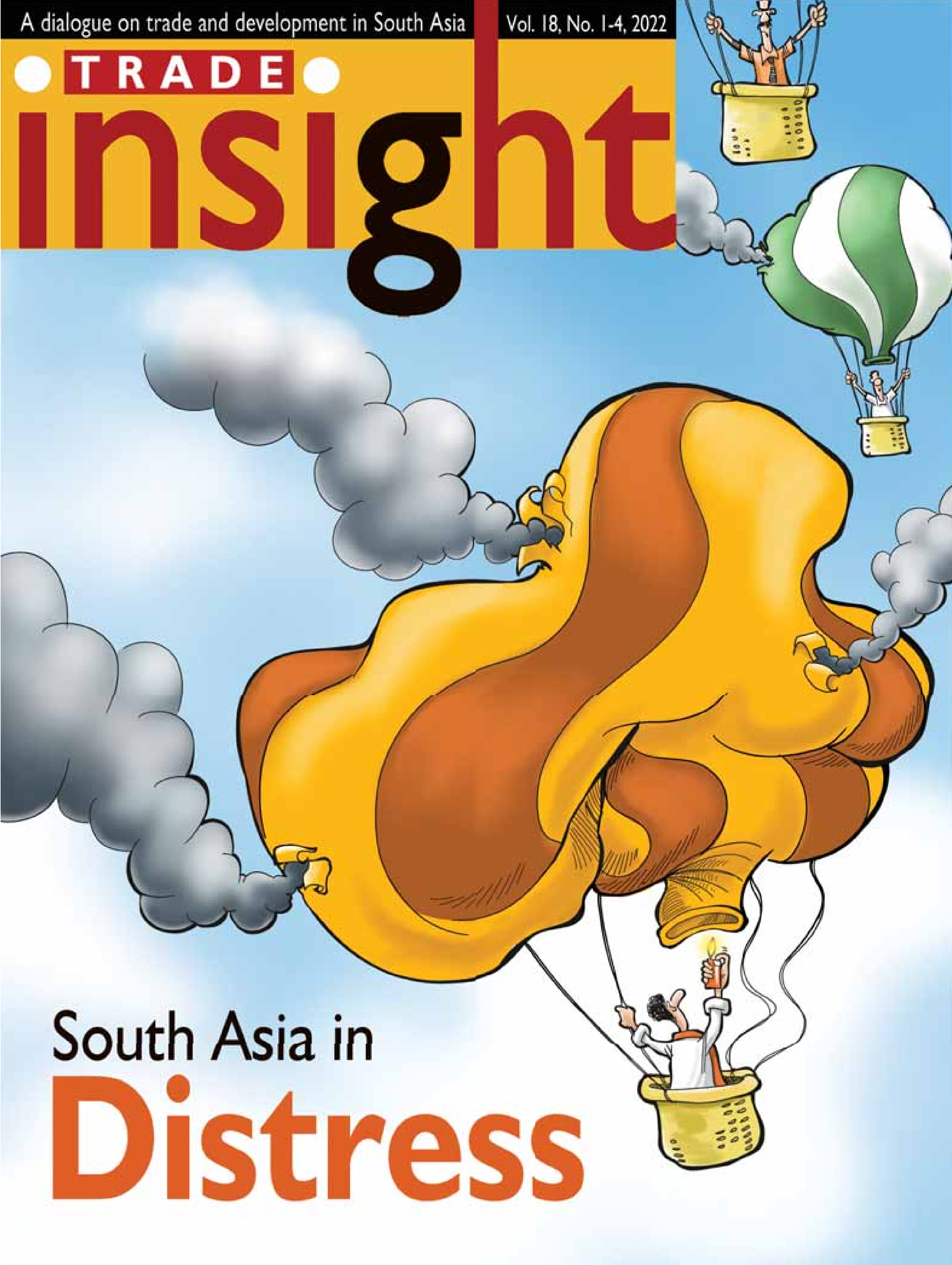
A dialogue on trade and development in South Asia
Vol. 18, No. 1-4, 2022

TRADE insight



South Asia in Distress

ECONOMIC SETBACK | ENERGY TRANSITION | POLICY COHERENCE

A dialogue on trade and development in South Asia Vol. 18, No. 1-4, 2022

TRADE insight

sawtee

P.O. Box: 19366
Tukucha Marg
Baluwatar, Kathmandu, Nepal
Tel: +977-1-4424360/4444438
Fax: +977-1-4444570
E-mail: sawtee@sawtee.org
Web: www.sawtee.org

Regd. No. 208/070/071 (Kathmandu)

editors' note

Hope amid despair

HOPES of a normal year in 2022 were dashed by escalating geopolitical tensions, continued US-China trade war, a war in Europe and the resulting rise in energy prices and persistent inflation. Freight and cargo rates fell but were still higher than pre-pandemic levels. Economic recovery was stymied. External shocks—high prices and a hit to foreign exchange earnings—combined with domestic structural weaknesses and policy missteps led to economic crises of varied intensity in South Asia, from an economic collapse in Sri Lanka to a severe foreign exchange crisis in Pakistan to a build-up of pressure on foreign exchange reserves in Bangladesh and Nepal. Partly attributed to climate change, the devastating floods in Pakistan added to its economic woes, not to mention the tragic loss of lives and displacement of millions of people. Year 2022 was also the half-way mark towards the Sustainable Development Goals (SDGs). The setback caused by the pandemic to progress towards the SDGs was exacerbated by the additional shocks.

Three South Asian least developed countries (LDCs) are expected to graduate from the LDC category by 2026: Bhutan in 2023, and Bangladesh and Nepal in 2026. Structural handicaps still characterize these economies. They stand to lose trade preferences in attractive markets. Rules of origin will tighten. They will lose policy space, notably in the area of intellectual property protection. The shocks of COVID-19 and the war in Europe have exposed the fragilities in these economies.

Originally scheduled to be held in June 2020 in Kazakhstan and postponed twice due to the pandemic, the Twelfth Ministerial Conference of the World Trade Organization (WTO) (MC12) was held in Geneva in June 2022 and concluded with the Geneva Package. A notable outcome was the decision to waive compulsory licensing for COVID-19 vaccines. The decision was considerably weaker than what the developing world had sought, but still was a welcome departure from the frustratingly slow progress in negotiations at the WTO on issues of special interest to poorer countries. As the scope of the decision is limited to COVID-19 vaccines, WTO members were supposed to decide within six months on an extension to cover the production and supply of COVID-19 diagnostics and therapeutics. Over a polarizing debate on the topic, the Trade-Related Aspects of Intellectual Property Rights (TRIPS) Council in December recommended a further delay on a decision on such an extension. The divide, mainly along developed and developing country lines, belied geopolitical alignments. MC12 could not deliver a package of support measures for graduated LDCs to ensure that graduation is smooth, meaningful, sustainable and irreversible.

In November, the 27th United Nations Climate Change Conference, COP27, reached a breakthrough decision to establish new funding arrangements to assist developing countries in responding to loss and damage (L&D). All eyes are now on the first meeting, expected to take place by March-end 2023, of the transitional committee, established to make recommendations on how to operationalize the new funding arrangements. Sustained advocacy and pressure are crucial to prevent a replay of the failure by developed countries to make good on their 2009 pledge to mobilize U$100 billion in climate finance annually to help vulnerable countries deal with climate change. But the fact that the case for funding for L&D has been formally recognized by COP27 is an achievement. It was an uplifting news in a year otherwise marred by geopolitical tensions and war, and the resultant economic fallout. ■

Trade Insight Vol. 18, No. 1-4, 2022

Content

MEMBER INSTITUTIONS OF SAWTEE

BANGLADESH 1. Bangladesh Environmental Lawyers' Association (BELA), Dhaka; 2. Unnayan Shamannay, Dhaka; INDIA 1. Citizen consumer and civic Action Group (CAG), Chennai; 2. Consumer Unity & Trust Society (CUTS), Jaipur; 3. Development Research and Action Group (DRAG), New Delhi; NEPAL 1. Society for Legal and Environmental Analysis and Development Research (LEADERS), Kathmandu; 2. Forum for Protection of Public Interest (Pro Public), Kathmandu; PAKISTAN 1. Journalists for Democracy and Human Rights (JDHR), Islamabad; 2. Sustainable Development Policy Institute (SDPI), Islamabad; SRI LANKA 1. Institute of Policy Studies (IPS), Colombo; 2. Law & Society Trust (LST), Colombo

EU agrees carbon market overhaul in bid to hit 2030 climate goal

EUROPEAN Union negotiators reached agreement on 18 December to reform the EU's Emissions Trading Scheme (ETS), the biggest carbon market in the world and the bloc's flagship climate policy instrument.

The ETS currently caps the emissions of around 10,000 factories and power plants, allowing those with surplus credits to make a profit by selling CO2 permits on the market. The scheme is now being extended to cover more sectors of the economy in order to align with the EU's 2030 climate goal – a commitment to reduce net emissions by 55 percent before they are eventually brought down to zero by 2050.

Under this agreement, sectors covered by the ETS will have to cut their emissions 62 percent below 2005 levels by 2030 – a significant increase on the current 43 percent target.

A separate carbon market is also being created for buildings and road transport. This second ETS will start applying as of 2027 and will be accompanied by an EU€87-billion social climate fund to compensate households for the extra costs this will create.

This new carbon price on heating and transport fuels will be capped at EU€45 per tonne in a bid to prevent social discontent and rising energy bills. And if energy prices are exceptionally high, the new scheme will be delayed by a year, until 2028. *(https://www.euractiv.com/, 18.12.2022)* ■

China reopens Kerung-Rasuwagadhi border to Nepali exports

BEIJING on 28 December allowed Nepal's exports to pass into China through the Kerung-Rasuwagadhi border after keeping it shut to two-way traffic for three years.

Chinese goods have been entering Nepal intermittently through Kerung, one of the two international border points on the Nepal-China border, but it was no go in the other direction.

The fate of another border point further to the east at Tatopani is uncertain. Once a hotspot for transit commerce, Tatopani has lain abandoned since the 2015 earthquake destroyed the infrastructure and trans-Himalayan trade came to a halt.

Nepali traders, who are reported to have suffered massive losses by missing out on the holiday shopping seasons in 2021 and 2022 after China closed the border, have been calling the policy a trade embargo.

For three years, China had permitted only outbound shipments to pass through the Kerung-Rasuwagadhi border point, about 175 km north of Kathmandu, and that too under a quota system.

From January 2020 when the coronavirus pandemic was beginning to spread, there was a near halt in the arrival of cargo containers from China to Nepal. Trade still has not resumed fully, with the northern neighbour placing strict restrictions at the border.*(https://kathmandupost.com, 28.12.2022)* ■

India allows international trade settlements in rupees

THE Indian government allowed international trade settlements in the Indian currency for export promotion schemes under its foreign trade policy. The government of India made suitable amendments in the Foreign Trade Policy and Handbook of Procedures to allow for international trade settlement in Indian rupees.

Given the rise in interest in the internationalization of the Indian rupee, the policy amendments have been undertaken to facilitate international trade transactions in Indian rupees, as per India's Ministry of Commerce and Industry.

The ministry said the changes have been notified for export performance for recognition as Status Holders, realization of export proceeds under advance authorization and Duty-Free Import Authorization schemes, and realization of export proceeds under export promotion capital goods scheme. *(https://www.livemint.com/, 09.11.2022)* ■

pixahive

Estimates place Pakistan's flood losses at US$28 bn

PAKISTAN has conducted a Post Disaster Needs Assessment (PDNA) in the wake of this year's severe floods and estimated damage to the extent of US$28 billion and an upsurge in poverty by 5 percent, indicating that between 9 million and 12 million people might fall below the poverty line.

On the unemployment front, official estimates reveal that between 1.8 million and 2 million jobs have been lost in the floods. The government has made plans for reconstruction and suggested that it might take 2–10 years for long-term construction of the flood-affected areas. Average inflation might touch the 23-25 percent mark in the current fiscal year.

