Nepal Graduates from LDC : An Explorative Impact Assessment

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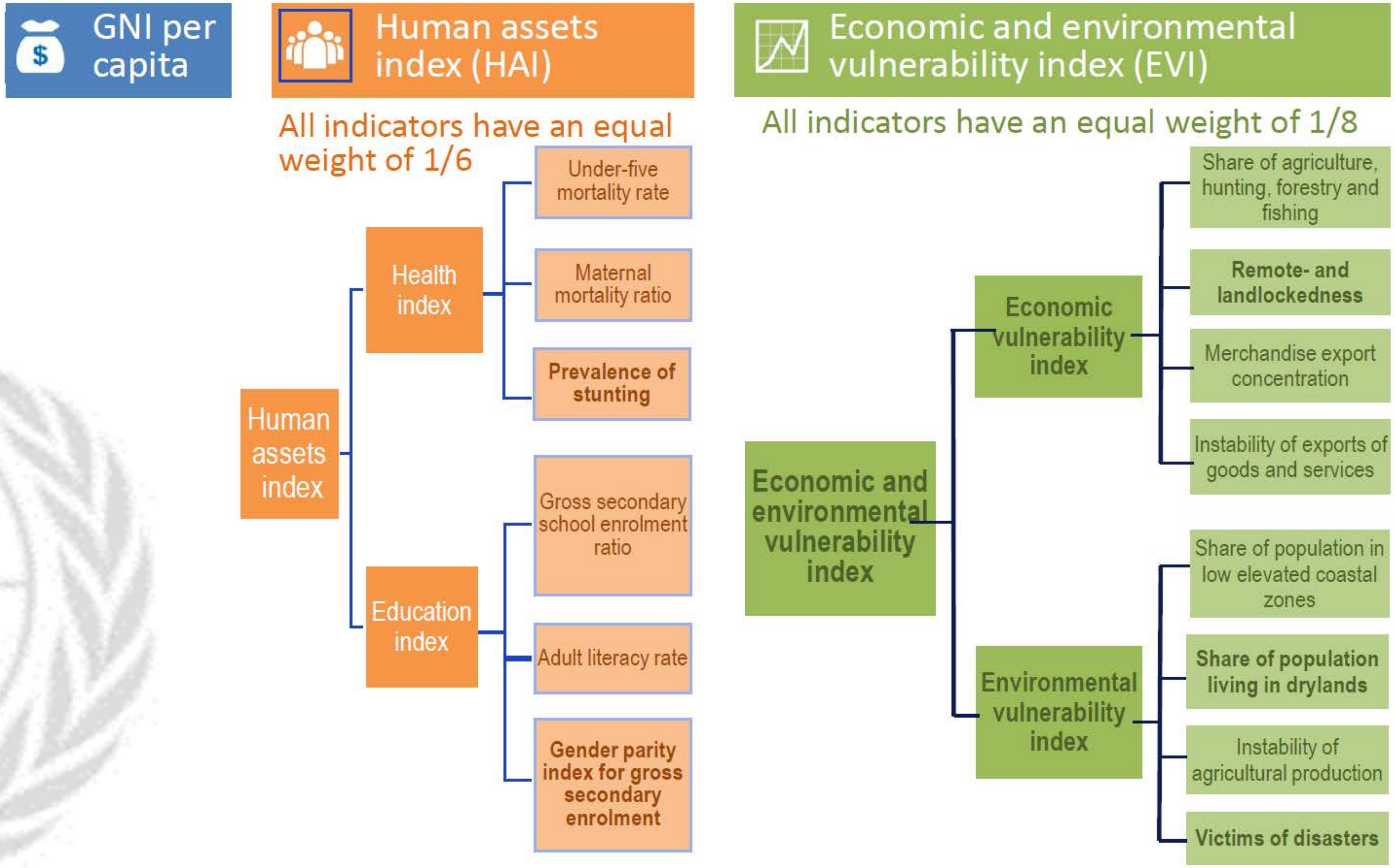
Presentation structure

- Brief introduction of LDC category
- International Support Measures (ISMs) for LDCs
- Impact of graduation
- Moving forward

Background: creation of LDC category

- Least developed country (LDC) category was established by the United Nations General Assembly in 1971 as a group of ***low-income countries*** with ***structural handicaps*** that hamper their development and growth,
- Nepal along with other 24 low-income countries were identified as LDCs at the time of its inception,
- Currently, there are 46 LDCs;
- So far, six countries- Botswana, Cabo Verde, Equatorial Guinea; Maldives, Samoa and Vanuatu- graduated from LDC;
- International community recognized that LDCs need special support to overcome development obstacles.

Background : LDC Criteria



Background: LDC Inclusion and Graduation Criteria

Indicators	2021 Triennial Review	
	Inclusion	Graduation
Per capita GNP (US$)	1018	1222
Human Assets Index (HAI)	<60	>66
Economic Vulnerability Index (EVI)	>36	<32

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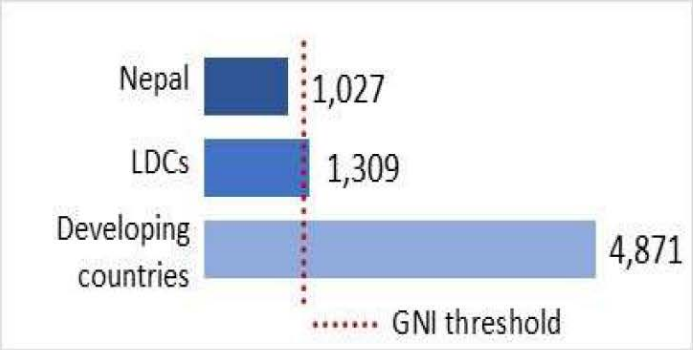
Where does Nepal stand?

