get back on a track which fully reaches their potential growth. Yet, “[t]he prosperity of [Africa] is now equally – or more – dependent on demand and investment from developing world countries – China foremost among them.”⁶ This is true for non-African LDCs as well. A second external condition for success in resuming growth is the continued increase of external aid – as well as best efforts to strengthen its efficient use – in spite of a high debt stock in OECD-countries, owing to their policies to recover from the financial crisis.

17. Domestic enabling conditions for a high-growth path are the object of the next chapter of this document, an action plan to enhance trade competitiveness and investment. The challenge is to create sufficient job opportunities for the very sizable cohorts of young people wanting to enter the job market each year, to create a business environment that facilitates production and exports – emphasizing most critically investments to provide reliable and less expensive energy and to increase dramatically land under irrigation – and to continue improving the quality of public sector management. Progress made in governance in the past years before and in reaction to the triple crises are an antecedent which makes further improvements feasible.

18. Special attention will have to be paid to LDCs which are not yet ready for such an optimistic outlook. New forms of cooperation with fragile States will have to become more common to help them find political stability and peace and consolidate their economies. The successful experience of small island States should be used as model for some small island LDCs, and oil-rich LDCs should use the vast experience of other oil-rich countries on how to avoid the pitfalls of an oil-driven economy.

⁶ Wallis William and Burgis Tom, The continent drives a harder bargain, in Financial Times Special Report, *Africa-China Trade*, June 14,2010, page1.

C. A development agenda for LDCs

The directions to be taken by expansion and diversification

19. This very short status report leads to the conclusion that the development agenda of LDCs should be geared to making sustainable the first successful steps in production and export diversification. This is a new prospect for most LDCs and requires them to put a much stronger emphasis in their development planning on economic diversification and trade development. Development cooperation partners will also have to follow suit as we explain in the following section. The following proposals are geared both towards the few LDCs which already have a relatively diverse production and export offer, and the majority which are embarking on economic diversification. The proposals will have to be adapted to oil-rich LDCs and small island States (and other micro-States). Their usefulness for fragile States is more limited at the present time.

20. LDCs should expand and diversify production in five main directions, often concurrently and sometimes sequentially, departing most often from a narrow agricultural and mineral commodity base. They should:

- make commodity production more cost-efficient, expand exports to traditional destinations and find new markets for them, particularly in emerging and other developing countries;
- diversify agricultural production particularly into non-traditional products;
- process local commodities associating, if useful, external investors;
- produce or increase the production of labor-intensive manufactured goods, entering into global value chains without relying only on national commodity resources; regional and other imported resources and inputs could be used;⁷
- diversify into modern services, both those that sustain production and export diversification (e.g. backbone as well as business and information technology services) and those that are directly consumed like tourism. As explained below, in regions with generally small and a number of land-locked countries, the main economic infrastructure, that is transport, energy production and telecommunications, including broadband internet access, have to be planned at the regional level.

⁷ Particularly in the few big LDCs (particularly Bangladesh and Ethiopia) it will be easier to create over time "forward and backward linkages", including a network of foreign-invested and national suppliers and new agricultural and livestock production, which may be necessary as input for certain manufactured goods.

Domestic drivers for export expansion and diversification

Regional cooperation and integration

21. As most LDC have small and shallow markets, a division of labor in productive investment with neighboring countries will in many cases allow for a scale of production which make output and exports internationally competitive and enhance regional trade. Therefore, stronger regional economic communities as well as regional investment in economic infrastructure are essential conditions for a successful diversification strategy. To mount and manage specific investments and reforms, ad-hoc groups of interested countries are often an efficient form of association. Regional integration should be given emphasis in development cooperation (see paragraphs 80 and 81).

22. A good example of renewed dynamism in regional integration is the East African Community. Its five members, four of which are LDCs, are negotiating now the conditions for preferential regional trade in goods and services. Common external tariffs have been decided but will only be applied after some time.

Strategies for trade expansion and diversification

23. Presently, most LDCs plan their future trade involvement by designing trade and private sector strategies which lead to action plans. The Enhanced Integrated Framework (paragraphs 75,75,78,79) is an international initiative to help LDCs to develop action plans and mobilize external cooperation and funding for their implementation. Action plans are then transformed into specific policy reforms, investment projects and capacity-building to modernize trade and investment institutions. Experience with such strategies in a number of African LDCs indicates that five basic elements condition their success.

24. ***Inclusive planning and implementation.*** Main concerned groups in a country have to be involved as key partners in designing the strategy and developing an action plan. They also have to be part and parcel of implementing and monitoring the action plan. To some extent a strategy is a means to build local capacities. At the end of the process a group of national experts and public officials should identify with the strategy and be able to advise the government on trade policy, business development and instruments to lower trade costs for local exporters. Trade sector studies (DTIS) undertaken in the first years of the Integrated Framework, in the early 2000s, were a first good step but did not always correspond to this condition and, today, are often not fully used in the planning of reforms and projects. The jury is out on the impact of the few trade sector studies undertaken since the Integrated Framework became the Enhanced Integrated Framework in 2009.

25. ***A participative and technically sound trade development strategy.*** The priorities and specific actions and projects should be proposed by domestic working groups. These groups should take advantage of technical tools which have been developed by academia and multilateral organizations to make proposals to the government: e.g. value chain analysis, ITC internet tools to establish destination market profiles for specific export products, export potential assessments, export income potential based upon revealed comparative advantage, and space methodology.⁸

26. ***A manageable group of projects and policy reforms.*** Action plans should be specific enough to lead to the preparation of a pipeline of priority projects and policy action. The LDC Government then takes up those projects and reforms with external development partners, which require technical and financial support.

27. ***Six areas of intervention:***

- an enabling business environment e.g. facilitating regulation for enterprises, the building-up of modern market institutions, financial market support through credit and equity, skills development, technology adaptation, and business courts which administer speedy and efficient redress;
- modern institutions to lower trade transaction costs and facilitate market access that is for instance trade facilitation/Customs, trade logistic and transport regulation and services (including cooperation with neighboring countries), technical standards and voluntary labels;
- trade-related economic infrastructure;
- international trade policies;
- policies to promote domestic and foreign investment;
- a public-private partnership for trade promotion and trade information.

28. ***Institutional anchors.*** A good option to ensure inclusive management of such a process is to form a trade council, comprised of the main stakeholders, and a technical coordinating agency, usually part of the Ministry of Trade. These will be put in charge by the Government to direct and monitor policy reforms, and monitor capacity-building and investment projects which will be implemented by domestic public and private agencies or partnerships.

29. It is not possible to explore all these areas in this note but a number of examples will be given in Sections D, E and F on how the international community as well as international

⁸ These last two tools mentioned were recently used by experts which studied options for diversification in Burkina-Faso as part of an economic memorandum of the World Bank: Chandra Vandana and Osorio-Rodarte Israel, *Options for Income-Enhancing Diversification in Burkina-Faso*, Munich Personal RePEc Archive, 24 November 2009. <http://mpira.ub.uni-muenchen-de/20928/>

and domestic enterprises could support such an agenda for trade competitiveness and economic diversification. It is essential however to point at this stage to the importance for LDC governments to follow sound governance principles when they decide on and implement trade and investment policies and projects, authorize foreign direct investments, are a partial or full owner of an investment, and shape international trade policy.