Alarmingly, the Planning Commission concedes that agriculture growth might plunge into negative territory, in the range of -0.7 percent to -2.1 percent, compared to the earlier target of 3.9 percent for the current fiscal year. Export losses might amount to US$3 billion.

In the external sector, overall export losses are anticipated to be around US$3 billion in fiscal year 2022/23 (FY23) due to a decline in global demand and lower exports of rice, cotton, fruits and vegetables. Imports of raw cotton, wheat and vegetables are expected to increase due to flood-induced losses. Water availability is expected to improve the energy mix, resulting in lower oil imports.

Additionally, lower GDP growth and income levels are expected to lower aggregate demand, causing a reduction in the overall import bill. GDP growth for FY23 is expected to be at 1.8-2.3 percent compared to the annual plan target of 5 percent, that is, an income loss of PKR2.4 trillion. *(https://www.geo.tv/l, 27.09.2022)* ■

Pakistani exporters pine for Indian cotton

WITH the devastating monsoon rains hitting cotton-producing areas, the Pakistan Textile Exporters Association has approached the federal government to allow the import of cotton from India via Wagah to meet rising export orders.

Exporters say early estimates show that 25 percent of the standing cotton crop had been damaged and there was a possibility of a raw material shortage in the country.

Separately, in the wake of flood losses suffered by the cotton harvest in Sindh and Punjab, the federal government formed a committee that will negotiate with seed companies and facilitate them to introduce state-of-the-art cotton seeds in the local market.

The decision was taken during a meeting at the Ministry of National Food Security and Research to consult with stakeholders and review proposals for the enhancement of yield and area of cotton crops. *(https://www.dawn.com/, 08.09.2022)* ■

Nepali tea growers breathe easier after India lifts ban on tea blending

INDIA has lifted an 11-month-old ban on blending Darjeeling tea with other teas, raising the spirits of the Nepali tea industry which greatly depends on exports to the southern neighbour.

Nepal's NPR 5-billion tea sector was badly hit as shipments plunged after India issued the restriction in November 2021 in a bid to protect its domestic industry.

Indian tea producers can now mix Nepali tea with their product, but they are not permitted to use the name “Darjeeling” on the mixture.

Darjeeling Tea is a geographical indication (GI) label given to items associated with a specific place or origin, and it cannot be put on tea not cultivated in their gardens or not manufactured by the standards outlined in the code of practice.

The Tea Board of India said it would take stern action if any Indian seller was found using the GI label for mixed teas.

Nepali manufacturers and traders were greatly worried following reports about India’s potential move to block Nepali tea. India is the largest buyer of the product. *(https://kathmandupost.com/, 20.10.2022)* ■

Nepal's Supreme Court halts construction of multi-billion-dollar Nijgadh airport

THE Supreme Court of Nepal quashed all government decisions to construct a full-fledged international airport in Nijgadh, Bara, an alternative to Kathmandu's Tribhuvan International Airport.

An extended full bench of the Supreme Court issued an order to the government to find an alternative to Nijgadh, if it wants to build the international airport.

The fate of the US$3.45 billion Nijgadh International Airport in Bara had been hanging in the balance for years, with successive governments pushing for it and environmentalists calling for taking into consideration the impacts of the national pride project on environment, biodiversity, local communities and wildlife.

The proposed site is adjacent to the Parsa National Park, a corridor to wildlife like tigers and elephants, and a habitat of rich biodiversity. Located 175 km south of Kathmandu, the planned construction site lies amid dense forests with nearly 90 percent of the project area covered by Shorea robusta trees, also known as sal or sakhua. The market value of the lumber stands at over NPR65 billion.

According to an environmental and social impact assessment carried out by the Tourism Ministry in February 2017, more than 2.4 million small and large trees would have to be felled to build the international airport in three phases. *(https://kathmandupost.com/, 24.05.2022)* ■

Nepal govt decides lifting ban on imports of luxury goods

THE government decided to lift the seven-month-old ban on the import of "luxury goods" to meet a condition of the International Monetary Fund (IMF) ahead of the formation of a new government.

The Cabinet meeting on 6 December decided to completely lift the ban from 16 December.

Earlier in April, alarmed by the fast pace at which Nepal's foreign currency reserve was going down, the government imposed import restrictions besides ordering importers to maintain a 100 percent margin amount to open a letter of credit.

The directive issued on 26 April embargoed 10 types of goods described as luxury items. They included, among other things, mobile sets worth over US$600 and motorcycles of over 250cc capacity. Harsher restrictions followed, and mobile sets costing more than US$300 and motorcycles with a capacity of more than 150cc were banned.

wikimedia commons

On August 30, the government loosened the restrictions by permitting the import of diamonds, large television sets, toys, snacks and tobacco. The ban on automobiles, mobile phones, liquor and heavy motorcycles had been extended until December 15.

While the International Monetary Fund (IMF) had questioned the wisdom behind lengthening the import ban on certain products as it was hurting trade and the economy, economists too have been saying that prolonging trade restrictions goes against the principles of a free market economy. (https://kathmandupost.com/, 06.12.2022) ■

India, Bangladesh, Nepal finalize MoU to boost trade and connectivity

INDIA, Bangladesh and Nepal in March finalized a memorandum of understanding (MoU) for implementing the Bangladesh-Bhutan-India-Nepal (BBIN) Motor Vehicles Agreement (MVA) that is aimed at boosting regional trade and connectivity.

The BBIN connectivity project was conceived after the South Asian Association for Regional Cooperation failed to agree on a regional motor vehicles agreement at a summit in Nepal in 2014.

The BBIN project suffered a setback in 2017 when Bhutan temporarily opted out of it after being unable to get parliamentary approval for the MVA. The three other countries decided at the time to press ahead with the agreement.

The MoU to be signed by India, Bangladesh and Nepal to implement the BBIN MVA was finalized at a meeting held in New Delhi during 7-8 March. Bhutan participated in the meeting as an observer. The MoU was finalized "pending ratification of the MVA by Bhutan", according to India's external affairs ministry.

The BBIN Motor Vehicles Agreement for the Regulation of Passenger, Personal and Cargo Vehicular Traffic between the four countries was signed during a transport ministers' meeting in Thimpu on 15 June 2015. Bhutan had earlier given its consent for the entry into force of the MVA among the other three countries, without any obligation to itself, pending the completion of internal procedures for ratifying the agreement. *(https://www.hindustantimes.com/, 09.03.2022)* ■

Afghanistan launches National Trade Policy

THE Government of Afghanistan launched an initiative to spur growth and create jobs by boosting the export capacities of the country's private sector, to trade with regional and global markets.

Afghanistan's Minister of Industry and Commerce Ajmal Ahmady said: "This national trade policy takes centre stage in transforming the direction of the economy's productive sectors toward producing and exporting high value-added products so that the country's full export potential can be realized. The policy document outlines the key principles and strategies that will guide the Afghanistan's strategic integration into global markets."

The Afghan Government anticipates that the policy will support the Afghanistan National Peace and Development Framework—the country's overarching policy strategy—and implementation of its WTO commitments, National Export Strategy, National Priority Programme on Private Sector Development, and national export targets. *(https://intracen.org/, 13.02.2022)* ■

Pakistan rules out trade with India

With a change in the federal government, the Ministry of Commerce (MoC) has ruled out the possibility of a resumption of stalled bilateral trade with India.

The response came from the commerce ministry over the widespread speculation on social media that the new government led by Prime Minister Shehbaz Sharif is considering a proposal to resume trade with India.

There is no change in Pakistan's policy on trade with India, an official announcement from the commerce ministry said.

On 19 August 2019, Pakistan formally downgraded its trade relations with India to the level of Israel, with which Islamabad has no trade ties at all. In reaction to India's decision to revoke Article 370 of its constitution, Pakistan has downgraded diplomatic relations with India and now suspended bilateral trade with it.

In March 2021, the Economic Coordination Committee announced it would allow the private sector to import 0.5 million tonnes of white sugar from India and cotton via the Wagah border. However, the decision was reversed within days following severe criticism from the main opposition parties—PML-N and PPP—who are now in a coalition government.

The National Security Policy launched by the former PTI government earlier in January had suggested development of trade and business ties as part of its focus on economic diplomacy and peace in the neighbourhood. *(https://www.dawn.com/, 12.05.2022)* ■

Case for intraregional investment integration

Low levels of intraregional trade and investment indicate the presence of significant unexploited development potential in South Asia. Enhanced knowledge connectivity and intraregional investment could unlock these potentials, according to a study on intraregional investment in South Asia.

The report 'Regional Investment Pioneers in South Asia: The Payoff of Knowing Your Neighbors', authored by Sanjay Kathuria, Ravindra A. Yatawara, and Xiao'ou Zhu and published by the World Bank, explores South Asia's regional knowledge connectivity and information barriers. A follow-up to the 2018 'A Glass Half Full: The Promise of Regional Trade in South Asia', this study focuses on intraregional investment through an outward investment lens to look into the suboptimal level of economic engagement within South Asia.

The report emphasizes the role of knowledge connectivity and information barriers in the decision to export or invest. It also draws attention to the distortionary outward investment arrangements in South Asia that restrain countries' dynamic firms and restrict regional value chains. Given trade-investment links, improving regional foreign direct investment (FDI) will also improve regional trade. Improvements in trade also come through FDI's role in developing regional value chains in low-trust environments and its scope for trust building in the longer term. Finally, regional engagement can provide a springboard for a more global push in both trade and investment.

South Asia shows weak performance relative to other low- and middle-income economies in other regions in attracting global FDI. The region is home to only 1.3 percent of the global stock of inward FDI (IFDI) of US$39.5 trillion as of 2017, despite producing more than 4 percent of global gross domestic product (GDP). The South Asian intraregional stock of investment is low (US$3 billion) and intraregional trade is 5-6 percent of the total trade and less than a third of its potential. South Asia ranks lowest among developing regions in intraregional investment as a share of total regional inward investment stocks (0.6 percent) or total regional outward investment stocks (2.7 percent). Almost 75 percent of intraregional investment funds flow from India, but this amount accounts for only 2 percent of India's total outward investment and is at least six times lower than Indian investments in Sub-Saharan Africa. However, for the next-largest outward investors, Sri Lanka and Pakistan, the region is a more important destination, accounting for 26 percent and 19 percent, respectively, of total national outward investments. Bhutan and Nepal register the lowest amount of outward investment.

Based on an in-depth survey of 1,274 firms across the eight countries of South Asia, the report finds limited and polarized knowledge connectivity and low bilateral trust. The report brings fresh insights into the analysis of South Asian regional engagement through its focus on South Asian multinational enterprises and the role of knowledge connectivity in South Asia. The report establishes the importance of knowledge connectivity for intraregional investment and identifies policies for addressing information barriers and network frictions. Similarly, it finds that distortions in the region's investment policies persist, particularly in outward FDI (OFDI) regimes. Apart from India and Sir Lanka, OFDI policies in South Asia are restrictive, discretionary, or nontransparent. Region-specific policies exist in both inward and outward investment arrangements. IFDI regimes in the region have undergone relatively more liberalization than OFDI regimes. Still, there are challenges like arduous dispute resolution mechanisms, restrictions on land ownership, and sector-specific restrictions.

The report's recommendations are organized around enhancing knowledge connectivity, boosting physical connectivity and digital connectivity, establishing regulatory and promotional policies for outward FDI, implementing inward FDI promotion strategies, incorporating emerging global business practices into policymaking, and identifying national policy reforms that may have regional implications.

The basis for a deeper level of regional engagement exists, fueled by the links between trade, investment, and connectivity. Building on this foundation can help South Asian countries bridge the gap between current and potential opportunities for regional engagement, increase global competitiveness, and diversify the risks that have become embedded in the global environment. ■

This is excerpted from the World Bank report 'Regional Investment Pioneers in South Asia: The Payoff of Knowing Your Neighbors.'

Pakistan's economic update

Achieving a GDP growth rate beyond 4 percent is fraught with macroeconomic risks for Pakistan unless industrial capacity is enhanced.