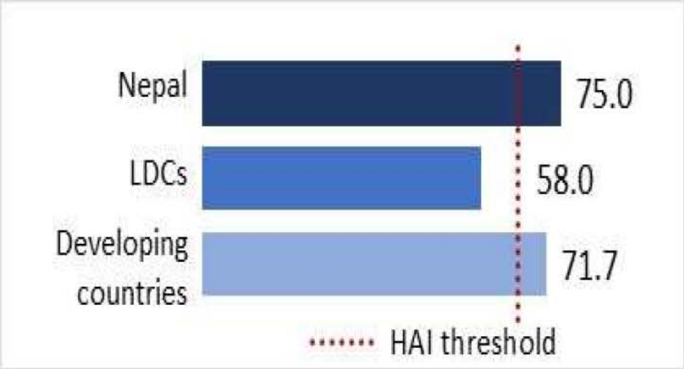
GNI

Graduation Threshold: $1,222
Nepal: US$1,027



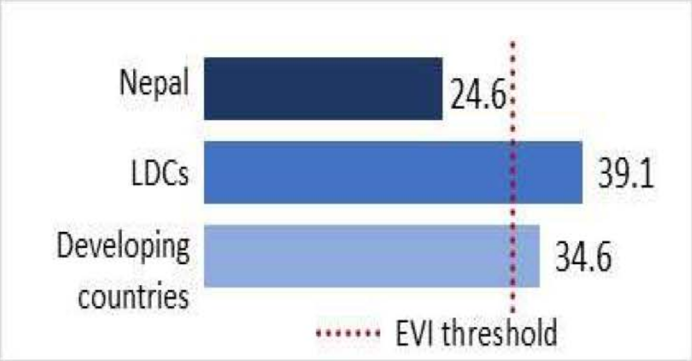
HAI

Graduation threshold: 66.0
Nepal: 75.0



EVI

Graduation threshold: 32.0
Nepal: 24.6



Nepal as a LDC country

- Nepal met LDC graduation thresholds- HAI and EVI- for the first time in 2015;
- Nepal also met graduation thresholds in 2018, becoming eligible for graduation;
- However, Nepal requested CDP to defer its recommendation for graduation citing impacts of 2015 earthquake, border blockade, low per capita income and high dependence on remittances and thereby sustainability of development gains ;
- CDP deferred its decision to recommend Nepal for graduation until its 2021 triennial review;
- CDP recommends for graduation in its 2021 triennial meeting, but with 5 years preparatory time.

International Supports Measures (ISMs) for LDCs: Brief Introduction

- ✓Trade –related support measures
  - ✓Preferential market access for goods
  - ✓Preferential treatment for service and service suppliers
  - ✓Special treatment regarding obligations and flexibilities under WTO rules
- ✓Development cooperation
- ✓Exclusive mechanism for LDCs

Special and Differential Treatment Provisions in the WTO

Types	Numbers
Provisions aimed at increasing the trade opportunities	12
Provisions that require WTO Members to safeguard the interest of developing Countries	45
Flexibility of commitments, of action and use of policy instruments	40
Transitional time period	20
Technical assistance	17
Total	**134**
Provisions relating to LDCs	**14**

Preferential Market Access for Goods (1)

Market	Duty free tariff line coverage and major exclusions
Australia	100 percent duty-free, quota-free entry (DFQF)
Canada	98.6 percent DFQF (Exclusion: dairy and other animal products, meat, meat preparation, cereal products)
Chile	99.5 percent DFQF (Exclusion: cereals, sugar, milling products)
China	96.6 percent DFQF (Exclusion: chemicals, transport vehicles, machinery and mechanical appliances, electrical machinery, paper)
European Union	99.8 percent DFQF (Exclusion: arms and ammunition)
Iceland	91.8 percent DFQF (Exclusion: meat, food preparation, vegetables, dairy and other animal products, plants and trees)
India	95.1 percent DFQF (Exclusion: plastics, coffee and tea, alcoholic beverages, tobacco, food residues)
Japan	97.9 percent DFQF (Exclusion: fish and crustaceans, footwear, milling products, cereal products, sugar)

Preferential Market Access for Goods (2)

Market	Duty free tariff line coverage and major exclusions
Republic of Korea	89.9 percent DFQF (Exclusion: fish and crustaceans, mineral fuels, oil seeds and oleaginous fruits, wood products, vegetables)
New Zealand	100 percent DFQF
Norway	100 percent DFQF
Russian Federation	37.1 percent DFQF (Exclusion: machinery and mechanical appliances, chemicals, electrical machinery, iron and steel products, transport vehicles)
Switzerland	100 percent DFQF
Chinese Taipei	30.8 percent DFQF (Exclusion: machinery and mechanical appliances, chemicals, electrical machinery, fish and crustaceans, plastics)
Thailand	70.4 percent DFQF
Turkey	80.5 per cent DFQF (iron and steel products, fish and crustaceans, food preparation, meat, oil and seeds and oleaginious fruits)
United States	82.2 percent DFQF (apparel and clothing, cotton fibres, footwear, diary and other animal products)

Preferential Treatment for Services and Service Suppliers

- ✓‘ Service Waiver’ of Eighth Ministerial Conference, 2011, until December 2030;
- ✓24 notifications from 23 countries- Australia, Brazil, Canada, Chile, China, Hong Kong, Iceland, India, Japan, Korea, Liechtenstein, Mexico, New Zealand, Norway, Panama, Singapore, South Africa, Switzerland, Chinese Taipei, Thailand, Turkey United States, Uruguay and the EU indicating preferential treatment on sectors and modes of supplies;

However, not yet implemented any waiver offer.

Flexibilities under WTO rules

- ✓ Understanding on the Balance of Payments Provision of GATT-simplified procedures,
- ✓ Agreement on Agriculture- flexibilities to provide certain export subsidies until 2030, notifications,
- ✓ Sanitary and Phytosanitary (SPS) Measures-priority for technical assistance,
- ✓ Agreement on Subsidies and Countervailing Measures- flexibility in export subsidies,
- ✓ Trade Facilitation Agreement- longer notification and implementation period,
- ✓ Trade-Related Aspects of Intellectual Property Rights (TRIPS)-exemption from applying all substantive TRIPS standards until 1 July 2021 and exemption from protecting pharmaceutical products until 2033;
- ✓ Dispute Settlement Understanding- free legal services;
- ✓ Trade Policy Review Mechanism- longer period.