Sound investment governance is essential

30. The funding conditions and distribution of risks, particularly of sizable investments in mining and economic infrastructure, have to be carefully evaluated to avoid that LDC governments incur inconsiderate debt risks, now that debt levels have been brought under control in most LDCs.

31. *Oil, gas and mining investments* are often little transparent in respect to the terms and conditions of contracts concluded for them. Critical issues are the identity of the investment's owners, auditing and publication of accounts, procurement, investment incentives obtained, payments to third parties and other financial arrangements. Often, they are prone to corruption. It is essential for LDC governments to adhere to and implement international transparency norms, notably the Extractive Industries Transparency Initiative (EITI) which ensures that investments are appraised and then monitored, tracing payments made by extractive firms to host governments. Civil society groups are involved in appraisal and monitoring and, to ensure a meaningful oversight, host State-investor contracts are publicly available, hiding truly confidential business information. Many LDCs counting on foreign direct investment in mineral resources have already subscribed to EITI or are about to do so. The main challenge for them is to turn their commitment into operational reality, going all the way from candidate status to compliance.⁹ Revenue transparency may be a prerequisite but is not sufficient to ensure a positive developmental outcome. It is paramount that governments allocate extractive revenue to priority sectors, mainly to diversify the economy.

32. Like in other developing countries *foreign direct investment in agriculture* has increased considerably in a number of LDCs. This has to do with the 2008 price spikes in food and fuel prices, the desire by food-importing LDCs to secure food supplies, a similar demand by emerging economies to ensure their future food supplies, speculation on longer-term international land and commodity price increases, and the search for bio-fuels as alternative energy source. In twelve African LDCs imports accounted for more than thirty per cent of grain supplies.¹⁰

⁹ The Extractive Industries Transparency Initiative is well explained on the EITI website: <http://eiti.org/>

¹⁰ *Issues notes for the sessions*, Brainstorming Meeting on the substantive preparation for UNLDC IV, UN-OHRLS, July 2010, page 5 (source not cited).

33. Such investment has the potential to raise productivity and welfare but only if it respects the rights of existing users of land, water and other resources; associates local communities and improves their livelihoods; and does not harm the environment. A group of international organizations have defined seven principles to ensure the quality of such investments.¹¹ These are now discussed in international forums and might become guidelines for governments and investors. LDCs should incorporate these principles into their agricultural policies and planning, and use them as part of the approval criteria for foreign and domestic investment in agriculture.

34. Some of the provisions in guidelines in mining and agriculture are valid for *sizable investments in all sectors*, be they foreign or domestic. Such principles are also retained in voluntary guidelines for international banks and sovereign wealth funds, the Equator Principles and the Santiago Principles. All these guidelines have their origin in investment practice and safeguard policies developed by multilateral public finance institutions that is mainly the World Bank and IFC but also Regional Development Banks. They are used by LDCs in that context. For investment to have a good potential to be sustainable, it has to be submitted to thorough feasibility studies and risk analysis.

35. Such an investment screening includes, very generally, the following:

- the project has to be profitable in the long-term not only for the investor but also for local stakeholders (workers, local suppliers and service providers, local communities and government);
- in the case of foreign investment, local investors and enterprises – or producers in the case of agriculture – should be associated to the investment, in the first place by participating in it (joint ownership) or then by becoming suppliers or service providers to the foreign-invested enterprise.
- The investment has to be environmentally and socially sound. In infrastructure and extractive industries this means mainly to mitigate environmental risks and choose the least invasive investment option. In industry, services, and agriculture cleaner production technologies and energy-efficiency options should be used. Social management methods, besides corresponding to the respect for basic human rights, are often today a plus for exports because they help an enterprise in accessing markets.
- In sizable private and in public investment, local private stakeholders – the directly affected population but also civil society organizations, local government and private sector organizations – have to be consulted during the design of the investment and should participate in monitoring. This implies that draft agreements are made public and open for consultation.

¹¹ *Principles for Responsible Agricultural Investment that Respects Rights, Livelihoods, and Resources*, a discussion note prepared by FAO, IFAD, the UNCTAD Secretariat and the World Bank Group to contribute to an ongoing global dialogue. This document was discussed at UNCTAD's Investment, Enterprise and Development Commission in April 2010, TD/B/C.II/CRP.3, 16 April 2010.

36. Most LDC governments are familiar with this approach to investment because it is the one required by multilateral public investment financiers (paragraph 34). It would be important for LDC governments to build technical capacities to screen investment projects, create investment incentives focusing on these sustainable investment requirements, and use these before authorizing or entering into a contract on an investment. Such criteria could be reflected in “new style” international investment agreements, negotiated bilaterally with home countries of investors or at the regional level, as well as in host State-investor contracts. We will make reference to such agreements and contracts in Sections D and F.

Governance in international trade and financial relations

37. As in the case of strategic investments, LDC governments should partner with concerned domestic groups on trade policy and trade institutions. This concerns business, employer and producer associations in the first place. Think tanks on external trade are emerging in some LDCs and other stakeholders are sometimes organized as NGOs. Such consultations should take place when trade strategies and action plans are developed as well as when negotiations are undertaken. Local experts groups should also accompany specific reforms and regional negotiations as for instance for Customs, trade facilitation and transport. Along some trade corridors they have proven to be essential partners in the harmonization of transport regulation, tax regimes and trade facilitation. This will be a good breeding ground also to form public-private partnerships for specific investments and projects in the transport and trade sectors.

38. From observing the international trade scene, it is quite obvious that exchange rates have something to do with export competitiveness. This point was driven home by a recent study which examined what could best explain the high and sustainable growth rates of a number of countries on all continents. The authors found that “...export surges in developing countries tend to be preceded by a large real depreciation – which leaves the exchange rate significantly undervalued – and a reduction in exchange rate volatility.”¹² Quite a few LDCs have exchange rates which reduce distinctly export competitiveness and should be substantially reduced. The most egregious example is the francophone countries in West and Central Africa whose currency is tied to the Euro.

39. A trade and investment strategy can only be successful if LDCs are better able to mobilize domestic financial resources.¹³ Substantially higher revenues is often the result of

¹² Freund Caroline and Pierola Martha D., *Export Surges, The Power of a Competitive Currency*, Policy Research Working Paper 4750, World Bank, October 2008.

¹³ This is one of the main topics of the *African Economic Outlook 2010*, a joint publication of the OECD Development Centre and the African Development Bank, see <http://www.africaneconomicoutlook.org/en/>

improved bargaining power of LDC governments with foreign investors in extractive industry given the heightened interest in mineral investment. As a result, LDCs are able to reduce their aid dependency.

40. LDC governments should improve their fiscal policies in several ways. They should:

- Collect taxes more efficiently and fight tax evasion and fraud particularly of enterprises, wealthy citizens and foreign investors;
- Use their bargaining power in primary sector investment by choosing investors through competitive bidding;
- fight the mispricing and smuggling of traded goods;
- negotiate tax agreements with industrialized and advanced developing countries to fight international tax evasion by way of transfer pricing and financial investment abroad;
- in the case of African LDCs, participate in the African Union/NEPAD's peer review mechanism on governance.