Vaqar Ahmed and Hammad Haider

In the fiscal year 2021-22 (FY22), Pakistan recorded its highest GDP growth rate—5.97 percent—in recent years.[1] At the same time, Pakistan also encountered macroeconomic challenges with regard to current account deficit, inflation, forex reserves and so on. Although the above statements sound irreconcilable, they make historical sense in Pakistan's case. The economic engine overheats every time a government tries to prime the economic pump with imported capital and goods as it cranks up inefficient public spending to boost domestic demand. Achieving a GDP growth rate beyond 4 percent, therefore, is fraught with macroeconomic risks unless industrial capacity is enhanced.

Between June 2021 and June 2022, the economy's fundamentals have taken a 180-degree shift. When the previous government presented a pro-growth budget in June 2021, the economy was in a healthier place, thanks to strong external buffers and robust domestic demand despite the pandemic. A year later, the macroeconomic crisis worsened so much that the new government had to opt for 'demand destruction' measures and take urgent steps to avoid a sovereign default.

The core reason for the economic unravelling is the deterioration in the external account, led by a massive expansion in dollar-based imports amid a global commodity price spiral, higher local demand despite diminishing purchasing power, and increased foreign debt repayments. The State Bank of Pakistan (SBP) is struggling to finance the current account deficit through debt-based forex reserves, as growth in remittance inflows and export proceeds were no match for imports. This led to a weakening of the Pakistani Rupee (PKR), adding to inflationary pressures. Meanwhile, the government's fiscal scorecard was in deep negative this year, after the previous government took politically expedient decisions to provide unaccounted-for subsidies on petrol, diesel and power.

Be that as it may, it appears that the crisis of confidence may now be reducing among external stakeholders. The government has been trying hard to resume International Monetary Fund (IMF)'s US$6 billion program so that the remaining US$3 billion from that loan as well as other multilaterals' financing can be unlocked. The Fund did not signal progress until fuel and power subsidies were zeroed down and administered prices brought to a level on a par with market rates. As the new government initially dithered on tough decisions, the IMF did not seem to share the government's urgency.

The IMF cleared the combined seventh and eighth programme reviews in August 2022 and agreed to an immediate disbursement of loans worth US$1.1 billion.[2]

External players have lately been uncomfortable despite GDP growth (for instance, the World Bank upgraded Pakistan's GDP growth forecast by 90 basis points to 4.3 percent for 2022)[3]—they are looking at cash flows of the country (dollar-based inflows, to be precise) and solvency. Pakistan requires at least US$36 billion in fresh external financing (a small part of which is rolled-over loans) to fully meet its debt obligations and finance the current account deficit in FY23. With inflows from China now credited to the central bank and the IMF's disbursement, Pakistan is on course to arrange the required external financing.


Pixabay

In that context, the recent development of the Financial Action Task Force (FATF) is a good omen, as the global watchdog has indicated that Pakistan is on a path to be taken off the list of countries that are subject to 'enhanced monitoring' of their legal and institutional frameworks.[4]

Current account challenge

Despite several import-restricting measures and higher taxes and duties on imports that have made imports much more expensive in rupee terms, the pressure on the external account refused to abate as of June 2022, making it the 18th consecutive month of external deficit. Only a rise in exports could neutralize a third of the increase in imports.

Pakistan's goods imports had reached US$72.3 billion in 11MFY22 (the first 11 months of FY22), growing by 45 percent year-on-year.[5] That's an additional import of US$22 billion over these 11 months relative to the same period last fiscal. Key drivers of this phenomenal growth include the doubling of oil imports to US$20 billion in 11MFY22. The additional US$10 billion in oil import was mostly due to a massive increase in international oil prices (due to the Russian invasion of Ukraine, and due to strong global demand). In addition, imports under the 'agricultural and chemicals group' also grew by 59 percent year-on-year. This was mainly due to commercial imports of vaccines for COVID-19 as well as high international fertilizer prices. Imports under the 'machinery group' category increased by 17 percent year-on-year in 11MFY22 to reach US$10.33 billion and a 55 percent annual increment was recorded in the transportation sector, which reached US$4 billion in 11MFY22.

Pakistan's goods exports witnessed strong double-digit growth in all 11 months of FY22. As per the payment-based central bank data, merchandise exports had reached US$29.33 billion in 11MFY22, showing a yearly growth of 27 percent.[6]

The 'textile group' made up 60 percent of total exports as these exports increased by 28 percent year-on-year to reach US$17.6 billion. Textile exports increased due to rising prices of cotton-based products internationally as well as higher volumetric exports of readymade garments, bed-wear articles, towels and cotton cloth. 'Food group' exports rose by 24 percent year-on-year to reach US$4.9

billion in the review period. On top was rice, where better international prices and higher volumetric exports both helped to provide a 23 percent annual growth to take overall rice exports to US$2.3 billion. Double-digit growth in export quantities of oil seeds, nuts, spices, tobacco, etc. also helped to raise the export tally.

While official workers' remittances continue to provide significant support to the country's balance of payments, the growth momentum cooled in FY22. Inflows had clocked US$28.4 billion during Jul-May FY22, growing by 6 percent year-on-year.[7] That's an addition of US$1.67 billion compared to the same period last fiscal. However, the 6 percent growth rate pales in comparison to the 29 percent growth rate seen earlier.

In relative terms, Pakistan saw the largest growth in remittance inflows from EU countries. Inflows from these countries collectively grew by 25 percent year-on-year in 11MFY22 to reach US$3.07 billion. Among large-sized remittance origins, the United States came in second, posting a 19 percent yearly growth to reach $2.78 billion in 11MFY22. The Gulf region presented a mixed trend. On the one hand, inflows from Saudi Arabia grew only 0.3 percent year-on-year to reach US$7.05 billion and proceeds from the UAE declined 5 percent year-on-year to reach $5.33 billion. On the other hand, inflows from other GCC countries (Bahrain, Kuwait, Qatar and Oman) grew by 9 percent to reach US$3.29 billion.

These vital inflows are being overshadowed by the massive trade deficit on account of galloping imports. In addition, annual remittance growth has decelerated to single digits in FY22. And there are signs that annual growth in inflows may further decrease in FY23.

The foreign investment scorecard continues to disappoint. The net foreign direct investment (FDI) was at US$1.59 billion in Jul-May FY22, down by 5 percent year-on-year (lower by US$82 million).[8] The deterioration was despite a notable decline in FDI outflows, as FDI inflows went down by double digits, too.

Pakistan's debt liabilities

As of the end of March 2022, Pakistan's total debt and liabilities increased by 18 percent year-on-year since March-end 2021 to reach PKR 53.5 trillion.[9] As of March-end 2022, 83 percent of the country's total debt and liabilities were accounted for by the public sector (almost the same as 84 percent seen in March 2021). This gross public debt increased by 17 percent in the year to March 2022, reaching PKR 44.3 trillion in stock. It is estimated that this level is about 70 percent of GDP, thus violating the 60 percent ceiling under the Fiscal Responsibility and Debt Limitation Act (2005).

The federal government's domestic debt crossed PKR 28 trillion at the end of March 2022, rising 10 percent year-on-year. The bulk of the growth in this period was accounted for by higher issuances of government securities to banks (Pakistan Investment Bonds), further issuance of Ijara Sukuk bonds and the central bank's lending to the government against SDR allocation, whereas there was a net retirement of treasury bills by the government.

The external debt of the government jumped 32 percent year-on-year to reach PKR 14.9 trillion at the end of March 2022.

Conclusion

Pakistan's economy entered a new fiscal year in July 2022 after getting beaten black and blue in FY22 by macroeconomic vulnerabilities, which were induced by surging international commodity prices amidst robust domestic demand that was being increasingly met by imported products. Those pressures were exacerbated by imprudent fiscal policy at home, delayed monetary adjustments by the central bank in the early months of FY22, expedient economic decisions by the previous government and heightened political instability since March. The new government took over in mid-April; however, it could not subdue chatter about early elections, which further complicates the pathway towards economic stability. The Shehbaz government seems to be slowly gaining strength, which may help with orderly political transition and economic certainty late next year. ■

Dr. Ahmed is Joint Executive Director and Mr. Haider is consultant at the Sustainable Development Policy Institute of Pakistan, Islamabad.

Notes

1 Ministry of Finance. 2022. *Economic Survey of Pakistan (2021-22)*. Finance Division, Government of Pakistan.

2 IMF. 2022. IMF Executive Board Completes the Combined Seventh, and Eighth Reviews of the Extended Fund Facility for Pakistan. https://www.imf.org/en/News/Articles/2022/08/29/pr22293-imf-executive-board-completes-reviews-of-extended-fund-facility-pakistan.

3 World Bank. 2022. *Global Economic Prospects*. Washington, DC: World Bank.

4 Financial Action Task Force. 2022. *Jurisdictions under Increased Monitoring - June 2022*. https://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/documents/increased-monitoring-june-2022.html#pakistan.

5 Pakistan Bureau of Statistics. 2022. "Imports of selected commodities during the period Jul-May 2021-22." https://www.pbs.gov.pk/sites/default/files/external_trade/monthly_external_trade/2022/may-2022/Import_May_2022.pdf.

6 State Bank of Pakistan. 2022. "Export Receipts by Commodities and Groups – May 2022." https://www.sbp.org.pk/ecodata/Export_Receipts_by_Commodities_and_Groups.pdf.

7 State Bank of Pakistan. 2022. "Country-wise Worker Remittances (Jul-May FY22)." https://www.sbp.org.pk/ecodata/Homeremit.pdf.

8 State Bank of Pakistan. 2022. "Summary of Foreign Investment in Pakistan (Jul-May FY22)." https://www.sbp.org.pk/ecodata/Netinflow-Summary.pdf.

9 State Bank of Pakistan. 2022. "Pakistan's Debt and Liabilities (as of March 2022)." http://www.sbp.org.pk/ecodata/Summary.pdf.

Sri Lanka's multidimensional crisis
Impacts on vulnerable groups

The road to recovery is not easy. It is imperative that the limited fiscal resources are not wasted. Initiatives must be implemented with care, especially in terms of beneficiary identification.

Ganga Tilakaratna and Lakshila Wanigasinghe

The COVID-19 outbreak, which was declared a global pandemic by early 2020, managed to alter the course of the global population. In addition to the millions of lives lost, the pandemic also disrupted economies worldwide, and Sri Lanka was no exception. However, unlike most others, Sri Lanka was hit by added challenges as the country fell into an economic crisis just as it was on the road to recovering from the pandemic. This has placed both the economy and the population under extreme stress with no immediate resolution in sight. Against this backdrop, this article aims to examine the effects of COVID-19 on the poor and vulnerable, how the current crisis came to be and the ways in which it has affected the lives and livelihoods of the Sri Lankan people.

Effects on the poor and vulnerable

As with the rest of the world, COVID-19 adversely impacted all aspects of the Sri Lankan economy and its people. However, the poor experienced these difficulties by a much higher degree. Their pre-existing vulnerabilities put them at greater risk of facing more significant challenges for prolonged periods of time. These groups experienced multiple impacts on various aspects of life such as employment, income, consumption, health, and education.

COVID-19 managed to diminish the country's employment levels as well as reduce the quality of work. The reductions in employment levels were prevalent in the services and industry sectors. The impact on service sector jobs is understandable as many services cannot be performed remotely; however, lockdowns and other travel restrictions imposed to curb the spread of the virus obstructed workers from commuting to jobs. Further, during this time the concept of remote working was fairly new in Sri Lanka and therefore neither organizations nor employees were adequately prepared for it. While the pandemic impacted occupations across all sectors to a certain degree, these adversities were greater for low-income families, informal sector workers and women. For instance, COVID-19 largely impacted individuals engaged in the tourism and hospitality sectors as global restrictions on foreign travel imposed during this time led to a drastic drop in tourist arrivals. Individuals engaged in informal work were affected by the inability to travel, both among and within cities.

Pixabay

The pandemic's impact on women cannot be ignored. Comparison of the employed population between the fourth quarter of 2019 and 2020 show that more females have experienced job losses during the pandemic than males. Evidence suggests that a disproportionate share of garment factory workers (a position that is mainly occupied by women) were impacted during the second wave of COVID-19 in Sri Lanka, which began in October 2020. Since Sri Lanka already has a comparatively low female labour force participation rate, pandemic-induced job losses are bound to increase the existing gender gaps in the labour force.