Flexibilities in Regional Groups

- ✓ **<u>South Asian Free Trade Agreement (SAFTA)</u>**
  - ✓ Nepal has maintained long sensitive list as an LDC member,
  - ✓ Members have smaller sensitive lists for LDCs and India provides DFQF market access,
  - ✓ There are less stringent rules of origin for LDCs
  - ✓ There are special considerations on the application of anti-dumping and/or countervailing measures against LDCs
  - ✓ There are special provision not to be applied special safeguard measures against products originating in LDC contracting states,
- ✓ **<u>The BIMSTEC Free Trade Area</u>** (yet to come into force)
  - ✓ It has less stringent rules of origin for LDCs. The rules of origin applicable to LDC will be 30 per cent plus a change in tariff sub-heading (CTSH), while as a non-LDC the requirement will be 40 per cent,

Development Cooperation

- ✓Commitment in bilateral ODA flows to LDCs- 0.15 to 0.20 percent of GNI to LDCs
- ✓Multilateral development cooperation- UNDP to ensure 60 percent of core resources are allocated to LDCs; UNICEF to allocate 60 per cent of regular resources to LDCs;
- ✓Though not reflected in ODA, several organizations, such as UN-DESA, UN-OHRLLS, UN-ESCAP, UNCTAD, UNFCCC and others, provide policy analysis and information services, capacity building, support in obtaining access to information and resources, and advocacy services.

LDC-Specific Mechanisms

- ✓Access to technology: LDC Technology Bank
- ✓Climate change: work programme for LDCs and LDC Fund
- ✓Aid for Trade: Enhanced Integrated Framework
- ✓Investment Support Programme: UNCDF, International Development Law organization (IDLO) and UN-OHRLLS
- ✓Support to participation in the United Nations and other international forum

Impact of LDC Graduation

Market Access

(Impact section heavily draws from SAWTEE. 2022. Nepal's graduation from the LDC category: Implications for international trade and development cooperation', a report submitted to FCDO, the United Kingdom.)

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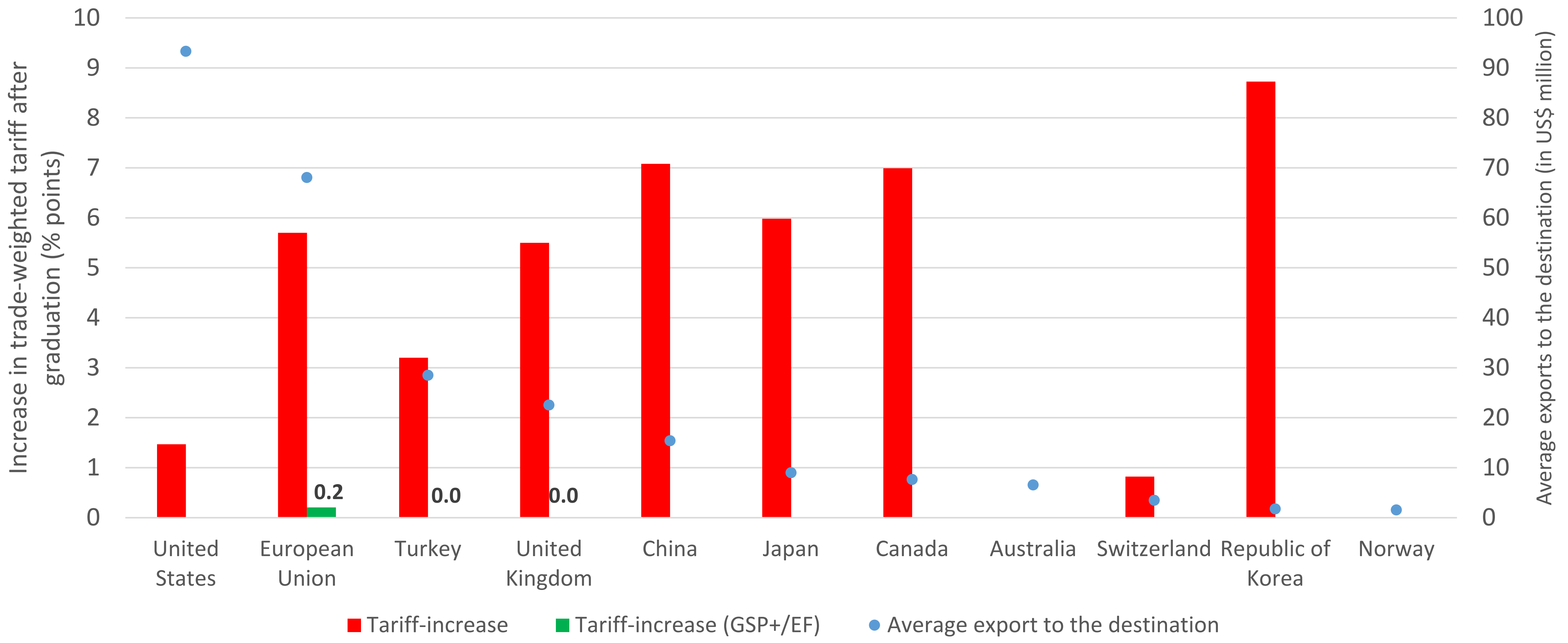
Applicable tariff schemes in international trade