How can the LDC group have a stronger voice in international organizations?

41. At WTO the LDC Group has emerged as a negotiating partner with a single and strong voice over the last years. This role has now to be strengthened to deal with new challenges in the trade agenda. Therefore, ***a small permanent Secretariat will be required*** which will be able to organize meetings, inform members of the group, and prepare analytical inputs for LDC governments and international negotiations.

42. How can such an effort be funded? We recommend that the LDC countries come up with the core funding for the Secretariat themselves, that is the permanent staff and expenses for basic logistics. Why? In a negotiating environment where economic and trade interests of different country groups clash and alliances change frequently, financial independence is an essential ingredient of political strength and negotiating credibility. Yet, the intellectual strength and efficiency of the group will depend on policy studies which are then discussed by LDC government to decide on their positions. Development partners, including emerging economies, and NGOs should contribute to such a fund.

43. The trade agenda might not include only WTO matters but also for instance the position of LDCs in regional economic communities, particularly when the members come from different income groups (what are the special and differential treatment provisions for LDCs?) or the role of LDCs in North-South trade and investment agreements. LDC countries will have to choose a limited set of concrete issues where the group needs to have a strong position. The Secretariat could also serve in monitoring the functioning of the Enhanced

Integrated Framework. Once up-and-running, the Secretariat should then study the strategy and tactics involved in strengthening the voice of the LDC Group in other international organizations.

The special case of oil-rich LDCs

44. While the oil and gas wealth could be a welcome source of financing development, it has developmental drawbacks, as the experience of many oil economies attests to. External cooperation should focus its support to oil-driven LDCs to cope with these specific issues which are well known but difficult to deal with.

45. Oil is a **source for corruption**. It is to be commended that most oil-producing LDCs in Africa are candidates for the EITI. Yet none has qualified so far as compliant country, and Equatorial Guinea has been excluded in April 2010 because it was not willing or in a position to submit the required validation documents for its oil investments in the two year window open for such submissions.

46. Oil development may act as an **obstacle to the growth and exports of other sectors** (a phenomenon which is called “Dutch disease”) and as a destabilizing factor for sound macro-policies. It requires excellent fiscal and monetary management and strong production and export incentives in other sectors to counter these negative effects of a strong oil sector. An investment pipeline has to be prepared to enhance social and non-oil economic development. In some cases oil revenues should be invested temporarily outside of the national economy to sterilize their monetary incidence for some time while using investment income for national development.

47. Export processing zones and technology parks may counter the worst impact of Dutch disease by **promoting competitive tradable sectors outside oil**. They are usually insulated from extreme forms of rent-seeking that often characterize oil and mining sectors.

48. Oil-rich LDCs have a higher investment capacity than other LDCs and for that reason are better able to **invest in institutions which will improve governance in the long term**. They should use this capacity to create universities and research institutions oriented towards the professions and technologies needed for economic diversification and should strengthen their justice systems so that they provide easy access and reliable and efficient redress to disputes. In both cases international partnerships with university departments and professional associations could prove to be essential.

The priorities of fragile States

49. The specific causes for weak governance are multifaceted and unique in each fragile State but they are often related to civil wars and other actions to contest the legitimacy of a government. “Fragile” means that a government is unable to ensure the security of the country’s population and work efficiently for poverty reduction and development. Under these circumstances, the priority for a local government usually is conflict resolution, security and peace-building while the economy is kept afloat in an emergency mode.

50. A strong focus on trade and investment is not always possible and the capacity to attract productive investment is limited. Yet creating job opportunities for demobilized combatants and returnees is critical to the consolidation of peace. Even in the direct aftermath of war, there are ways to stimulate production and employment which have quick effects. In addition, making progress on economic and trade issues is often part of conflict resolution, as shown for instance by the need for an oil revenue-sharing agreement between North and South Sudan. The country plans to hold a referendum in the Southern territory of the country on the question whether Southern Sudan should become independent. In case the referendum leads to a partition, the attribution of oil resources to the two parts of the country, the price for transport and refining of oil, and more generally the planning of economic and trade cooperation are high on the agenda.

51. Here again, business and economic interest groups outside oil and minerals should be promoted to counter-balance the natural tendency in resources-rich countries to focus on the extractive sector, which is not labor-intensive and prone to corruption. This specific situation conditions the forms of support which development partners of this sub-group of LDCs should provide.

Is there relevant experience for small island development?

52. A trade and investment agenda is useful for most small island States and very small continental countries which are part of the LDC group but has to take into account the special vulnerability of these small economies.¹⁴ They are ecologically fragile, prone to natural disasters, and concentrate their exports on very few goods and often on tourism services. The impact of global warming is, therefore, an overriding concern. For Pacific islands the distance to international markets and transport costs are other distinguishing features. In trade and investment they are highly dependent on the Australian and New Zealand economies and are in need of regulating labor exports to these countries.

¹⁴ Seven Polynesian islands and two African islands (Comoros and Sao Tomé and Príncipe) are LDCs. Djibouti and Guinea-Bissau, two small continental and coastal countries, may be associated to this LDC sub-group because of the small size of their population and their economy. The UN category of Small Island Developing States (SIDS) includes also Haiti but excludes Djibouti.

53. All small island States are heavily exposed to external economic shocks because of the narrow range of production and exports. Yet smallness also may entail special economic opportunities. Several islands have been quite successful in high-end and eco-tourism and Vanuatu, for instance, has become a successful exporter of meat to Australia, New Zealand and Japan. Labor remittances have become an important income for most island economies. Like landlocked LDCs they should explore opportunities to diversify into other services than only tourism, for instance offshore information technology or transport services.

54. It will be essential for island LDCs to study the development policy of successful small island States and small economies. Examples are to be found among Pacific islands, in the Caribbean region and in Africa. Mauritius, for instance, has been quite successful in anticipating a shock to one of its main export sectors, sugar, losing its highly preferential market access to the European Union. Using adaptive economic and trade planning, Mauritius diversified into textiles and clothing and became a financial offshore centre.

D. International community: trade and investment policies

Policy coherence

55. Not all external policies of developed and advanced developing countries are supportive of LDCs. Policies sometimes contradict each other. For instance agricultural trade policies of many OECD-countries limit export possibilities of LDCs while the same donors fund projects to increase agricultural exports of LDCs. This is why today the overall effect of policies in different areas is looked at, for instance in the annual Commitment to Development Index published by the Center on Global Development (Washington DC). The Index measures performance of OECD countries in seven areas: aid, trade, investment, migration, environment, security, and technology.¹⁵ In this note we are particularly interested in aid, trade, investment and technology policies.