Although formal sector workers and other middle-high income earning individuals have suffered adversities due to the pandemic, the poor and vulnerable are more likely to suffer from severe consequences. This is owing to the country's considerably high share of informal sector workers (around 68 percent) and the absence of any official unemployment insurance schemes to protect them from shocks (unlike formal sector employees). For low-income households, job losses imply a direct hit to their household incomes since many poor families solely rely on their occupation-related earnings due to the lack of alternate modes of income. Hence the higher level of job losses during the pandemic among low-income families, informal sector workers and women are a likely indicator of significant increases in COVID-19-induced poverty.

Estimations by the World Bank using pre-pandemic data suggest that a 10 percent drop in consumption levels can increase the poverty rate (at US$ 3.20 a day poverty line) from 11 percent to 15.5 percent. It further reveals that a considerably large share of households exist just above the poverty line and the pandemic is likely to have pushed them into poverty. In fact, nearly 500,000 individuals are projected to have fallen into poverty resulting from COVID-19-instigated job and income losses. As of 2020, the pandemic is projected to have doubled extreme poverty from its 2019 levels. Therefore, in addition to the pandemic leading to a higher number of poor individuals, it has also pushed the existing poor deeper into poverty, thereby leading to both a deepening and widening of poverty levels. The rise in poverty has thus exacerbated inequalities, especially as Sri Lanka was experiencing high levels of income disparities between the rich and the poor even before the pandemic.

Sri Lanka's economic crisis

Just as Sri Lanka was coming out of the pandemic, the island was hit by a new crisis of a higher magnitude. At present, Sri Lanka is facing its worst economic crisis since independence. Hence the country's current socioeconomic standing has unfortunately gone from bad to worse.

A multitude of factors, both global and local, contributed to the prevailing economic status of the country. The Russian invasion of Ukraine caused global disruptions in oil markets leading to constant price fluctuations, which in turn hampered domestic oil supplies. Fallouts of the pandemic have impacted almost every aspect of economies worldwide. Healthcare, employment, tourism, food supply and education are a few key sectors in Sri Lanka that have faced severe adversities in this regard.

While global disruptions have undoubtedly contributed to worsening the economic standing of the country, the root causes of the crisis can be attributed to several shortsighted policies adopted by local policymakers in the recent past. The prevailing economic situation is an amalgamation of a number of unfavourable factors that Sri Lanka has been facing over the past few years. The country has been dealing with a continuous series of

Figure 1 **Adverse effects of the economic crisis**

Source: Central Bank of Sri Lanka, 2022

misfortunes since the Easter Sunday bombings in 2019, followed by the COVID-19 pandemic, and now an economic crisis.

Politically motivated tax cuts that were introduced in 2019 contributed to large declines in government revenue, which in turn widened the pre-existing budget deficit. This was followed by the unexpected outcomes of COVID-19 such as financing emergency healthcare needs and drastic drops in tourist income. Apart from this, a ban on chemical fertilizer imports was introduced in early 2021 in an attempt to minimize import. This policy was counterproductive as it led to a drop in domestic crop production and consequently rice had to be imported to make up for production losses. Although this policy has since been reversed, its consequences continue to affect local agriculture. The depreciation of the Sri Lankan Rupee against the US dollar during this time forced the Central Bank of Sri Lanka (CBSL) to print money to finance some essential expenses such as the payment of salaries for the country's large public sector workforce. The losses in government revenue coupled with mounting loan repayments on external borrowings were followed by a lack of foreign reserves in the CBSL.

Effects of the economic crisis

As Sri Lanka grapples against the worst economic crisis in the nation's independent history, its repercussions are all-encompassing (Figure 1).

In addition to the low levels of foreign exchange reserves and the inability to finance external debt repayments as discussed above, the country is currently experiencing very high levels of inflation. In the month of August 2022 headline inflation as measured by the National Consumer Price Index (NCPI) recorded at 70.2 percent in comparison to 66.7 percent in the previous month (Figure 2). This was largely driven by the rise in food inflation which was reported at 84.6 percent in August 2022 in comparison to 82.5 percent in the month of July. In terms of food, price increases were seen in fresh fish, eggs, biscuits and fruits, etc. As for non-food inflation, the transportation sector observed the highest price increase in the month of August; a likely result of fuel limitations hindering the effective functioning of both public and private sector transport.

The adversities brought on by the crisis have left citizens struggling to make ends meet, with little hope for an immediate solution. Sri Lanka ranked amongst the top five countries with the highest food price inflation as per the latest World Bank estimates. The continuous rise in the prices of everyday use food items such as rice and milk powder coupled with the lack of foreign exchange for food imports poses a real threat to food security in Sri Lanka. Further adding to this problem is the drop in domestic agricultural production by almost 50 percent due to shortages in fertilizer. Findings reveal that nearly 6.26 million people in the country are currently dealing with food insecurity. Most families suffering from food insecurity are likely consuming less food and not meeting the recommended daily calorie intake. These factors are bound to have long-term repercussions on the health of the population, especially among children (malnourishment, stunting, etc.).

Insufficient fuel supplies and the rising cost of fuel have made transportation a costly affair for the general public. In addition, the regularly scheduled power outages are hindering business operations, especially those of small business owners. Further, the limiting of imports into the country has drastically affected people's consumption and non-consumption-related purchases, thus, leading to lifestyle changes along with a drop in the general standard of living for most Sri Lankans.

Impacts on poverty and vulnerability

The economic crisis has exacerbated the adversities caused by the COVID-19 pandemic. As previously mentioned, the ongoing crisis has led to job and income losses, food insecurity and an overall loss of livelihoods. The alarming rates of inflation have drastically reduced the standard of living. Although it is still too early to accurately measure the effects of the crisis, it is clear that it has impacted the poor and the vulnerable the most. As with any adverse shock, they are most likely to bear the brunt of the burden in this instance as well.

As for the country as a whole, the economic crisis implies further backsliding on the progress made towards poverty alleviation. Poverty is expected to further increase in 2022 following the already estimated rise in poverty levels due to the pandemic. This will likely give rise to greater income inequalities. The degree of intensity of these effects are yet to be understood as Sri Lanka's economic crisis is ongoing and its long-term effects can only be seen in due course.

Way forward

In order to overcome the current economic crisis, several measures must be adopted. These include a series of initiatives targeting multiple segments of the economy, including certain changes at the policy level.

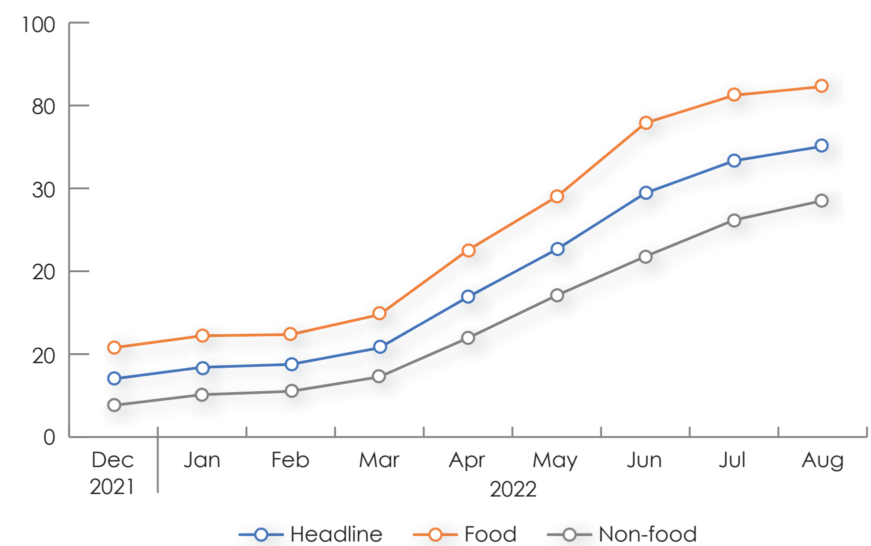
Achieving public debt sustainability is an important fiscal aspect in this regard. This requires drafting a feasible, long-term action plan for Sri Lanka to follow through in the upcoming years. Further, external debt restructuring and seeking support from the International Monetary Fund to ensure smooth progress in this regard are vital. Such measures will help Sri Lanka regain investor confidence and encourage foreign exchange inflows. Attracting new investments into the country will help with building up the much-needed foreign currency reserves and managing the supply of essential commodities such as food and fuel. Steps must also be taken to minimize government spending to narrow the prevailing budget deficit. This includes structural reforms in state-owned business enterprises, cutting down on unnecessary expenses and implementing measures to increase government revenue. Further, initiatives must be put in place to restore price stability and curb inflation, especially in relation to the current high levels of food inflation.

While action needs to be taken to overcome the ongoing economic crisis, it is also vital to extend support for citizens to cope with the crisis. In this regard, special attention must be directed towards the poor and the vulnerable. Thus, it is essential to utilize existing safety nets to provide targeted relief to the poor and the vulnerable. However, given Sri Lanka's present financial standing, it is imperative that the limited fiscal resources are not wasted. Hence, initiatives must be implemented with care, especially in terms of beneficiary identification. Thus, any cash or in-kind transfer initiatives should first and foremost focus on the poorest and most vulnerable groups in society. This would require officials to make tough choices and ensure targeting errors are minimized. When providing assistance, it is also important that groups are sufficiently supported for an adequate amount of time, instead of through one-time initiatives that are ineffective given the volatility and length of the crisis.

The road to recovery does not look easy. Improvements need to be made on all fronts in order to boost the overall economy. As such, Sri Lanka is looking at a long and tough journey ahead. While the effects of the current economic crisis may not be completely reversed, some form of relief can be expected for the people and the economic standing of Sri Lanka in the upcoming years if a corrective course of action is followed. ■

Dr. Tilakaratna is Research Fellow and Head of Poverty and Social Welfare Policy Research and Ms. Wanigasinghe is Research Officer at the Institute of Policy Studies of Sri Lanka (IPS), Colombo.