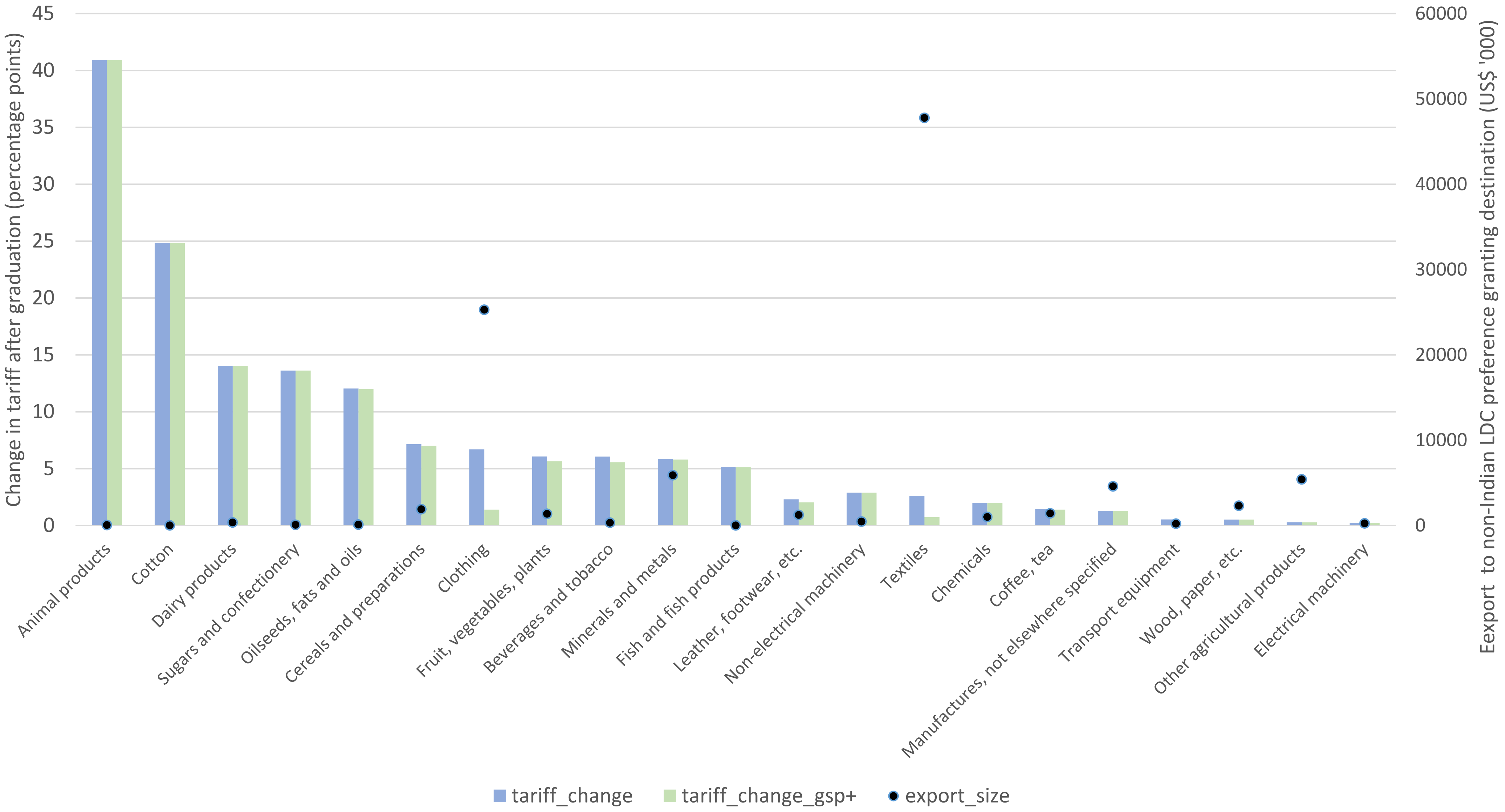
- Most Favoured Nation (MFN) tariff
- Duty Free Quota Free (DFQF) market access for LDCs
- Generalized System of Preference (GSP) and its variants for specific group of developing countries
- Tariffs applicable under Free Trade Agreement (FTA)/ Regional Group

Projected tariff change in top destinations



Tariff increase is especially pronounced in European Union and United Kingdom. However, entry into GSP+ or EF will result in insignificant or no change in tariff after graduation.

Sector-wise trade-weighted tariff change



Estimates of impact on export volume

Source	Trade impact	Methodology
WTO (2020)	2.48% (US$ 20.1 million) reduction in total exports	Partial equilibrium model (using trade data for 2016-2018) taking into account preference utilization rates
ITC (n.d.)	4% reduction (US$ 59 million) in total projected exports of US$ 1.4 billion in 2026.	Partial equilibrium model (using projected trade for the year 2026)
NPC and UNDP (2020)	3.7% reduction in total exports	Partial equilibrium model (using trade data for 2017) assuming MFN tariffs as the next best tariffs

Other consequence of LDC graduation: Change in ROO provisions

- No change in ROO provisions in USA, Japan, and New Zealand but ROO gets stricter, in general or in specific products, in other destinations.

EU, Turkey, and UK:

- ROO changes from single transformation to double transformation (in many apparel products)
- Local content requirement of 30% increases to 50% for some products.

Canada:

- Value-added criteria (RVC) increases from 40% to 60%
- LDC-specific ROO preferences in several apparel and textile articles no longer applicable

Australia:

- RVC increases from 25% (provided another RVC 25% comes from the qualifying area) to 50%

Primary impact

- Impact of change in ROO will be witnessed primarily in Nepal's apparel exports to the European Union, United Kingdom, and Canada. Studies (e.g. EIF, 2022) and our interaction with the private sector indicate that many apparel exporters will find it difficult to fulfill the new ROO provisions.

Impact of LDC graduation on Nepal's bilateral/regional trading arrangements

- No fundamental change in exports to India as preferences in Nepal-India Trade treaty are not based on Nepal's LDC status.
- Impact on exports to SAFTA countries will be marginal, given the bilateral Nepal-India trade treaty and low volume of exports to non-Indian SAFTA destinations.
- Caveat with regard to Nepal's exports to SAFTA (India):

HS Code	Description	Average export to India in 5 years	No. of years exported in the five-year period	Share of export in total export to India (%)	Tariff in India for SAFTA (LDC) (%)	Tariff in India for SAFTA (non-LDC) (%)	MFN Tariff (%)
150790*	Refined soyabean oil	117.01	3	20.2	0	25	45
151190	Refined palm oil	49.81	3	8.6	0	54	54

*HS 150790 has two tariff lines. HS 15079010 doesn't have preferential rate for non-LDC SAFTA members and attracts a MFN rate of 45% whereas HS 15079090 offers a preferential rate of 5% for non-LDC SAFTA members.