Trade and investment policy of industrialized countries

Preferences for market entry

56. Headway has been made in the area of trade preferences: Major industrialized partners have granted duty-free and quota-free (DFQF) preferences to LDCs, in some cases assorted with better adapted (MFN) rules of origin, particularly for textiles and garments. But this process is still incomplete comprising of important exceptions in most countries. The

¹⁵ The 2009 Commitment to Development Index is to be found on the Center for Global Development's website: http://www.cgdev.org/section/initiatives/_active/cdi/

main exceptions which are found in specific OECD countries are: crucial agricultural or processed export items are on an exception list, quotas remain on sensitive products, not all LDCs qualify, programs are limited in time, and rules of origin have a low flexibility that is the origin of inputs used for the exported item is restricted geographically, or the rule on value-added in the exporting country is very demanding.¹⁶ This is a shame since there is evidence that the quality and scope of preferences is crucial for market access and for creating incentives to invest in LDCs. What impact projections for preference regimes also indicate is that the inclusion of other small-market low income countries will not divert significantly local production in the preference-providing country.¹⁷

57. It is to be commended that present negotiating texts in the Doha Round include a commitment of developed countries to provide DFQF preferences to LDCs. This will give an incentive to those countries that are providing time-bound preferences to make these predictable and stable in the future, improving thereby the investment climate in LDCs. Unfortunately, if the minimum threshold of 97 percent of imported goods remains in the Doha negotiating texts and is not increased to 100 percent, this will in many cases hurt exactly those LDC exports which have a high potential for market access.

58. Industrialized countries should expand coverage to all products and all LDCs, and make rules of origin more trade-promoting: be flexible on the value-added rule, allow for inputs into LDC production to come from all developing countries, provide for a regional application of rules of origin (cumulation), and ensure program stability and predictability to encourage foreign direct investment in LDCs. Also similar preferences should be extended to other small-market low-income countries.

North-South trade agreements

59. A new generation of North-South agreements is being negotiated by developing sub-regions and countries and the European Union (Economic Partnership Agreements, EPA). An agreement with the Caribbean States was concluded recently; in Africa only preliminary agreements have been signed, mainly by non-LDC countries while most African LDCs have refused so far to enter into such agreements, mainly because they have a non-reciprocal duty-free and quota-free access to European Union countries. The jury is out on the value of such agreements for LDCs and other low-income countries.

60. Elements should be defined which would make such agreements a useful trade development tool for LDCs, as members of Regional Economic Communities (RECs). This

¹⁶ Elliott, Kimberly A.; *Open Markets for the Poorest Countries, Trade Preferences That Work*; The CGD Working Group on Global Trade Preference Reform, Center for Global Development, March 2010.

¹⁷ Bouët Antoine, David L. Debuquet, Elisa Dienesch, and Kimberly Elliot; *the costs and benefits of Duty-Free, Quota-Free Market Access for Poor Countries: Who and What Matters*; Working Paper 206, Center for Global Development, March 2010.

would offer a model for other developed countries than EU members to enter into agreements with developing sub-regions. Other experiences have been made recently with North-South agreements on all continents which could also be of interest to LDCs.

61. Elements to explore in North-South negotiations would be to:

- Provide room for less than reciprocity in tariff reductions by lowering import tariffs of REC members gradually over a long period but making these reductions dependent on a previously established common external tariff of the REC concerned.
- Define special and differential treatment needs of LDCs inside of RECs (which always have non-LDC members too), and reflect these special conditions in the North-South agreement.
- Include flexible and investment-enhancing rules of origin as discussed above in the context of duty-free and quota-free preferences.
- Establish effective safeguards for tariff reductions and services' commitments.
- Cover commitments for services with less than reciprocity using positive lists and a gradual increase of commitments over time, taking into account a previously established preferential market for services in the REC concerned.
- Reflect the good investment practice described in this document in the services' imports which are tied to investment. This concerns mainly economic infrastructure.
- Negotiate ambitious concessions and cooperative monitoring mechanisms for Mode 4 service exports of LDCs (labor services in the developed partner country) using for instance the Jamaica model.
- Deal with the most important technical barriers for LDCs in the developed partner countries, particularly technical regulations and standards, by negotiating a practical certification and conformity assessment process (where such a process is presently too cumbersome and comprises of protectionist features) combining it with technical assistance to establish certification capacities and help exporting enterprises in LDCs to cope with standards.
- Through the agreement, start a process of defining private eco-social standards and labels which would be useful for market access of LDC enterprises, make them official and provide preferential market access to them, treating them as "unlike goods" in WTO parlance. This would be an excellent way to create incentives for environmentally-sound production and for social management of enterprises in accordance with international labor norms.
- More generally, tie-in aid for trade funding programs to help LDCs with the trade and investment agenda described earlier. Of particular importance will be to develop negotiating skills and trade analysis, prepare sector strategies – for instance to promote services, process agricultural goods and diversify into other labor-intensive manufacturing – and develop modern trade institutions.

Finish quickly the Doha Round

62. With all its limitations, the Doha Round, as it stands, is in the interest of developing countries and LDCs and should therefore be concluded quickly. If an early conclusion is not feasible, then it will be essential to firm up immediately an agreement (an “early harvest”) which combines the uncontested results of negotiations which are in the interest of LDCs as, for instance, the commitment by developed and advanced developing countries for duty-free and quota-free access of LDC exports, the agreement on trade facilitation, and a more than proportional reduction of cotton subsidies in developed countries.

A new type of North-South Investment Agreement

63. Home and host countries of investors have concluded almost three thousand investment protection agreements over the past fifty years. The goal of these agreements has been to protect investors from nationalization of assets, unfair treatment and other forms of discrimination. Developing countries and LDCs typically conclude such agreements in the hope of attracting foreign investment. However, recent studies confirm that there is not much evidence that such agreements have been an important factor in promoting investment in host countries. Moreover, since the late 1990s investors have begun using the dispute settlement mechanisms under these treaties, which usually give them the right to sue states directly before international tribunals. The development of such legal action came as a surprise to many developing States who have to resort to expensive law firms for their defense.

64. Over time, some of these agreements have become more ambitious, and cover both the establishment phase as well as the operation of the enterprise after the investment. They are increasingly included in trade agreements, including in regional agreements, such as NAFTA, the first of its kind to include an investment chapter.

65. It is time that investment agreements be remodeled to become a development tool rather than an obstacle, particularly in LDCs. Besides a legitimate protection of investors this would imply that they give support to a screening mechanism for important investments to ensure that investment projects follow sound practice and take into account also the interests of other stakeholders than the invested enterprise. Such agreements could in fact give official support to voluntary guidelines for investors (and host governments in the case of EITI) and make them compulsory (paragraphs 31, 33 to 36). The dispute settlement modalities also have to become more transparent, predictable and independent.

66. In 2005, the International Institute for Sustainable Development (IISD) developed a Model International Agreement, the first substantial effort to review the nature and purpose of international investment agreements since the current model was developed fifty years ago. IISD's Model Agreement establishes a clear purpose for the agreement: to foster international investment that is supportive of sustainable development aspirations and requirements in both the North and South. The agreement develops provisions that balance the rights and obligations of investors, host states and home states; and sets out specific proposals to fix the broken investor-state arbitration system.¹⁸ But the impetus for better agreements is only possible if the officials negotiating international investment agreements understand the implications of the language they negotiate. In response to this need, IISD has initiated a program that offers advisory legal services to developing countries based on their specific needs and circumstances, free of cost.