Figure 2 Consumer price inflation (Y-o-Y percentage change), 2022

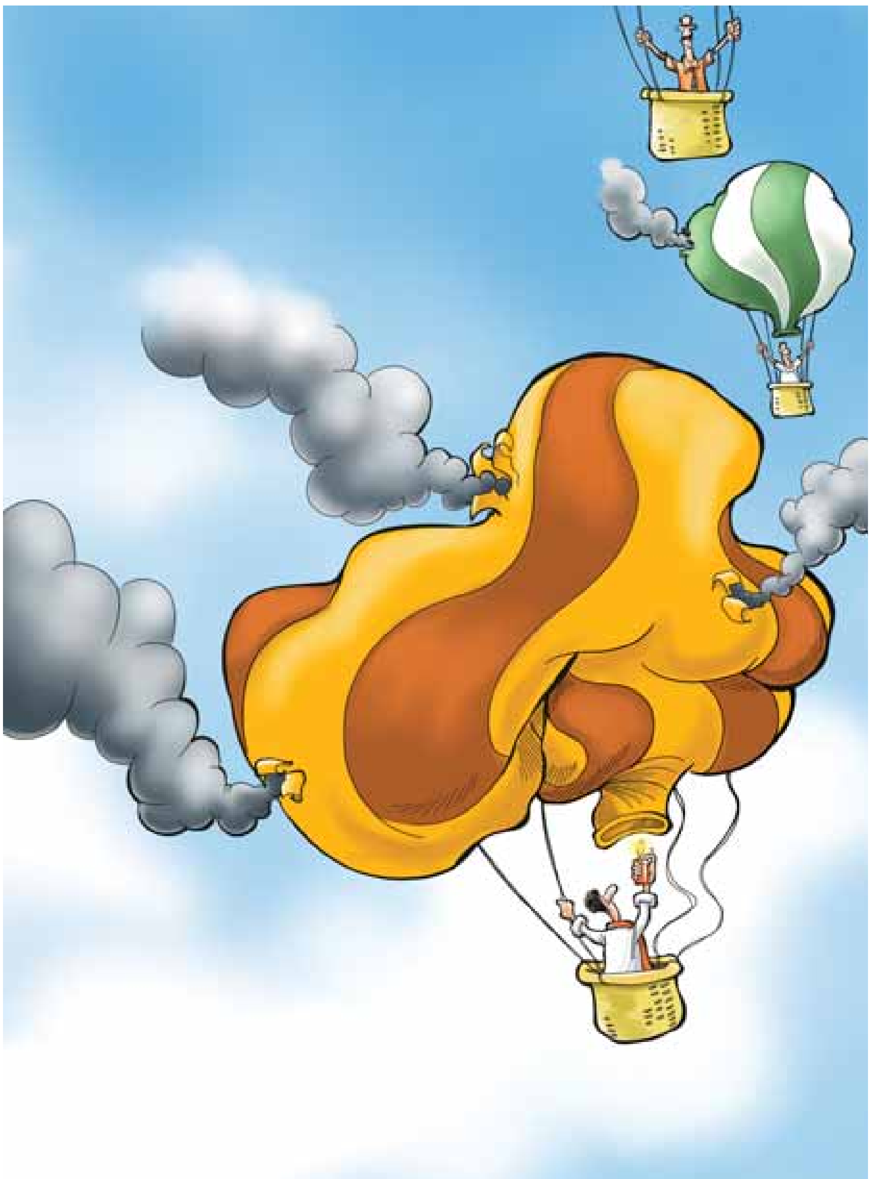


Source: Central Bank of Sri Lanka, monthly press releases

Notes

1. Arunatilake, N., and Ranasinghe, S. 2021. Pandemics and the New Normal: Sri Lanka's Labour Market. In *Sri Lanka State of the Economy 2021.* Colombo: Institute of Policy Studies of Sri Lanka.
2. Madurawela, S. 2021. Female Employment: Ensuring Gender Equality Beyond the Pandemic. In *Sri Lanka State of the Economy 2021.* Colombo: Institute of Policy Studies of Sri Lanka.
3. UNESCAP. 2021. *Impact of the COVID-19 pandemic on the SDGs in Sri Lanka and the potential for regional cooperation.* ESCAP South and South-West Asia Office.
4. *ibid.*
5. World Bank. 2021. *The COVID-19 Impact on Livelihoods and Poverty in Sri Lanka.* World Bank.
6. Weerakoon, D. 2022. Sri Lanka's crisis of legitimacy. *East Asia Forum,* 16 July 2022.
7. Wijesinghe, A., & Yogarajah, C. 2022. Sri Lanka's Food Crisis: What is the Role of Imports? *Talking Economics,* Institute of Policy Studies of Sri Lanka.
8. *ibid.* Note 6.
9. Central Bank of Sri Lanka. 2022. Inflation in August 2022 - NCPI. Colombo: Central Bank of Sri Lanka.
10. World Bank. 2022. *Food Security Update.* Washington, DC: World Bank.
11. *ibid.*
12. WFP. 2022. *WFP Sri Lanka Situation Report.* Colombo: World Food Programme.
13. Tilakaratna, G., and Seneviratne, B. 2022. Crises and Recovery: Meeting the 2030 Agenda on SDGs. In *Sri Lanka State of the Economy 2022.* Colombo: Institute of Policy Studies of Sri Lanka.
14. Central Bank of Sri Lanka. 2022. *Annual Report 2021.* Colombo: Central Bank of Sri Lanka.

South Asia in distress



The economic woes of four South Asian countries emanate from different sources, generating lessons for the developing world.

Ranjan Sapkota

With the after effects of the COVID-19-induced disruptions interacting with the fallout from the war in Ukraine, countries across the world are facing economic turmoil in one form or the other. South Asian economies are no exception. Sri Lanka is submerged in an unprecedented crisis, caused in no small measure by economic mismanagement. Pakistan is struggling with a large current account deficit and a high public debt while Bangladesh is also in a precarious situation brought about by strained public finances and foreign exchange reserves. Both Pakistan and Bangladesh have approached the International Monetary Fund (IMF) for loans to tide them over their economic difficulties. Nepal's economy is plagued by shrinking foreign reserves.

South Asia's economy, as measured by gross domestic product (GDP), shrunk in the year 2020 on the back of a reduction in economic activities caused by the pandemic.[1] World Bank data show GDP in all the countries in South Asia fell, except for

Bangladesh, in 2020. The economic performance of the region seems to be improving as the GDP growth forecast for the next couple of years is about 5.8 percent.[2] However, Sri Lanka's prospects are expected to remain dire as the island country's economy is estimated to contract by 9.2 percent in the fiscal year 2022 (FY22) and continue to shrink in FY23. South Asian countries are facing economic challenges in different forms. But four countries—Bangladesh, Nepal, Pakistan and Sri Lanka—are facing economic troubles that are similar in nature. Although their troubles vary in degrees, widening current account deficits, depleting foreign exchange reserves, high or increasing public debt and rising inflation are some of the common issues tormenting these economies. This article will focus on these four economies.

Sri Lankan crisis

Once seen as the model nation of South Asia, Sri Lanka has lately turned into a cautionary tale. Sri Lanka had never experienced a crisis like this one in its 74-year history since its independence, as its economic crisis turned into a full-blown social and political crisis. By May 2022, the economy was in such a bad state that the country did not have sufficient foreign exchange reserves to even pay for its imports and service its debts. Exogenous shocks also played a part but Sri Lanka's current mess is largely a result of a series of policy missteps and corrupt governance. Haphazard policies, such as tax cuts, and increased public spending, largely caused by the COVID-19 pandemic, led to large fiscal deficits. Unsustainable monetary expansion to pay for the deficit in public finances, and difficulties in sovereign debt servicing caused the Sri Lankan rupee to crash. A global rise in fuel and food prices created a cost-of-living crisis.

Sri Lanka was staring at difficult times even in 2019, before the outbreak of the pandemic. The 2019 Easter terrorist attack and the COVID-19 pandemic badly affected tourism revenue—one of the major sources of foreign exchange. Tourism earnings contributed to 5.6 percent of Sri Lankan GDP in 2018, which dropped to 0.8 percent in 2020.[3] Similarly, remittance income—another major source of foreign exchange—fell. The average monthly remittance income, which was US$560 million in 2019, declined to US$458 million in 2021 and further slid to US$293 million in 2022.[4] Although Sri Lankan exports recovered from the slump caused by the pandemic, it was not enough to compensate for the drop in remittance and tourism earnings.

In a bid to prop up the economy, the government took short-sighted decisions with devastating results. With the intention of reducing imports and promoting organic farming, in April 2021, the government decided to ban the import of chemical fertilizers. The policy backfired spectacularly as the overall food production in 2021 was estimated to have declined by about 40-50 percent compared to the previous year.[5] By September 2021, the Sri Lankan government had to declare a state of emergency over food shortages. Production of tea—a major cash crop and export product—slipped to its lowest level in the last 26 years.[6] The need to import food products even as exports plunged added to the pressure on the declining foreign exchange reserves.

The situation deteriorated so much that in May 2022 Sri Lanka defaulted on its loans for the first time in its history.[7] By that time, Sri Lanka was seeking to restructure debts of more than US$50 billion it owed to foreign creditors. Loss of confidence in the international credit market, and rampant shortages and inflation at home triggered a political crisis. After weeks-long protests across the country, the government was forced to resign. Public hatred of the governing class was evident from the public storming of the presidential residence.

Pakistan's precarious situation

The COVID-19 pandemic, the depreciating Pakistani rupee and the country's large debt servicing needs had squeezed Pakistan's finances, especially its foreign exchange reserve, by 2022. Anticipating a political crisis at hand, the government attempted to win over the public with a few populist decisions that further strained the economy. One such example is the government reducing petrol prices and electricity tariffs at the end of February 2022 in the midst of the rise in oil prices across the globe as Russia invaded Ukraine. The move was estimated to cause a loss of around US$2.1 billion to the state coffers. It not only made government finance unsustainable but also endangered Pakistan's IMF rescue programme. The opposition party was on the verge of tabling a no-confidence vote against the government. A new government had to roll back the subsidy as it sought the release of a US$1.1 billion tranche of loans from the IMF.[8] Unprecedented floods in June further worsened the economic position. The loss and damage caused by the floods is estimated at about US$30 billion, with reconstruction needs amounting to over US$16 billion.[9] By the end of 2022, the country's central bank announced that it only had enough foreign reserves to meet three weeks of imports.[10]

Other countries nearing crisis

The economic situation in Bangladesh and Nepal is not as bad as that in Sri Lanka and Pakistan, but both the least developed countries are facing a pressure on foreign exchange reserves. Unlike Sri Lanka and Pakistan, these two countries' economic stress cannot be immediately traced to populist political moves. Bangladesh's foreign exchange reserves fell to US$39.67 billion as of mid-July 2022—sufficient for imports for more than five months—from US$45.5 billion a year earlier. During that period workers' remittance had also dipped by 5 percent, while the Bangladeshi taka depreciated against the US dollar, adding to the pressure on forex reserves.[11] In May, to arrest the dip in forex reserves, the Bangladeshi government announced a series of policy decisions that tightened the rules on imports of goods deemed luxury items such as sports utility vehicles, washing machines, air conditioners and refrigerators. In addition, a temporary ban on foreign tours of government employees was also imposed. The strain on forex reserves prompted Bangladesh to seek loans from the IMF.

The situation in Nepal was no better as declining forex reserves forced the government in April 2022 to ban the import of products such as all kinds of readymade liquor (excluding raw materials), readymade cigarettes and tobacco products, snacks like potato chips, cars, high-powered motorcycles, expensive mobile phones, among others. Likewise, traders were required to deposit 100 percent of the import amount with banks to open a letter of credit for imports of some more products. The ban was extended till December 2022. The ban was prompted by Nepal's foreign exchange reserves depleting to a level sufficient to finance only six months of imports. The plunge in reserves was the result of a ballooning trade deficit, a slowdown in remittance income, and other sources of foreign exchange such as exports and foreign direct investment unable to pick up the slack. The situation in Nepal was not crippling but rising inflation and the psychological impact of the ongoing crisis in Sri Lanka created almost a panic-like situation. Partly with an eye on the local election in May and the general election in November, the government resorted to an import ban to appear proactive in forestalling a full-blown crisis.

Untamed borrowings

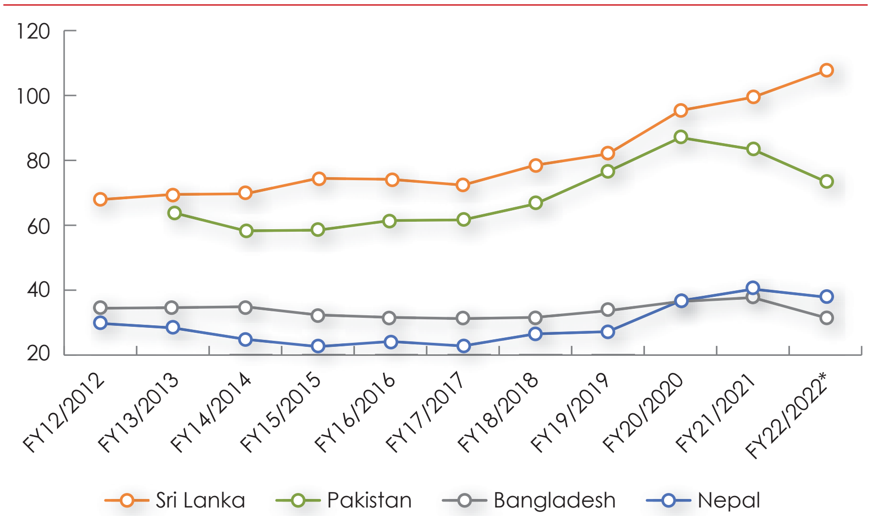
A characteristic common to several South Asian economies is high and/or rising indebtedness. This was evident in Sri Lanka and Pakistan, but was less pronounced in Bangladesh and Nepal (Figure 1).