- Potential exports to SAFTA might be affected by a more stringent ROO provisions after graduation: CTH+30% value-addition will change to CTH+40% value-addition

Impact on services trade of Nepal

- Insignificant change on services trade because of the lack of operationalization of LDC services waiver.
- Much of Nepal's export of services is in the travel and tourism sector, which has been taking place without any connection to the services waiver.

Development Cooperation

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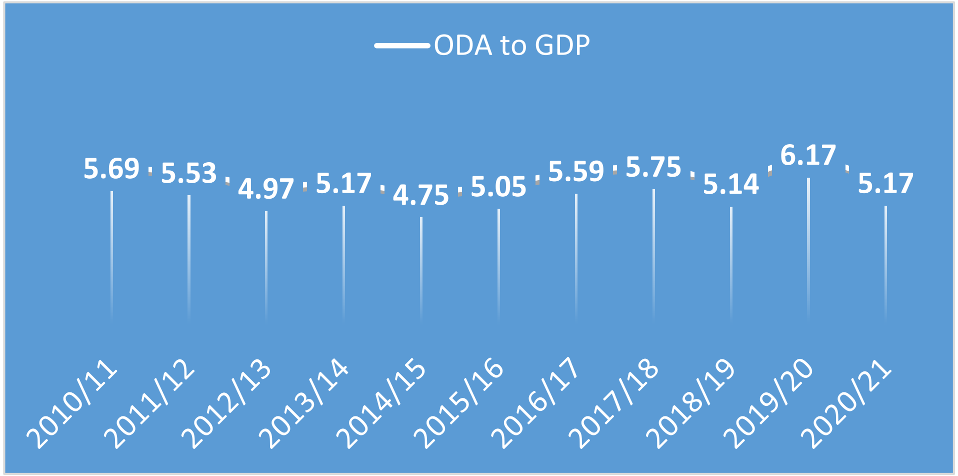
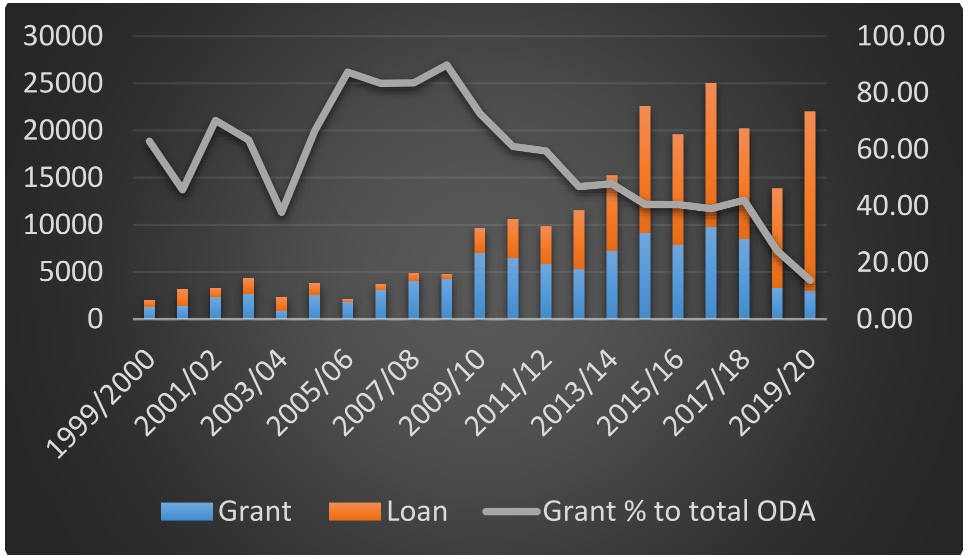
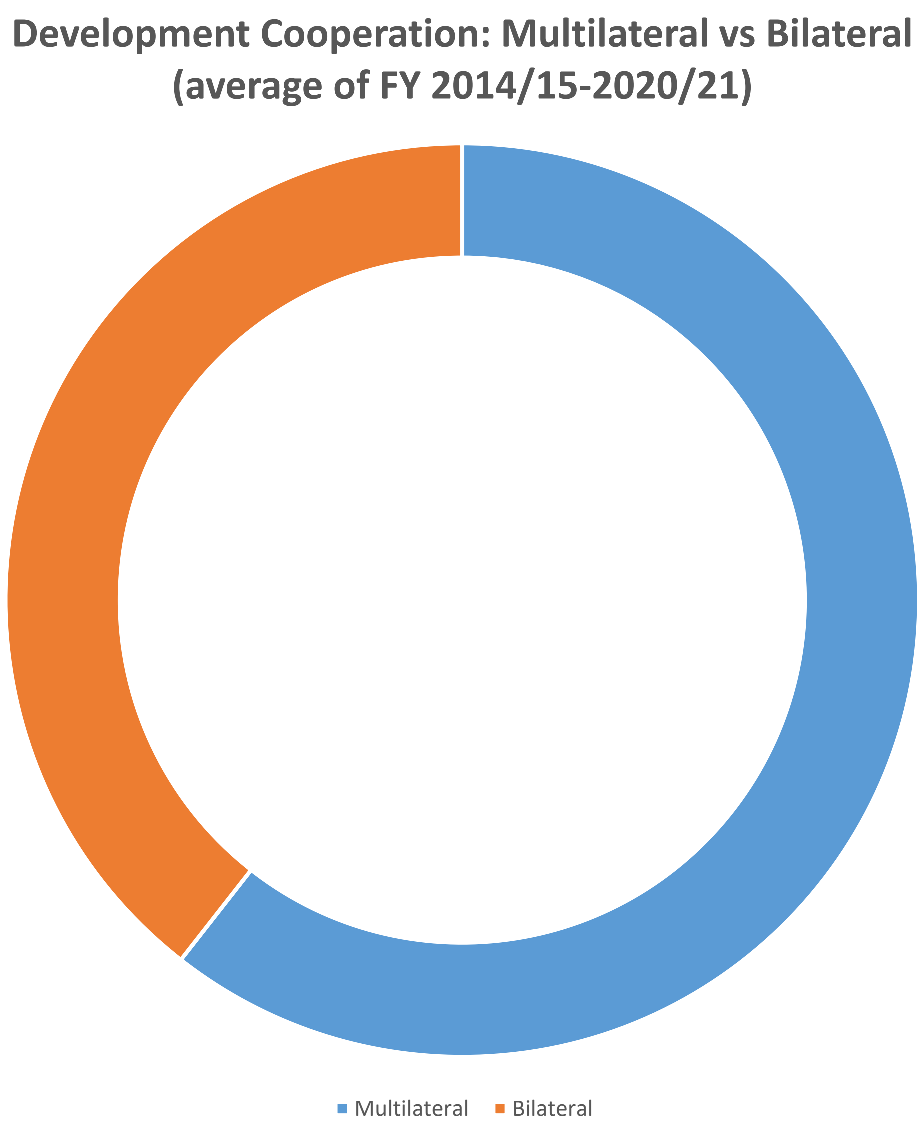
Overview of ODA