Trade and investment policy of emerging market partner countries

Trade imbalance makes better access of LDCs imperative¹⁹

67. LDC export share in South-South trade has increased from 1.7% in 2001 to 2.4% in 2007. Markets of developing countries represent today 50% of LDC exports; these comprise mainly of fuel and minerals. China has become the biggest importer of LDC products (23% against 21% of the EU in 2008) but India's and Thailand's imports have also become sizable. Although the developed countries' import share has decreased over time, they absorb 75% of LDCs' manufactured goods. Average tariffs of agricultural goods faced by LDCs in developing countries were 12% in 2006, agricultural exports were subject to far higher rates than non-agricultural goods.

68. Some advanced developing countries (Brazil, China, India) have started to buy into tariff-free preferences for LDCs but make greater exceptions than industrialized countries: coverage of tariff lines ranges from 80 to 95 percent although Brazil plans to move to 100 percent soon. China extends preferences to African LDCs only; for other LDCs ad hoc arrangements are followed. The potential gain for LDCs from moving to 100% coverage in duty-free and quota-free tariffs is much greater in emerging economies (and particularly India) than in developed country markets.²⁰ LDCs might also find it easier to have market

¹⁸ Available at : <http://www.iisd.org/investment/model/>

¹⁹ Data used in this paragraph are taken from the UNCTAD 2010 report, referenced in footnote 1, pp.12/13.

²⁰ See Laborde, David: *Looking for a meaningful Duty Free Quota Free Access Initiative in the Doha Development Agenda*, Issue paper No. 4, ICTSD, December 2008. see <http://ictsd.org/downloads/2009/01/labrodeweb.pdf>. These gains tend to offset preference erosion concerns associated with MFN liberalization and would allow several LDCs to move from being net losers to being net winners in the DDA.

access in emerging market economies because SPS and TBT measures tend to be less difficult to comply with than in OECD countries.²¹

Emerging market investments in LDCs should be sustainable

69. The same considerations on investment quality and transparency, which were mentioned for investment policies of developed countries and transnational enterprises (paragraphs 65, 66) are valid in the case of advanced developing countries. As many of the sizable investments, particularly in the primary sector and in infrastructure, are the responsibility of public enterprises and agencies of these countries, the accountability of governments is at stake. This means that intergovernmental investment treaties and host State-investor agreements should be concluded which comprise of transparent modalities for dispute settlement as well as screening mechanisms for investment ensuring its sustainability and endorsing voluntary guidelines.

Recommendations

70. Similar recommendations as in the case of developed countries are justified by the fact that East-South trade is highly imbalanced and includes significant tariffs for LDCs. LDCs would find easier access in emerging market economies than in developed countries, if they were to benefit from full preferences. Also, the weight of investments in LDCs of advanced developing countries has become considerable and the quality of these investments is therefore critical for LDC development. Governments of advanced developing countries should therefore:

- complete the reform of import preferences by going gradually to 100 percent of tariff lines, abolishing quotas (if there are any) and including flexible rules of origin;
- conclude trade agreements that are balanced in the sense that they comprise of significant provisions for LDCs to improve trade competitiveness and have better access to markets of advanced developing countries, considering also new sectors and non-trade barriers;
- explore agreements between regional economic communities;
- conclude investment treaties and host-State investor agreements that ensure sustainable investment and transparent dispute settlement.

²¹ This is not true at least in the case of India which is very restrictive for TBT and SPS import standards.

E. Development cooperation

LDC governments and external cooperation should focus on production and exports

71. As mentioned earlier, the time has come to give priority in LDCs to trade competitiveness and economic diversification. A development agenda with six areas of reform has been presented (paragraph 27). Government and cooperation agencies should focus more decisively on these reforms. To lead to sustainable and poverty-focused development, growth pursued must be of high quality: labor-intensive diversification should be privileged; SMEs and micro-enterprises should get particular attention; land rights, infrastructure and technical support to smallholding farmers and their associations should be strengthened; business services for agriculture, manufacturing and exports should be organized; and land-locked countries in particular should specialize in exporting modern services and become transport and communication hubs for their neighbors.

72. LDC governments have other important development tasks: revenues from oil and mining should flow not only into modern infrastructure but also into education, technical training, and capacity-building to adapt technologies in all sectors. For that to happen, the national tax base has to become broader, and tax administration has to become more transparent and efficient, using information technology.

Aid: geographical scope and effectiveness

73. Aid requirements for these reforms are considerable. Only a limited number of LDCs have been able to obtain adequate support so far to pursue this new agenda. And additional demands will have to be addressed on the account of climate mitigation and adaptation in order to reach climate-resilient development.

74. To be able to use external aid efficiently and effectively will require an enhanced effort by the donor community to help each LDC in planning and implementing such a strategy. The Enhanced Integrated Framework is a good framework for aid alignment and harmonization to the extent that it becomes operational and down-to-earth in LDCs. This is not yet the case today.²² For instance, most bilateral donors in Africa have chosen only a few partners, and often these are the same for many donors. Multilateral agencies like the World Bank and the African Development Bank are able to give some counterweight to this aid concentration but are limited themselves by tight resource constraints in their field presence in a number of LDCs. Strong technical representation in LDCs by donors is a must for an

²² See the excellent report by the Geneva Director of CUTS: Kaushik Atul, *Reassessing Scope and Mandate of the Enhanced Integrated Framework*, GTZ, 24 January 2010. The views expressed here, particularly in the next paragraph, also correspond to the author's own observations made on visits in October 2009 to two EIF countries, Ethiopia and Tanzania.

enhanced dialogue which will lead to effective assistance. *Both bilateral and multilateral cooperation agencies should ensure that aid for export expansion and diversification is not concentrated only in a small number of LDCs.*

75. The Enhanced Integrated Framework itself should have a key role in trade competitiveness and diversification strategies in LDCs. It has taken quite some time for LDCs to set up international trade sector priorities and institutional arrangements to implement action plans. In many LDCs strengthened investment, reforms in trade, and private sector development are still in the starting blocks. This hesitation has good reasons and should not be by-passed by donors. But non-controversial reforms, capacity-building and trade infrastructure should make progress even if ideal institutional arrangements have not been sorted out yet. *Donors and LDC stakeholders have a shared responsibility to make the Enhanced Integrated Framework work and accelerate its implementation. They should jointly report on progress and difficulties annually, country by country.*

76. Support to this agenda requires expertise and presence in LDCs of cooperation agencies which often go beyond their resources and skills. For instance there are very few agency experts familiar with trade and investment policy and negotiations. The same is true for major technical areas of capacity-building like trade facilitation and technical standards. Sometimes “coherence” is also at stake in the sense that specialists familiar with investment or trade policy and treaties are not sufficiently familiar with LDC priorities and constraints espousing positions and interests of their countries of origin, often without realizing it.

77. Bilateral agencies should make an effort to train and upgrade their staff to become familiar with trade and investment policies of developing countries and particularly LDCs. Even if projects are delegated to multilateral agencies, expert groups or technical NGOs with a global scope or resident in developing countries, such technical expertise will be of essence to monitor the performance of the agency to which capacity-building was delegated. Donor staff should have direct and frequent contacts with policy makers, experts and project owners in LDCs and be recruited increasingly in the host countries. *They should be present in LDC partner countries with staff that is well versed in trade, investment and private sector support.*

78. Finally, to keep aid effective, it does not only have to be monitored but, from time to time also evaluated by independent experts. Evaluation is an essential tool but it serves only its purpose if institutions learn from it by heeding its recommendations. Not many cooperation agencies have established reliable feed-back into the new programs they finance. The Enhanced Integrated Framework could serve as a coordinating instance to organize multi-donor evaluations and share the results.