Sri Lanka's indebtedness has risen sharply in recent years with the gross debt-to-GDP ratio reaching 130.5 percent in October 2022.[12] Generally, an emerging market with a debt-to-GDP ratio of more than 64 percent is considered to be vulnerable.[13] A study shows that with each percentage point increase above the 64 percent threshold, real GDP growth is likely to decline by 0.02 percentage points.[14] Since about 70 percent of Sri Lankan debt is denominated in US dollars, rupee depreciation worsened the situation.

A key factor behind Sri Lanka's debt distress is its significant commercial borrowings, typically characterized by high interest rates and shorter repayment periods. After Sri Lanka became a middle-income country, its ability to acquire concessionary loans from multilateral and bilateral organizations declined, which pushed it towards alternative means of financing. Sri Lanka's commercial loans were just 2.5 percent of its total external debt in 2004, which rose to 56 percent by 2019.[15] Debt distress is equally concerning for Pakistan. Its gross debt-to-GDP ratio was around 78 percent by October 2022. The Pakistani government is trying to reschedule loan repayments with its bilateral lenders. The biggest chunk of Pakistan's bilateral debt is owed to China. Of the outstanding external loans worth US$91.7 billion, Pakistan owes US$18.4 billion in bilateral debt to China and US$6.7 billion to Chinese commercial banks (the figures make up as much as 27 percent of the total foreign borrowings).[16] With the Pakistani rupee depreciating to a new low, external debt servicing requirements further strained government finances. As of November 2022, Pakistan's total external debt and liabilities remained almost unchanged at US$127 billion, but in terms of the Pakistani rupee, the liabilities increased by 23.7 percent compared to last year. Both Sri Lanka and Pakistan have borrowed heavily to finance their infrastructure spending. Some of Sri Lanka's infrastructure projects were ill-conceived and politically motivated. The debt distress in both countries has caused their bonds to be rated junk by all of the leading credit rating agencies.

According to the IMF, Bangladesh would do well to not over-borrow to fund infrastructure projects that could turn out to be white elephants. Bangladesh's debt-to-GDP ratio stood at 37.5 percent as of October 2022.[17] The country's external debt repayment requirements associated with large foreign loans are expected to increase to US$4.02 billion in 2025 from US$2.4 billion in 2022.[18] Nepal's debt-to-GDP ratio stands at 41.47 percent as of mid-July 2022.[19] Nepal, thus, has a comfortable fiscal space, although a surge in the ratio in the past several years even as capital expenditure remained sluggish is concerning. Like Bangladesh, Nepal will face a higher

Figure 1 **Public Debt (% of GDP)**



Source: Data extracted from the central banks and the ministries of finance of the respective countries.
**Provisional figures: Sri Lanka (till second quarter); Pakistan (till June); Bangladesh and Nepal (till March)*

debt burden when the grace period of concessional loans ends. However, Nepal has not taken a commercial loan yet. A joint debt review by the World Bank and the IMF had identified both Bangladesh and Nepal as having a low risk.[20]

Foreign exchange depletion

A central feature of the economic troubles in South Asian countries is a forex reserve crisis. Pakistan, Sri Lanka and Bangladesh have good enough manufacturing and export bases, but these could not compensate for the financial impacts of the exogenous shocks hitting their economies. Export earnings took a dip during the pandemic while remittances declined. Just when the countries were witnessing a resurgence of import demand, they were hit by soaring import costs in the wake of Russia's invasion of Ukraine. This was accompanied by a depreciation/devaluation of their currencies. Hence, import bills and debt service skyrocketed while exports could not adequately take advantage of the falling currencies.

Between May 2019 and May 2022, Sri Lanka's forex reserves fell by 71 percent.[21] As per the IMF's projection, Sri Lanka is most likely to operate with reserves as low as one month of import cover in the period 2022-2026.[22] Similarly, Pakistan's reserves depleted to a four-year low of US$6.1 billion in December 2022.[23] In an indication of the severity of the situation, Pakistan's increasing trade deficit and depleting reserves prompted a minister to urge the people to drink less tea.[24] Pakistan is one of world's biggest tea importers, with approximately US$400 million worth of tea consumed in the fiscal year 2021-22, an increase of US$40 million over the fiscal year 2020-21.

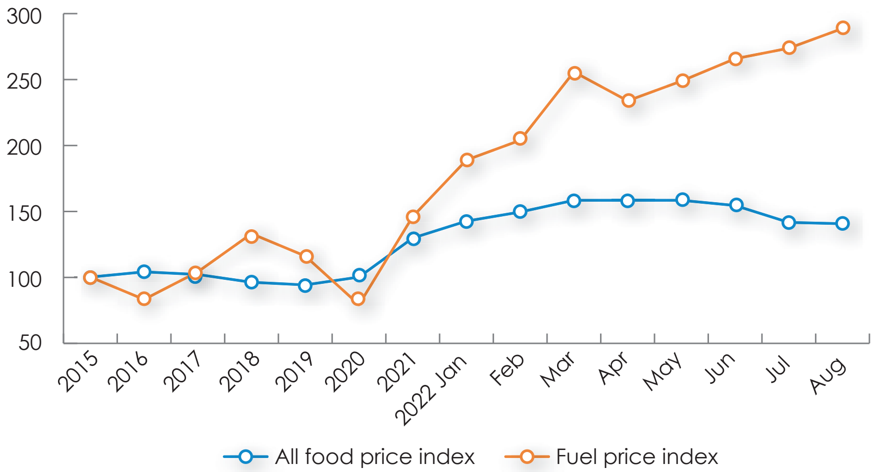
On the other side, Bangladesh was operating at a comfortable reserves position till 2021. But it saw a whirlwind decrease in 2022. Bangladesh's reserves could only support five months of imports by May 2022.[25] The value of forex reserves consistently showed a decline each month. From US$44.8 billion a year ago, it fell by 32.82 percent to US$33.7 billion in November 2022.[26] It is notable that just in August 2021 Bangladesh's reserve position had recorded its highest-ever level, by crossing the US$48 billion mark.[27] However, within a year of the impressive performance, the weakening reserves forced Bangladesh to impose restrictions on imports. Bangladesh is negotiating a loan package of US$4 billion with the IMF.

As for Nepal, the import ban on select goods imposed in April to rein in fast depleting forex reserves was lifted in December following pressure from the private sector. The balance-of-payments and the reserve position had improved, mainly on the back of a plunge in imports. However, due to an extremely low export base and foreign currency earnings being overwhelmingly dependent on remittances, the pressure on reserves may resurface as imports rebound.

Rising prices

A painful global economic fallout of the Russia-Ukraine war has been a spike in inflation, mainly that of food and fuel prices. The United Nations Conference on Trade and Development's All Food Price Index showed a 76-point increase from August 2021 to August 2022 (Figure 2).[26] The Fuel Price Index, which stood at 105 in January 2021, had skyrocketed to 289 by August 2022.

Figure 2 All Food and Fuel Price Index (Global)



Source: UNCTAD's Handbook of Statistics 2022.

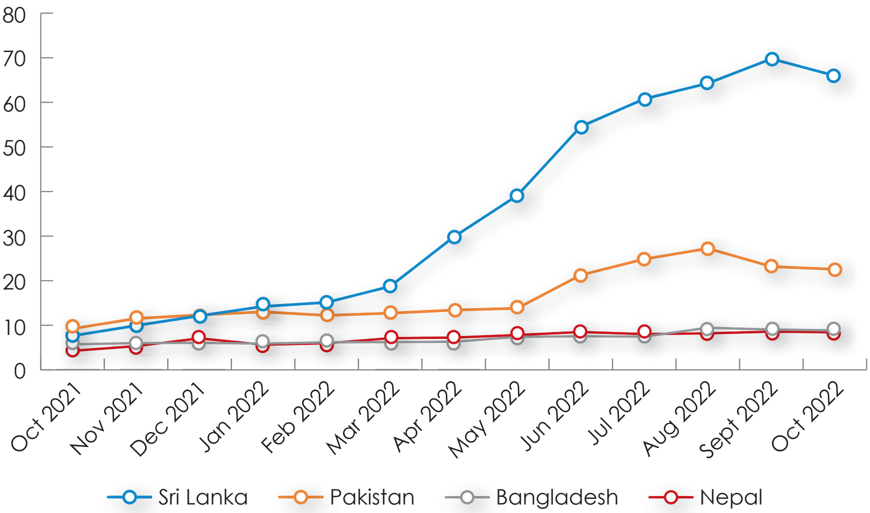
Inflation was felt severely in Sri Lanka (Figure 3). Sri Lanka's inflation has consistently increased each month over the past year. On November 2022 Sri Lanka had an inflation rate of 65 percent and it is only expected to get worse in the coming months.[29] Bangladesh and Nepal have a much lower inflation rate compared to Pakistan and Sri Lanka, but they are also facing increased inflation.

Takeaways

The situation in South Asian countries offers cautionary tales of various degrees. While Sri Lanka has struggled to remain afloat, alarm bells have rung in Nepal and Bangladesh. Although their problems appear similar—debt distress, inflation, shrinking foreign exchange reserves—the situation in each country is unique and the problems sprouted from different issues. Still, their experiences do provide some lessons for all developing and least developed countries.

The debt distress in Sri Lanka and Pakistan shows that Nepal and Bangladesh need to be cautious about excessive borrowing, even for projects that look highly attractive. Being lower-middle-income countries, both Nepal and Bangladesh can borrow at concessional rates from multilateral agencies for some more years.

Figure 3 Inflation



Source: Inflation data compiled by author from statistics available at the websites of the four countries' central banks.

Sri Lanka's situation is a result of populist policies. Populist moves such as tax cuts could garner support from the public in the short term but when things turn bad it will not take long for the very public to turn against the government. This should especially be a lesson for the to-be-formed government in Nepal following the rise of new faces in the general elections of November. Moreover, each policy decision, especially when it is likely to affect productivity, needs to be carefully examined.

All four governments' decision to ban luxurious products was not a sustainable solution. A long-term solution requires concerted efforts to encourage investment—both foreign and domestic—in sectors with high production potential and build the productive capacities needed to sustainably generate foreign currency earnings.

Approaching the IMF for an economic bailout should not be considered a shameful action, but there is always a limit to borrowing more to pay for loans. Also, countries hesitate to seek IMF funds due to stringent policy conditionalities that the Washington-based lender imposes on borrowers. Moreover, the current economic troubles show that domestic policy reforms alone may not be able to achieve a lot in the face of sudden exogenous shocks. Hence, policies need to maintain a certain buffer to tide their economies over such shocks.

Mr. Sapkota is Research/Programme Associate at SAWTEE.

Notes

1 Based on data available at the World Bank.

2 World Bank. 2022. *Migration and the Road to Resilience*. Washington, DC: World Bank.

3 Bhowmik, Soumya. 2022. "How tourism in Sri Lanka went downhill: Causes and consequences." *Raisina Debates*, *Observer Research Foundation*, 22 June 2022.

4 Central Bank of Sri Lanka. 2022. Flow of Foreign Remittances to Sri Lanka 2015–2022.

5 Singh, Sikha. 2022. "Sri Lanka waking up to reality of food shortages after failed organic farming dream." I*nsight Blog*,11 august 2022.

6 economynext. 2022. *"Sri Lanka records the lowest tea production in 26-years." economynext,* 23 October 2022.

7 Hoskins, Peter. 2022. "Sri Lanka defaults on debt for first time in its history." *BBC News*, 20 May 2022.

8 IMF. 2022. *"IMF Executive Board Completes the Combined Seventh, and Eighth Reviews of the Extended Fund Facility for Pakistan."* Press Release No. 22/293.

9 UNDP. 2022. "Pakistan: Flood Damages and Economic Losses Over USD 30 billion and Reconstruction Needs Over USD 16 billion." Press Release.

10 Dawn. 2022. "SBP's forex reserves plunge to 8-year low." *Dawn,* 22 December 2022.

11 Al Jazeera. 2022. "Bangladesh seeks $4.5bn IMF loan as forex reserves shrink: Report." *Al Jazeera,* 26 July 2022.

12 https://www.imf.org/en/Countries/LKA.