- ODA disbursement to GDP: 5% (avg of 2010/11—2020/21)
- Multilateral sources (59%) vs bilateral source (41%)
- Loan outstripped grants after 2013/14
- Top three sectors for ODA disbursement: education, health and energy

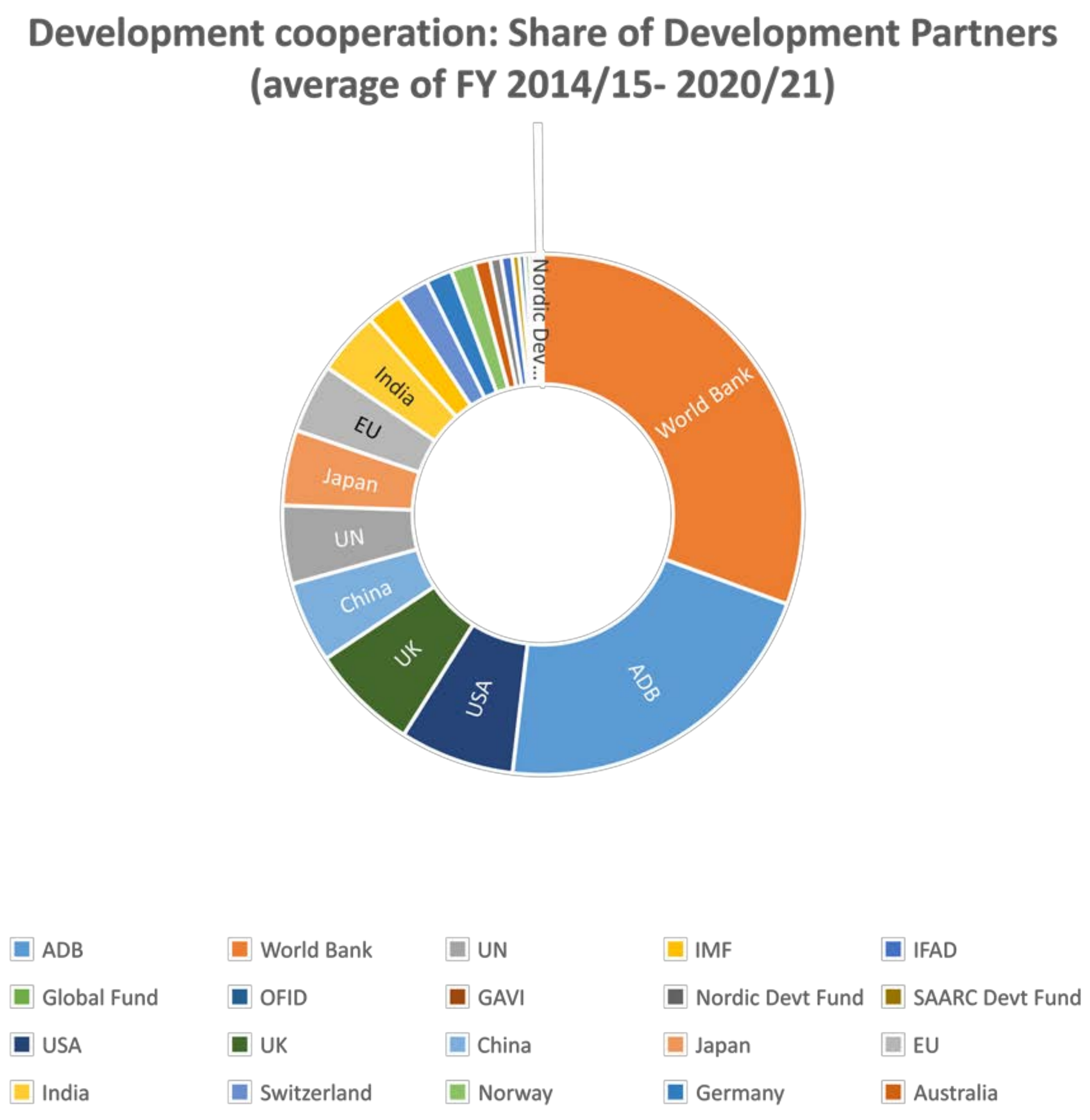




Development cooperation: Multilateral vs. Bilateral



Development Cooperation: Contribution of each development partners



Impact of LDC graduation

Assessment based on consultations with 15 major development partners and publicly available data

ODA mostly not contingent on LDC status as bilateral and cultural ties; GNI per capita; creditworthiness; geopolitical factors also matter

LDC graduation and, along with it, improved GNI per capita figure may result in Nepal losing some level of concessionality and favourable terms