79. Monitoring and evaluation of the effectiveness of aid for trade should be given more importance both by cooperation agencies and by LDC Governments. LDC Governments should start establishing small groups of autonomous evaluators familiar with evaluation methodologies since they cannot afford not to learn from mistakes. Particular care has to be taken to ensure a rigorous feed-back of the track record into new operations, a function which the Enhanced Integrated Framework could coordinate.

Examples of initiatives in investment and trade cooperation

80. ***Regional cooperation and integration.*** The most important task now is to take stock of the trends and develop policy prescriptions. This is best done in common with LDC researchers and policy makers in a combination of research studies and dissemination workshops. Based on this analysis cooperation agencies should give support to LDCs in their regional integration policies: What are the lessons of South-South integration where often LDCs are members of regional integration treaties together with non-LDC developing countries. Is the special and differential treatment of LDCs working to their benefit (e.g. in ASEAN, South Asia, SACU/South Africa)? What is the best sequence of operational steps to create a preferential/free trade zone, remove technical obstacles to trade and, eventually, reach a customs and monetary union? For example should technical trade institutions in the member countries be harmonized first (like single electronic windows in ASEAN) or priority be given to tariff reduction or elimination together with community rules of origin?

81. Regional economic communities are just one option of integration which runs parallel to regional partnerships around a single common cause. An essential area of cooperation, which can rely on ad hoc arrangements, is economic infrastructure that is electricity transmission, gas pipelines, telecommunications development and transport infrastructure. This is another essential enabling factor in a production and export diversification strategy.

82. ***Aid should enhance investment initiatives by LDCs.*** We mentioned the need for better investment policies. Diversification requires strong investment by the domestic private and public sectors as well as by foreign companies. Tools have to be found which enable higher investment and technology absorption as well as a sustainable choice and management of investment with high benefits to the society as a whole.

83. An innovative, high-risk venture which is used to foment local initiatives as well as involve external mainly Chinese investors is the China-Africa Development Fund.²³ This is a USD 1 billion equity fund (to be extended to USD 5 billion over time) which is considered a major building block of China's strategic partnership with Africa. The Fund usually takes minority shares in medium and big enterprises in all productive sectors and infrastructure, associating either Chinese enterprises or other local and international partners. Investments go from USD 5 to 50 million for each project. By October 2010, the USD 1 billion was almost entirely committed in about thirty projects in twenty African countries. Two typical uses of funds in agri-business are cotton planting and processing in Zambia, Malawi and Mozambique (involving about 100'000 farmers) and a leather processing project in Ethiopia.

84. Such investments are in some cases in stark contrast with the effect of cheap Asian exports, for instance of textiles, which have displaced earlier investments made by Asian and Chinese investors in Africa. Over many years, Chinese exports have led to the closure of manufacturing of current consumer goods in Africa. In Nigeria, for instance, the closing of local textile firms owing to Chinese imports has allegedly led to hundreds of thousands of lost jobs.²⁴ It is unclear how much the trade flow from China and other Asian countries actually limits the present industrializing attempts in African LDCs.

85. Investment enabling tools and donor support to investment concern the following:

- An investment promotion agency should be created or reformed - if already in place but not working in an efficient partnership with the private sector - learning from the experience of countries which have been relatively successful in their promotion efforts (e.g. Ghana, Mauritius); it should not only act as a one-stop shop for foreign investors but also find technical or marketing partners for domestic investors.
- Investment regulation and incentives for backbone and business services – energy, telecommunications including broadband internet access and mobile phone services, transport infrastructure, finance, IT and other services to enterprises – have to be given special attention; regulation has to create a level playing field and rule out monopolies.
- Innovative financial instruments are needed for domestic SMEs: equity financing, guarantees, green credit often combined with technical assistance to enterprise management,²⁵

²³ Powerpoint presentation by Liliang Teng, Chief Representative in South Africa of the China Africa Development Fund, ICTSD/Finland Dialogue on emerging issues on trade-related development assistance, Geneva, 20/21 October 2010.

²⁴ Tom Burgis, *Generation of industrialists makes way for a new wave*, in Financial Times, June 14, 2010, Africa-China Trade Special Report, page 2.

²⁵ A recent review of innovative financing schemes in Africa is to be found in: *Innovative financing for sustainable small and medium enterprises in Africa*, International Workshop Geneva Switzerland, 2007 Meeting Report. The event was organized by UNEP, WWF, Geneva International Academic Network and the University of Geneva.

- Financial and technical support should be provided, if needed, to design or manage voluntary, best-practice investment codes as the ones mentioned earlier in the text (paragraphs 29 to 32) ;
- Donor agencies should lobby and advise their own governments in the design, negotiations and management of trade and investment codes and (bilateral or multilateral) agreements, involving LDCs, preventing corruption, money-laundering and tax evasion;
- Donor agencies should assist the technical secretariats and public-private partnerships in LDCs involved in the planning and management of trade and private sector projects and reforms; effective management of investment and project pipelines is crucial for development and is a difficult task to master.

86. ***A science and technology culture to facilitate technology transfer.*** Academic and vocational training as well as technological adaptive research should be attended to and reinforced in close cooperation with private enterprise; an essential element in that context is literacy in information technology and therefore a broad access to affordable services to as many people as possible. In earlier decades, basic education and literacy had precedence in aid because illiteracy in many LDCs was high and formal basic education was poor. Yet a sea change has happened in the last fifty years. Now LDCs should build on that success in basic education, continue to make progress to reach full literacy and improve the quality of basic education. But then they should also set a new priority: strengthen and enlarge the capacity for teaching vocational and technical training, establish natural-science, engineering and business administration in universities, and create adaptive research centers in the main production sectors.

87. The next step will be to introduce production technologies and find innovative business management methods which marry good international practice and the prevailing conditions in the LDC. Most technologies and business methods to be used in the economic diversification process are already used elsewhere, including in the same region. So research is mainly adaptive and one of the main hurdles for fast technological change is that the presence of modern production units does not by itself ensure that these technologies are adopted by other enterprises. New production technologies and methods will not only have to be introduced (for instance through direct investment) but also disseminated in the country.