13 Caner, Mehmet, Thomas Grennes, and Fritzi Koehler. 2010. *"Finding The Tipping Point—When Sovereign Debt Turns Bad."* Policy Research Working Paper 5391, World Bank, July 2010.

14 *ibid.*

15 Moramudali, Umesh. *"Sri Lanka's Foreign Debt Crisis Could Get Critical in 2021." The Diplomat*, 9 February 2019.

16 IMF. 2022. Pakistan: 2021 Article IV Consultation, Sixth Review. IMF.

17 https://www.imf.org/en/Countries/BGD.

18 Saif, Saifuddin. 2022. "Annual external debt servicing to hit $2.5b in 4 years." *The Business Standard,* 29 April 2022.

19 PDMO. 2022. Quarterly Debt Position, 4th Quarter of FY 2078/79. Kathmandu: Public Debt Management Office.

20 IDA and IMF. 2020. Joint World Bank-IMF Debt Sustainability Analysis. World Bank and IMF.

21 Calculations based on different issues of Central Bank of Sri Lanka's Weekly Economic Indicators.

22 IMF. 2022. Sri Lanka: 2021 Article IV Consultation. IMF.

23 State Bank of Pakistan (SBP). 2022. Liquid Foreign Exchange Reserves.

24 The Guardian. *"Pakistanis told to drink less tea to help fight economic crisis." Associated Press in Islamabad*, 15 June 2022.

25 Byron, Rejaul Karim, and Zina Tasreen. *"Forex reserves under strain: Govt defers employees' foreign tours, less important projects." The Daily Star*, 12 May 2022.

26 Bangladesh Bank' Foreign Exchange Reserve (Monthly) statistics available at https://www.bb.org.bd/en/index.php/econdata/intreserve.

27 Hasina, Sheikh. 2022. *"Bangladesh's forex reserves enough to cover up to 9 months of imports: PM." The Business Standard,* 28 July 2022.

28 UNCTAD. *UNCTAD Handbook of Statistics 2022*. https://unctad.org/system/files/official-document/tdstat47_en.pdf.

29 Ministry of Finance (MoF). 2022. SriLanka. Colombo Consumer Price Index.

Swastik Aryal

On trade policy coherence & coordination

Poor coordination within and among government agencies impacts formulation and implementation of trade policy in Nepal.

Paras Kharel and Kshitiz Dahal

Promotion of industrialization and exports is a key component of Nepal's trade and industrial policy as well as other sectoral policies. However, progress in both industrialization and exports remains lacklustre. A poor state of coordination among different government agencies has been identified, including by government's policy documents such as Nepal Trade Integration Strategy, as a major impediment to the proper implementation of government's policy. A study published by SAWTEE and The Asia Foundation, "Trade Policy Coherence and Coordination in Nepal: An Exploratory Assessment", highlights some of the coordination issues.

Firstly, lack of coordination between industrial and export promotion agencies (different government agencies under the Ministry of Industry, Commerce and Supplies (MoICS)), and between them and revenue-related agencies (under the Ministry of Finance) has hindered the implementation of some of the industrial and export promotion tools such as facilities and concessions accorded to industries. Furthermore, it has fostered an environment of uncertainty among industries regarding the incentives provided by the law.

Lack of coordination has been affecting the administration of sanitary and phytosanitary (SPS) measures and technical barriers to trade, where coordination among government agencies is pivotal. Trade negotiation capacity and economic diplomacy also suffer from lack of coordination. Likewise, lack of coordination among customs and other government agencies prevents an efficient customs-clearance process, thereby increasing costs and time for traders. Lack of coordination among different government agencies has created issues in the planning and design of inland container depots (ICDs) and integrated checkposts (ICPs), rendering them unable to efficiently manage current trade flows. The apex body, the Board of Trade, is largely non-functional, unable to even hold meetings regularly. The absence of dedicated secretariat services has stymied the functioning of the board as well as other trade-related bodies.

Against the findings of the study, the following broad actions and reforms have been proposed:

- Ensure implementation of incentives provided to industries by the Industrial Enterprises Act. Moreover, ensure that the incentives provided do not erode through amendments, including through provisions in other legislation. A significant ownership of the Industrial Enterprises Act by the Ministry of Finance is necessary for the implementation and continuance of industrial incentives, which requires increased coordination between the Ministry of Finance and MoICS. Furthermore, a clear vision is needed on the government's part to balance two competing interests in the form of industrialization and government revenue, at least in the initial phase.

Pixabay

- Move away from the practice of making laws in silos. Ensure wide stakeholder participation during the law-making process so that the laws are coherent, and gain the ownership of all stakeholders, and secure necessary funds for their proper implementation. A vigorous discussion has to be carried out, for instance through the parliamentary committees, regarding implications of the law before they are implemented. All the contentious issues have to be sorted out beforehand. Once the laws are endorsed, it is an obligation of all agencies to follow them. Hence, when the Finance Act is formulated each year, the provisions made by other laws affecting it should be respected. Some sort of monitoring mechanism might be needed to ensure that there are no conflicts with provisions mentioned in other laws. This would once again require a coordinated approach from different government ministries rather than each ministry only focusing on its immediate sectors. Furthermore, a robust mechanism for the implementation of laws has to be developed.
- Ensure that the filing process for claiming facilities such as duty drawback and export subsidy is simple and transparent. Promoting electronic filing and electronic payment of the incentives may be considered.
- Formulate a clear vision with regard to the export subsidy scheme—for instance, its priorities with regard to market diversification, product diversification, export growth, etc.—and ensure that adequate fund is allocated and the scheme is efficiently implemented.
- Disseminate information to industries, for instance through publication in the ministries' website or in the website of Nepal Trade Information Portal, regarding the concessions and facilities that the industries are entitled to and the procedures for claiming the incentives.
- Ensure proper implementation of National Single Window that has recently been launched at the customs offices. More non-customs offices/other government agencies such as banks should be integrated into the national single window for an efficient customs clearance. Expedited introduction of e-payments for the payment of customs duties will also enhance the customs clearance process.
- Introduce guidelines detailing the minimum facilities and standards that must be ensured in ICDs and ICPs. Ensure effective representation and participation of customs in the process of designing ICDs

and ICPs so that the layout and facilities are adequate to meet current and future needs.

- With regard to SPS issues on the import front, having an integrated import permit system and an integrated office that hosts all the different SPS agencies would be a more efficient system. Furthermore, while Nepal's law currently does not allow it, having all the different agencies needed for customs administration under a single agency, through potential reforms in the legislative framework, can solve SPS-related coordination issues. On the export front, as SPS-related non-tariff measures in destination countries are a key obstacle to exports, the National SPS Coordination Committee should be made functional with priority.
- A Logistics Policy, being developed by the government with MoICS as the lead agency, stands to help reduce time and cost in domestic and international trade by tackling the underlying constraints in an integrated and coordinated manner. At the same time, successful implementation of this policy critically depends on good coordination. The lessons from existing trade-related institutional mechanisms should be utilized when setting up and refining an institutional mechanism for the execution of Logistics Policy. Against the failures of so many committee-style coordination institutions as well as a body chaired by the minister, formulate a clear vision on the mechanism for institutional coordination, learning from past mistakes as well as international good practices. Adequate resources—human and financial—a clear mandate and/or legislative backing are the essentials. But a commitment at the highest political level is crucial for effective operationalization of existing or proposed mechanisms.

Making the Board of Trade functional would be a key first step. This requires, first of all, holding its meetings regularly. It should be backed by a dedicated secretariat, which must be provided with adequate human and financial resources. The Board of Trade should be expanded to include yet other ministries handling sectors relevant to international trade such as tourism and civil aviation, communication and information technology, and physical infrastructure and transport. An implementation committee may be formed under the Board of Trade headed by a Secretary (Commerce and Supplies) and having as members joint secretaries or representatives of a similar level from the agencies represented in the Board of Trade. An undersecretary from MoICS, supported by a couple of section officers, can provide secretariat services to the implementation committee. The National Trade and Transport Facilitation Committee and the National Trade Facilitation Committee, which have virtually the same composition and ToR, should be turned into a single committee/body with staff specifically assigned to it. This committee could be a subset of the implementation committee. Working groups/committees could be formed under the implementation committee as per the need, and each of these should have permanent staff member(s) to provide secretariat-like services.

As there are issues on which the requisite decisions from various ministries are forthcoming only with the involvement of the prime minister, a mechanism must be instituted to enable such issues to be forwarded from the Board of Trade to a meeting chaired by the prime minister (i.e., cabinet meeting). Forming a (say, coordination) council/committee chaired by the chief secretary with secretaries of key trade-relevant line ministries as members would be one way of improving inter-ministerial coordination and of ensuring issues requiring intervention by the prime minister is brought to his/her attention. This is critical for effectively operationalizing the Board of Trade. The various bodies formed to implement Nepal Trade Integration Strategy need to be tightly linked to the Board of Trade through a robust reporting and feedback mechanism. Revitalizing the Nepal Business Forum and leveraging it in trade policy formulation and implementation also merit consideration.

While holding regular meetings is a basic necessary condition for various bodies to function well, ultimately their effectiveness depends upon discipline in terms of the meetings having clear agendas, setting targets and conducting diligent follow-ups, along with accountability of all participants

This paper has focused on coherence and coordination in the context of federal policies and federal agencies. Although many prominent instruments and activities under trade policy, such as tariffs, customs clearance, border infrastructure, regulation of foreign direction investment, standards and technical regulations and trade negotiations, fall exclusively under the remit of the federal government, subnational governments can introduce laws, policies, strategies and programmes that impact production and international trade, including exports. For example, agriculture is an area that falls under the authority of all three tiers of government, and a coordinated effort by all three is needed to set up a credible system of traceability, a tool that will help Nepali agro-forestry-based products carve out a niche for themselves in international markets. How to ensure synergy between the activities of the three tiers of government to improve export competiveness is a subject worth investigating in future work. On another front, while this paper has briefly touched upon coordination issues in economic/commercial diplomacy, this topic merits a detailed study. One fruitful line of enquiry would be to identify the institutional interventions needed to make economic/commercial diplomacy effective, including ways to ensure the participation of provincial governments in such diplomacy. ■

This is excerpted from a study report, authored by Dr. Paras Kharel, Executive Director, SAWTEE, and Mr. Kshitiz Dahal, Senior Research Officer, SAWTEE, and published by SAWTEE and The Asia Foundation.

12th WTO Ministerial Conference

Outcomes and missed opportunities

The MC12 made an important contribution to the global fight against COVID-19 by taking a decision to waive compulsory licensing for COVID-19 vaccines.

Buddhi Prasad Upadhyaya

The World Trade Organization (WTO) sets the rules of global trade and works towards ensuring smooth, predictable and free flow of trade. The WTO's agreements and the ministerial decisions as well as declarations are the main basis and legal foundation of the multilateral trading system.

The Ministerial Conference is the highest body to take decisions on international trade rules at the WTO. Such decisions are normally taken by consensus. Since the establishment of the WTO in 1995, 12 Ministerial Conferences have been held. Originally scheduled to be held in June 2020 in Nursultan, Kazakhstan and postponed twice due to the COVID-19 pandemic, the Twelfth Ministerial Conference of the WTO (MC12) was held in Geneva from 12 to 17 June 2022 and concluded with multilaterally negotiated outcomes named the 'Geneva Package'. Through this Ministerial, the WTO has demonstrated that it can deliver at a critical moment.

Some of the preparatory works had been done in 2021, especially the MC12 outcome document and the WTO's response to the pandemic. Members at the level of ambassadors and experts in Geneva worked hard to bridge gaps in most of the areas before the meeting of the trade ministers. There was significant progress in some areas such as the MC12 outcome document, the WTO response to the pandemic, and the decision on the World Food Programme's food purchase. The WTO response to the pandemic was a single document agreed among the membership before the arrival of the ministers in Geneva.