Bilateral partners

- EU, Japan and Finland take into account Nepal's aspirations to graduate from the LDC category
- Bilateral development partners' strategies in line with 15th development plan, hence, implicitly support graduation strategy
- Direct impact
  - Lose preferential lending terms provided by Japan and South Korea

Multilateral partners-1

Asian Development Bank

- Nepal is receiving concessional terms (maturity of 24-32 years, a grace period of 8 years, and an interest rate of 1-1.5 percent) due to its GNI per capita, creditworthiness and LDC status
- Having crossed income threshold, losing LDC status will shift Nepal from concessional to blend assistance with a maturity period of 25 years, the grace period of five years and the interest rate is at least 2%

World Bank

- Nepal is already low-middle income country hence may not be eligible for IDA concessional credit for longer period
- By 2026, World Bank might offer blend credit a (30-year maturity, 5-year grace period, 1.25% interest rate apart from a 0.75% service charge)

Multilateral partners-2

UN Systems

- UNDP and UNICEF are mandated to provide a certain portion of their core resources to LDCs
- Nepal will not receive new funding support from LDCF but will be eligible to access other financing sources of UNFCCC
- Nepal may lose access to other agencies that support LDCs in capacity building and advocacy

Others

- Enhanced Integrated Framework (EIF): EIF's aid for trade technical assistance has helped in designing NTIS, trade institutional capacity building projects; productive capacity building interventions in priority sectors etc; graduating LDCs receive support for 5 more years
- Will lose support provided for participation in international forums

Policy Space

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Implications for policy space - I

- Loss of flexibilities enjoyed as an LDC in implementing policies related to trade, industrial development and health
- Greater scrutiny of Nepal's policies- inability to continue with policies that run afoul of WTO rules or are potentially challengeable
- Pressure to liberalize trade further at the WTO and regional forums- less space to protect domestic industry; revenue loss

Implications for policy space - II

Export subsidies	
Agriculture	Prohibited, but LDCs given exemption for some types of export subsidies in agriculture. Nepal committed not to provide any agriculture export subsidies. Graduation could invite scrutiny.
Non-agriculture	Prohibited, but allowed to LDCs. May lose this exemption. Listed countries with per capita GNI below $1,000 (constant 1990 US dollars) also allowed to provide non-agricultural export subsidies. Under current rules, a graduated LDC is not automatically eligible for the income-based exemption even if its income is below the cut-off.
Incentives under SEZ Act	Most of these are subsidies if they are contingent upon exporting. The above implications hold.
Services	No impact. WTO lacks specific disciplines on subsidies in the services sector.

Implications for policy space - III

Domestic support/subsidies	
Agriculture	No impact. Considerable scope to provide domestic agricultural subsidies.
Non-agriculture	Local content subsidies prohibited (all members). Nepal provides/plans to provide such subsidies. Will attract greater scrutiny. Non-specific subsidies are not prohibited (though actionable). This holds true for all members.
Services	No impact. WTO lacks specific disciplines on subsidies in the services sector.

Implications for policy space - IV

Intellectual property rights (Implementation of TRIPS Agreement)	
<u>General transition period for LDCs</u> Exemption from applying all substantive TRIPS standards until 1 July 2034 (Article 66.1, latest extension IP/C/88).	No direct impact – but greater scrutiny of commitment. When acceding to the WTO, Nepal had agreed to apply the TRIPS Agreement by no later than 1 January 2007.
<u>Transition period for pharmaceutical products for LDCs</u> Exemption from providing protection for patents and undisclosed information until 1 January 2033 Waiver from notification requirements for issuing compulsory licenses for exports of pharmaceutical products to LDCs or other countries with insufficient manufacturing capacities in the pharmaceutical sector (Article 31 bis)	Will lose these flexibilities. Upon graduation, if Nepal wants to use this system, it has to make a notification of its intention to use the system and confirm its insufficient manufacturing capacity. Nepal has not used this system to date.

Implications for policy space - V

Intellectual property rights (Implementation of TRIPS Agreement)	
<u>Technology transfer</u> Developed country members required to provide incentives to enterprises and institutions in their territories to promote technology transfer to LDCs (Article 66.2).	Upon graduation, Nepal will lose the S&D concerning technology transfer. But the implementation of this provision has been weak.
<u>Notifications</u> LDCs are exempt from most TRIPS notification requirements.	Following graduation, Nepal will be required to adhere to the transparency provisions outlined in the TRIPS Agreement and TRIPS Council decisions, including the obligation in Article 63 to notify laws and regulations on intellectual property rights pertaining to TRIPS.

Implications for policy space - VI

- Under current rules at the WTO, LDCs will lose all exemptions from making new liberalization commitments. Hence, Nepal may be required to undertake new liberalization commitments even in the ongoing round of negotiations if it continues after 2026, besides future rounds of negotiations.
- As a developing country WTO member, Nepal will not have access to S&D provisions that may result from the ongoing negotiations.
- Developing country WTO members also enjoy some flexibilities in negotiations and are not expected to undertake the same level of commitments as developed country members.
- Nepal could come under pressure also at regional forums to liberalize trade further. The government has concerns about the (real or perceived) adverse impacts of trade liberalization to date on public revenue and domestic industry.
- Nepal will continue to have the option to raise tariffs up to bound levels; take contingency measures to protect domestic industry.