88. **The following more specific suggestions are:**

- Science, technology and innovation should become a chapter of poverty reduction strategies and trade sector studies (like DTIS). Each LDC should, in fact, establish an innovation and technology report, with support from experts of developing and industrialized countries, in which a practical action plan is defined.
- As part of such an innovation and technology report, LDCs should explore and build-up capacity in intellectual property rights focusing on those rights which correspond to the country's present interests, as for instance the use of traditional knowledge and plant resources, geographical indications and artistic production. They should also explore the sources of publicly available information on technological innovation and research and development which might prove important for local enterprises.
- Research institutes and university faculties linked to agriculture, manufacturing and modern services should be established or strengthened. Thought should be given to establishing partnerships with academic and research institutions in other countries which have successfully diversified in the areas in which the LDC is acquiring a comparative advantage.
- Thought should be given to locate research and technology centers as well as technical universities at the regional level. This is particularly opportune if the LDC is small and belongs to a regional economic community.
- Technical and vocational training should be upgraded. The country's private and public enterprises as well as its academic institutions should be closely associated to curriculum development, teaching and practical work periods (apprenticeship system).
- Telecommunications and information technology infrastructure should be upgraded to make internet tools accessible everywhere in the country. Such a program requires regional cooperation and, probably, support from international public or private cooperation.
- More efficient and broadly available IT services will make it possible to launch a national IT literacy campaign, give incentives for the creation of enterprises providing IT services, attract IT service providers from other countries, and introduce computers in schools as a pedagogical tool.
- Local entrepreneurs should be given support through science and technology grants to support innovation and development of new industry.

89. ***Agricultural exports and food security.*** We have mentioned earlier, in paragraph 30, the need for guidelines for external agricultural investment to ensure its contribution to food security. "Nearly half of the least-developed countries are considered by FAO as experiencing a food crisis requiring external assistance or being at risk of crisis due to high

commodity prices, which are likely to remain higher and more volatile than in the past decade.”²⁶ The impact of global warming and the production of bio-fuels might exacerbate these problems.

90. Aid agencies have to focus much more than in the past on giving support to LDC agriculture. Particularly African LDCs have to invest in technologies and irrigation to use the sizable untapped potential and produce higher yields, following the lead of other developing countries.²⁷ The agenda includes traditional agricultural commodities as well as fruits and vegetables. Higher production and exports, particularly to neighbors and the region, are essential for small countries as food security will improve if it is organized at the regional level.²⁸ Agricultural research should also be considered a cooperative undertaking of the region. Therefore, agricultural technology, trade and infrastructure should become an important concern for regional economic communities.

91. Below is an example of a trade-related agricultural project:²⁹

Growing Mali’s Mango Exports

Mali exported small quantities of mangoes by airfreight, mainly to France, since the 1970s. A decisive change came about in the year 2000, when Mali’s export promotion agency, in partnership with an Ivorian firm, was able to successfully export by sea from Abidjan. Malian trade authorities, in consultation with professionals and local export promotion agencies, defined strict quality, calibration and conditioning norms for mango exports in 2005. A “Mango Task Force” was established that included the three producers’ associations for fruits and vegetables, export intermediaries and public export promotion and competitiveness units. The Netherlands, the World Bank and USAID made available funding to establish and manage a pack house including cold storage, calibration, and quality control, and located close to Bamako airport (PLAZA). It opened in 2008. ITC contributed by training Malian exporters in marketing and having them participate several times in a major European fair. The joint effort of Malian producers and their associations, the Malian promotion agency, private transport and shipping firms and several cooperation agencies have so far resulted in a major increase of mango exports, from 2915 tons in 2005 (only to France) to 12677 tons to eight export markets in 2008.

²⁶ Issues notes for the sessions, Brainstorming meeting on the substantive preparation for UNLDC IV, July 14 to 16, 2010, UN-OHRLLS, page 5.

²⁷ A recent study by the International Food Policy Research Institute (IFPRI) evaluates the potential of irrigation in African countries. Presently only 6% of cultivable land is irrigated. Potentially, irrigation could boost agricultural productivities by at least 50 percent. You Liangzhi and Ringler Claudia eds., *What is the irrigation potential for Africa?* IFPRI 2010.

²⁸ Pannhausen Christoph and Untied Bianca, *Regional Agricultural Trade for Economic Development and Food Security in Sub-Saharan Africa*, GTZ, January 2010.

²⁹ Main source: *Growing Mali’s Mango Exports: Linking Farmers to Markets through Innovations in the Value Chain*, World Bank, February 2010.

The volumes decreased in 2009 to 10000 tons but the 2010 season has been buoyant again. Now attempts are made to diversify exports into dried mangoes, mango jam and juice. The pack house PLAZA will be used also for the export of French beans, melon and pawpaw, as the mango season lasts only five months. It is now owned by the three producers' associations and managed by a private firm.

92. **Processing of commodities.** Now that duty-free and quota-free access has become likely in the industrialized world and in emerging market economies, tariff escalation should not be a hindering factor anymore to exporting processed agricultural commodities like roasted coffee beans, milk powder, fruit concentrates and cocoa butter, and those based on oil seeds or containing a lot of sugar. Also, countries like Malaysia show the way how innovative derivative products with a high value added can be produced and exported using commodities as raw material.

93. Concrete proposals are to engage in research and development and market research of commodity-based products for instance through partnerships of research institutes and universities, provide credit and technical assistance to build up domestic processing capacity, encourage direct investments by international food retailers, and promote equity investments of domestic enterprises.

94. **Modern services.** For the first time some attention has been paid recently by international institutions, and particularly the World Bank, to the essential role of other services than tourism in diversifying production of low-income developing countries. A lot could be done through domestic studies and regulatory reform, as well as through external cooperation and investment: LDCs should develop service strategies (both on the export and import side) to get services on their development map. They should then implement the action and reform program which has to be the tangible result of the strategy. They should then also negotiate conditions for trade in services in trade and investment agreements taking into account the country's interest and priorities. Good examples of ongoing work in services in Africa are the countries of the East African Community, Zambia and Mozambique.

95. Particular attention should be paid to the development (and export in some cases) of more efficient backbone services (energy, transport, telecommunications, including broadband internet access). Business services are required which support SMEs and exporters and trade in financial services should be promoted. Finally, the development of information technology services could be feasible in some LDCs, leading among others to out-sourcing contracts from domestic, regional and global enterprises.

96. **Trade facilitation.** It is uncontested today that a combination of thorough reform of Customs and other border agencies, more efficient trade logistics services and regulation,

and improved infrastructure have a good potential to lower export and import costs (often more than reducing tariffs). The positive impact on land-locked LDCs is greater, if efficient trade corridors to ports are organized. Important initiatives are undertaken today concerning LDCs: Laos and Vietnam have opened a new corridor to Da Nang port, projects for a North-South transport corridor in Africa have been launched and a trade facilitation agreement has been negotiated at WTO. If concluded, the agreement will create aid partnerships for Customs' reform. This will help LDCs to reach the performance standards of the agreement. A Trade Facilitation Facility was created at the World Bank (with support from several bilateral cooperation agencies) to work predominantly with low-income countries on trade facilitation reform. These opportunities have now to be seized.

97. An example of a successful reform in a low-income African country is described below.³⁰

Modernizing Customs in Ghana

In Ghana, a single electronic window was established to manage border passage of goods (imports, exports and transit). It started in 2000 and took about three years to become operational at an investment cost of USD 6 million. To initiate and implement the reform, a Joint Venture Company was formed that obtained a ten year mandate to operate Customs, using Customs' staff. Ghana Customs has a 20 % share. The total public share is 35% (including two other public shareholders), while two private shareholders hold 65% of the shares. The main private shareholder and technical partner of the venture is SGS, a Geneva-based inspection company. It holds a 60% share. Operation of the system as well as dividends to shareholders are paid through a 0.4% FOB price levy on imports (all other transactions are free of charge). Ghana took over a software (Tradenet) that was first used in Singapore and then in Mauritius. Since 2003 government revenues from Customs' tariffs and other border charges have increased annually between 20% and 40 %, passage times at the main border points are now mostly below one day compared to about 5 days before. The company serves as a model for other e-government ventures in Ghana and as export to other countries in the region. The two ports in Ghana have become main entry points to the West African region serving several Sahel countries.