Elements of Smooth Transition Strategy

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Smooth Transition Strategy-1

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Fiscal Policy	Improve MTEF ensuring clear linkages among input, output, outcome, and impact and internalizing green, resilient and inclusive development (GRID) approach at all three tiers of government Develop fiscal policy framework together with review of SDGs financing	Robust MTEFs integrated with GRID approach in place at all levels of government Spend 30 percent of total expenditure as capital expenditure by 2026 and 40 percent by 2020 Substantially increase expenditure in Science, Technology, Engineering and Mathematics (STEM) areas Substantially increase expenditure in health sector Reduce share of import-based revenue to 40 percent of total revenue by 2026 and to 33 percent by 2030. Reduce budget deficits to 7.5 percent of GDP by 2026 and to 6 percent by 2030.	Medium to Long-term Medium to Long-term Medium to Long-term Medium to Long-term Medium to Long-term Medium to Long-term	Ministry of Finance, National Planning Commission;, Provinces and Local Governments

Smooth Transition Strategy-2

Policy Area • .	Proposed Policy Action	Expected Outcome	Time frame **Short-less than1 year** **Medium-2-5 years** **Long-more than 5 years**	Responsible Agencies
Monetary and exchange rate policies	Maintain money supply (M2) and credit expansion in tandem with GDP growth and inflation target	Maintain inflation rate at below 5 percent	Medium to Long term	Nepal Rastra Bank
		Maintain credit expansion rate at below 3.5 times of GDP growth	Short to Medium term	Nepal Rastra Bank
		Mobilize 2/3rd of credit disbursed towards the productive sectors.	Short-term to Medium-term	Nepal Rastra Bank
	Review exchange rate regime	Review exchange rate with Indian currency and maintain stability	Short-term	Nepal Rastra Bank

Smooth Transition Strategy-3

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Trade and Industrial Policy	Review trade policy and tax regime with a view to reduce/eliminate anti-export bias and promote domestic industries Review and update NTIS by taking into account new developments in regional and global economy, and elimination of ISMs Review and update industrial policy, including foreign direct investment policy, by taking into account, fourth industrial revolution, new developments in regional and global economy, and elimination of ISMs	Increase manufacturing value added to 8 percent of Gross Domestic Product (GDP) by 2026 Increase merchandise exports to 6.5 percent of GDP by 2026 and to 10 percent by 2030. Increase export import ratio to 30 percent by 2030 Increase annual FDI inflows to GDP ratio to 1 percent by 2026 and to 2 percent by 2030.	Medium term Medium term to long term Long-term Medium to Long-term	Ministry of Industry, Commerce and Supplies Ministry of Finance Ministry of Finance Investment Board of Nepal

Smooth Transition Strategy-4

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Trade-related capacity building	Prepare trade related capacity building plan including capacities in the areas of trade policy making, trade negotiation sanitary and phyto-sanitary standards, and technical standards	Successful negotiation with major trading partners on extension of trade preferences by minimum of 5 years after graduation	Short to Medium-term	Ministry of Industry, Commerce and Supplies, Ministry of Foreign Affairs, Ministry of Agriculture and Livestock Development, Ministry of Finance
		Prepare action plan for the implementation of WTO agreements such as AoA, TRIPs, TRIMs, SCMs, GATS by 2024	Short to Medium-term	
	Prepare and enforce Trade Logistics Policy	Establish internationally accredited laboratories in all seven provinces	Short to Medium-term	
		Reduce trade cost by 30 percent by 2026	Short to Medium-term	

Smooth Transition Strategy-5

Policy Area • .	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Investment climate	Develop and implement a comprehensive action plan for improving the investment climate taking into account policy and legal instruments, investment incentives and investment protection, among others.	Improve Doing Business score by minimum 20 percent by 2026 and minimum 35 percent by 2030	Short to Medium-term	Ministry of Industry Commerce and Supplies Ministry of Finance Investment Board Nepal
Institution building and rule of law	Develop and implement framework for institution building, good governance, and rule of law	Improve Rule of Law Index by minimum 5 percent every year until 2030	Short to Medium term	Prime Minister's Office

Smooth Transition Strategy-6

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Productive and decent employment	Review employment policy and mainstream in other sectoral policies, such as agriculture policy, industrial policy, trade policy, technology policy, etc.	Reduce unemployment rate by half by 2026 and achieve full employment by 2030 Increase employment in the secondary sector to **35** percent by 2026 and by 45 percent by 2030 Increase formal sector employment by 50 percent by 2030 Double the labour market participation rate of women by 2030	Medium to Long-term Medium to Long-term Medium to Long-term Medium to Long-term	Ministry of Labour, Employment and Social Security; Ministry of Agriculture and Livestock Development, Ministry of Industry Commerce and Supplies, Ministry of Finance, Prime Minister's Office

Smooth Transition Strategy-7

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Reducing vulnerabilities and Enhancing Resilience	Revise Disaster Risk Reduction and Management Act (2017) and prepare more robust disaster risk management framework at the federal and provincial level Consolidate social security programs and make them targeted Develop action plan for accelerate energy transition Design and implement national short-lived climate pollutants (SLCPs) mitigation strategies	Substantially reduce death and injuries occurring from disasters Increase the share of targeted poor and vulnerable receiving social protection to 75 percent by 2026 and 100 percent by 2030 Rapidly reduce greenhouse gas emissions and air pollution Significantly reduce the share of fossil fuels in energy mix Reduce death and morbidity from pulmonary diseases	Medium to Long-term Medium to Long-term Short to Long-term Short to Long-term Short to Long-term	Ministry of Home Affairs, Ministry of Federal Affairs and General Administration, Provincial Governments, Ministry of Energy, Water Resources and Irrigation, Ministry of Forest and Environment

Smooth Transition Strategy-8

Policy Area	Proposed Policy Action	Expected Outcome	Time frame Short-less than1 year Medium-2-5 years Long-more than 5 years	Responsible Agencies
Private Sector Development	Develop and Implement Private Sector Development Framework with focus on women and other small entrepreneurs	Share of private sector investment increases by 1 percentage point every year until 2030. Substantially increase the share of women owned/managed enterprises and SMEs in industrial output	Short to Long-term Short to Long-term	Ministry of Industry, Commerce and Supplies, FNCCI, CNI, Chamber of Commerce, commodity associations etc
Diplomatic capital	Strengthen economic diplomacy and better communicate geographical and structural constraints for development to international community Review trade agreements and explore possibilities of Free Trade Agreements (FTA) with major trading partners	Gradual phasing out of ISMs during post-graduation transition period Adoption/offer of post graduation adjustment package by major development partners	Short to Medium term Short to Long-term	Ministry of Foreign Affairs, Ministry of Finance, Ministry of Industry, Trade and Supplies

Thank you

For comments and queries

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