98. **Lowering business costs by improving business procedures and management.** In the last years, cooperation agencies have increased their support to the business sector in low-income countries. One vector has been the complexity of business procedures, that is the time required (and implicit costs) of establishing enterprises, and of authorities intervening in their management, transactions (including trade facilitation) and bankruptcy procedures. IFC spearheaded this effort by ranking each country and reporting on annual changes in "Doing Business Reports".

³⁰ Source: *The Private Sector and Aid for Trade, a report*, ITC/ICTSD dialogue, Montreux 3-5 June 2007, ITC 2007.

99. There are many ways to reduce business costs, some are in the hands of enterprises themselves, for example when they reduce or eliminate intermediation costs:

This has happened for instance with fair trade coffee producers in Central America some of which now negotiate direct contracts with retailers in industrialized countries doubling their share in the final price. ITC has helped G-4 cotton producers to export directly to China lowering transaction costs significantly. Such examples should be followed by LDCs in their exports to developing countries.

F. The international and domestic private sector

There is no reason for the foreign investment boom in LDCs to fizzle out

100. We saw in Section B of this note that developed countries remained the main source of FDI in LDCs in the last ten years but that the field has increased not only to some emerging market countries such as China, India, Malaysia, South Africa and Russia but to many others including intra-regional investment. Besides big public investment in oil, gas and mining many private investors from developing countries have started to invest in LDCs. We expect these investment trends to continue, after reduced levels of investment during the recent international crisis. This implies that LDC governments have to gear up to engage responsibly and efficiently with investors, be they foreign or domestic.

Contracts between host states and investors

101. We referred in Section C to the opportunities and risks of extractive and agricultural investments. Similar risks are present in investments in economic infrastructure. It will be essential for foreign investors and financiers in all sectors to follow sound investment criteria which have been laid down in voluntary investment codes or are emerging. The best course for the future will be for LDCs to lay down the criteria which they will use in screening foreign investment and make them public so that investors know the rules.

102. Not only treaties between States are important to help LDCs to ensure sustainable investment, contracts between host states and investors are too, particularly when investments have a considerable impact on the domestic economy and the environment. This is the case for investments in the oil and minerals' sector. In April 2009, the Mining Law Committee of the International Bar Association (IBA) took the initiative to develop a model mining development agreement (MMDA) to serve as a negotiation template for investor-state agreements in the mining sector in developing countries. It is based on international best practice in this field. The IBA proposes a model contract which should lead to sustainable development in mining through effective community participation.³¹

103. Today it is essential for mining companies to obtain the support and goodwill of mining and near mining communities for mining projects which have an impact on such communities. Generally, this is done by companies initiating projects which improve the lives of such communities and which enable communities to benefit directly from mining operations. At the same time, mining companies require certainty in terms of the legal regime governing their mining operations and stable investment conditions under which to operate in order to ensure the long-term security of their investments.

FDI has to be beneficial for LDC stakeholders and has to draw in local investors

104. The four general points presented in paragraph 35 are summarized here: investments have to be profitable for local stakeholders also (workers, suppliers, service providers, government), local producers and investors should be associated as much as feasible through joint ventures or supplies and services; the investment has to be environmentally and socially sound; and, in the case of sizable and intrusive investments, local communities have to be consulted.

Domestic investment is essential, independently from FDI

105. In many cases investment grows out of domestic trading activities, SMEs and microenterprises be it in agriculture, manufacturing or services. As we mentioned earlier, governments have to create a level playing field for these new entrepreneurs and strengthen the local business culture through good training opportunities.

Remittances for investment of the diasporas

106. Remittances are often transferred through costly informal channels. Even when they pass through formal financial intermediaries, their purpose is often to complement family income for consumption. Part of remittances flows into construction, trading working capital and small investments. At the other end of the spectrum some long-term emigrants invest in

³¹ <http://www.ibanet.org/Article/Detail.aspx?ArticleUid=41f1038e-dcbf-44fd-ad17-898b7aa04a1a>

their country of origin. An example are US investors of Ethiopian origin building textile firms in Ethiopia.

107. Our interest goes to the group in-between: Emigrates which would like to invest in their country of origin but not as direct investors. In order to invest and not run into red tape or costly payments of intermediaries (incurring sometimes a risk of fraud) they have to be able to rely on sound investment vehicles (investment companies or operational entrepreneurial NGOs) which then are willing to submit projects, report on investments transparently and fully, and know how to cope with domestic administrative rules. Do such investment vehicles exist? Or should cooperation agencies intervene in helping to design such vehicles and finding investment companies willing to deal with such investments? The intermediaries might be publicly owned companies or foreign equity investors (like the Chinese investors we mentioned in paragraph 83) given the high first mover risk involved.

Two examples of international partnerships

108. Both are examples of private initiatives. The first one has been exclusively organized by private partners on both sides:

An integrated textile production chain: the COOP experience³²

Since 1991, REMEI AG, a small Swiss textile trading firm, has built up an integrated chain of textile production forming alliances with cotton farmers in India and Tanzania, using a network of firms for spinning and processing in many countries but predominantly in India and Eastern Europe, and selling, today, 8400 articles through the Swiss retail chain Coop (“Naturaline”), representing a CHF 57 million turnover in 2006. Similar retail partnerships have been developed since 2002 with Monoprix, France, and Coop, Italy. An eco-social label, “ bioRe®” is used for all products and is independently monitored. Biological cotton is used and farmers are remunerated, in cash and in kind (training, social community projects) between 20% and 40 % above local market prices. Part of the farmers are also shareholders in the Indian bioRe® company. Spinning and manufacturing follows ecologically-friendly methods (e.g. non-chlorine bleaching, no use of formaldehyde, dyestuff use following high environmental standards, adequate waste water treatment) and respects international labor rights (SA 8000 criteria).

109. This second transnational enterprise initiative would be built on a triangular partnership:

³² Source : *The Private Sector and Aid for Trade, a report*, ITC/iCTSD dialogue, Montreux 3-5 June 2007, ITC 2007.

An initiative of international retailers³³

International food retailers envisage to guarantee the buying of food products in the future from developing countries following investments in projects and capacity-building of smallholders with the participation of specialized technical agencies. Such triangular projects might be interesting for LDCs provided that they contribute to satisfying local and regional markets needs in the first place, reaching higher productivity in farming and improving the organization of smallholder producers, that is following the principles laid out on page 8. Similar initiatives have been undertaken by eighty European retail firms using a social standard as basis for labeled food products sold in their stores (BSCI) and helping the suppliers to conform to these standards. As far as we know, this standard have been used mainly with plantation farmers including outsourcing schemes.

³³ Source : Discussions of the author with a leading Swiss retailer.