Major outcomes

Round-the-clock negotiations among members from 12 to 17 June concluded the Geneva Package by demonstrating that the WTO members can come together to address problems of the global commons. The Eleventh Ministerial conference (MC11) had ended without any tangible outcomes. This indicated that the organization had not been able to deliver since its Tenth Ministerial in 2015. This time, members held various rounds of consultations and negotiations at different configurations—including bilateral, small group and the entire membership—and the MC12 achieved some concrete results, including those on a few most urgent global issues. An overview of the MC12 outcomes is presented next.

MC12 Outcome document

The Ministerial Conference adopted the MC12 outcome document which covers a wide range of issues and agenda that members had been discussing at the WTO for the last few years. It reaffirmed members' commitment to a rule-based, predictable, inclusive and fair multilateral trading system.

The document recognized the priorities and interests of the least developed countries (LDCs). For the first time, trade ministers acknowledged challenges that graduation poses, including the loss of trade-related international support measures, as they leave the LDC category. They recognized the role that certain measures in the WTO can play in facilitating smooth and sustainable transition for these Members after graduation. This is an important achievement for the graduating as well as all LDCs because all will graduate sooner or later. This can be a good basis to continue negotiations on the LDC graduation-related agenda and conclude some deliverables through the Thirteenth Ministerial Conference (MC13).

Likewise, Ministers reaffirmed their commitment to implementing past decisions in favour of the LDCs, especially in the areas of service waiver, duty-free and quota-free market access, and rules of origin, and instructed the relevant bodies to report to the General Council, which would then report to the next Ministerial Conference. The Conference urged all Members to assist the LDCs in meeting their definitive category C deadlines of the Trade Facilitation Agreement. Finally, Ministers recognized the importance of the Aid for Trade (AfT) initiative in building trade-related capacities for the LDCs and recommended such programmes that prioritize the objectives identified by the LDCs.

In addition, the outcome document has acknowledged the challenges faced by landlocked developing country (LLDC) Members, especially in transit-related matters. It has instructed the Trade Facilitation Committee to hold a dedicated session on transit issues annually until the next review of the Trade Facilitation Agreement is completed. Such dedicated sessions will discuss the importance of transit and best practices, as well as the constraints and challenges faced by all landlocked Members. This is a small but significant achievement for the LLDCs, and it can be a good basis for expediting discussions on transit issues in a more constructive manner in future.

WTO reform remained an important component of the outcome document. A separate thematic session was organized to discuss this issue where members shared their perspectives. Based on the views expressed on the thematic session and negotiations among members, Ministers agreed to work towards necessary reform of the WTO to improve its overall functioning. This will provide an opportunity to bridge the existing gaps in the WTO functioning and also make the WTO fit for purpose. Members agreed to carry out the reform work in a member-driven, open, transparent, fair, and inclusive manner, and by addressing the interests of all Members, including development issues. Ministers committed to conducting discussions with a view to having a fully and well-functioning dispute settlement system accessible to all Members by 2024. Developing and least developed country Members need to be well-prepared and careful to secure their interests and priorities while conducting the reform.

The outcome document also speaks to cross-cutting areas such as women's empowerment, trade and environment, and micro, small and medium enterprises (MSMEs) in a very careful way as discussions on these areas have also been initiated in a plurilateral manner at the WTO. Ministers recognized women's economic empowerment and the contribution of MSMEs to inclusive and sustainable economic growth, and acknowledged their different contexts, challenges and capabilities in countries at different stages of development. These matters have been delinked with joint statement initiatives through a clarification in a footnote. Similarly, Ministers reaffirmed the importance of providing relevant support to developing country Members, especially for LDCs, to achieve sustainable development goals, including through technological innovations.

Ministerial decisions and declarations

Ministerial Decision on TRIPS Non-violation and Situation Complaints: Ministers directed the General Council to continue examination of the scope and modalities for complaints and make recommendations to MC13. The Conference agreed that, in the meantime, Members will not initiate such complaints under the TRIPS Agreement.

Ministerial Declaration on Responding to Modern SPS Challenges: By acknowledging the evolving global agricultural landscape with new opportunities and challenges, the declaration instructs the Sanitary and Phytosanitary (SPS) Committee to further enhance the implementation of the SPS Agreement to better manage issues related to international trade in food, animals and plants by undertaking a work programme. The declaration mandates the SPS Committee to explore how the implementation and application of the SPS Agreement can support addressing the emerging issues by taking into account the special needs of developing and LDC Members.

Ministerial Declaration on the Emergency Response to Food Insecurity: Ministers adopted a declaration on emergency response to food insecurity with special consideration to the specific needs and circumstances of LDCs and net food-importing developing countries (NFIDCs). They also emphasized enhancing productivity and production, trade, and availability, accessibility and affordability of food, especially in humanitarian emergencies. Ministers committed to having a dedicated work programme in the Committee on Agriculture with special consideration for the needs of LDCs and NFIDCs to increase their resilience in responding to acute food instability.

Ministerial Decision on World Food Programme (WFP) Food Purchase Exemption from Export Prohibitions or Restrictions: The Conference decided to exempt from export prohibitions/restrictions food purchase by the WFP by considering the critical humanitarian support that it provides. As per the decision, Members shall not impose export prohibitions/restrictions on foodstuffs purchased for non-commercial humanitarian purposes by the WFP. They also agreed that this decision shall not be construed to prevent the adoption by any Member of measures to ensure its domestic food security in accordance with the relevant provisions of the WTO agreements.

Ministerial Decision on the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS): The Conference made an important contribution to the global fight against COVID-19 by taking a decision of waiver of compulsory licensing for COVID-19 vaccines. It will help increase the production, supply and availability of vaccines and expand access to vaccines. This decision will be applicable for five years and the General Council may extend this period considering the exceptional circumstances of the COVID-19 pandemic. The General Council will review annually the operation of this Decision. Furthermore, as the scope of the decision is limited to COVID-19 vaccines, Ministers have instructed that no later than six months from the date of this Decision, Members will decide on its extension to cover the production and supply of COVID-19 diagnostics and therapeutics.

Ministerial Declaration on the WTO Response to the COVID-19 Pandemic and Preparedness for Future Pandemics: It aims to address the challenges and crisis being experienced by members as a result of the COVID-19 pandemic. Ministers recognized the uneven level of severity of the pandemic and recovery from it. They underscored the critical role the WTO can play in promoting inclusive growth including industrialization, development and resilience.

Similarly, they acknowledged the capacity building needs of developing country Members, and especially LDCs. They recognized that increasing the level of global preparedness to COVID-19 and future pandemics requires strengthened productive, scientific and technological capacity across the world. They reaffirmed the commitment of developed country Members, as enshrined in Article 66.2 of the TRIPS Agreement, on technology transfer.

Furthermore, they recognized the significant impact of the pandemic on services sectors including tourism and stressed the importance of services trade to support economic recovery of developing, and especially LDC, Members. They underscored the importance of global food security in resilience-building and responding to the current and future pandemics.

Ministerial Decision on Work Programme on Electronic Commerce: After rounds of negotiations and discussions, and holding a thematic session on this topic, Ministers agreed to reinvigorate the work under the Work Programme on Electronic Commerce, based on the mandate as set out in WT/L/274 and particularly in line with its development dimension. They also agreed to intensify discussions on the moratorium on customs duties on electronic transmissions, and instructed the General Council to hold periodic reviews based on the reports by relevant WTO bodies, including on the scope, definition and impact of the moratorium. Finally, they agreed to maintain the current practice of not imposing customs duties on electronic transmissions until MC13 or 31 March 2024 whichever comes early.

> For the first time, ministers acknowledged challenges posed by graduation, including the loss of trade-related support measures.

Ministerial Decision on Agreement on Fisheries Subsidies: Another important achievement was the Agreement on Fisheries Subsidies which was overdue since 2019 as mandated by the Sustainable Development Goals 2030 and MC11. After round-the-clock negotiations, Ministers adopted the Agreement on Fisheries Subsidies, though it is only partially agreed, with a view to provisioning comprehensive and effective disciplines to prohibit certain forms of fisheries subsidies. Furthermore, they mandated the Negotiating Group on Rules to continue negotiations based on the outstanding issues in the document with a view to making recommendations to the MC13 for additional provisions on fisheries subsidies contributing to overcapacity and overfishing.

Potential benefits

Benefits to Nepal come through the special provisions in favour of the LDCs, LLDCs and Article XII members (members who joined the WTO through the accession process). They are briefly summarized as follows:

- The outcome document and decisions and declarations have considered LDCs as a weaker segment of the membership and given them special consideration by mentioning “especially” or “in particular” LDCs.
- The outcome document has a separate paragraph on issues and priorities of LDCs focusing on duty-free and quota-free market access, service waiver, rules of origin, support for implementation of category C measures of the Trade Facilitation Agreement, and need-based aid for trade in LDCs. This may not be a significant achievement, but it ensures continuation of monitoring of the implementation of past decisions.
- It also has a sperate paragraph on LDC graduation, acknowledging the challenges that graduation presents, and recognizing the role that certain measures in the WTO can play in facilitating smooth and sustainable transition for these Members after graduation from the LDC category. This is an important achievement for the LDCs which can be a good reference to expedite

negotiations on this matter for achieving some concrete results from the next Ministerial.

- It also recognizes the special situation of the acceded Members (Article XII) and this situation shall be taken into account in subsequent negotiations. This can be an important basis for achieving some reforms in favour of Article XII Members through the reforms.
- It has a separate paragraph on LLDCs, which instructs the Trade Facilitation Committee to hold a Dedicated Session on transit issues to discuss best practices, as well as the constraints and challenges faced by landlocked countries. This is an important achievement for LLDCs and it can be a good basis for future work on ensuring smooth transit facilitation.
- The Ministerial Declaration on the WTO Response to the COVID-19 Pandemic has clearly indicated special priority to the LDCs in access to vaccines and other medical products as well as post-pandemic recovery.
- An assessment of the scope, definition and impact of the moratorium on customs duties on electronic transmissions, and reinvigoration of e-commerce work programme as per its mandate will be helpful for the LDCs and LLDCs in terms of capacity building and policy space while deciding on customs duties. The decision on TRIPS waiver will support increasing production of COVID-19 vaccines, especially in developing economies, and smooth supply in LDCs and LLDCs that have no or limited capacity to produce such vaccines.
- The declaration on emergency response to food insecurity has emphasized enhancing productivity and production, trade and availability, and accessibility and affordability of food in the LDCs and NFIDCs. Special consideration will be given to these countries in the dedicated work programme.
- The Ministerial decision on WFP food purchase would be helpful to address food insecurity in the LDCs and it also provides policy space to adopt necessary measures for domestic food security.

Nepal's participation

The Nepali delegation, led by Hon'ble. Mr. Dilendra Prasad Badu, Minister for Industry, Commerce and Supplies, attended the formal opening session, and participated in all the sessions and events during the Ministerial. Nepal shared its concerns and priorities on various occasions. While addressing the session on challenges facing the multilateral trading system, the Hon'ble Minister highlighted the current trend of the global trading system and serious constraints of LDCs and LLDCs in realizing benefits from it. He urged a strong commitment to upholding the principles of a rules-based, fair, transparent and predictable multilateral trading system, and sharing the prosperity from the system equitably.

> MC12 could not deliver a crucial decision on LDC Group's request for the extension of existing facilities and flexibilities to graduated LDCs.

Views expressed by Nepal have been reflected in the MC12 outcomes to some extent—for instance, the WTO reform through General Council and its subsidiary bodies, reinvigoration of the e-commerce work programme, TRIPS waiver, and adoption of a decision related to WFP's food purchase.

Some missed opportunities

The Geneva package was appreciated in different forums globally. One reason was the sharp contrast to the MC11, which had concluded without any significant outcome. However, while going through the details of the outcomes, it can be observed that some important areas were missed out. For instance, it could not deliver a crucial decision as per the proposal by the LDC Group requesting for the extension of existing facilities and flexibilities to graduated LDCs for a few more years after graduation. This matter was left aside while concluding the final deal of the Ministerial.

Similarly, the Ministerial could not take any decision on agriculture negotiations, including agriculture subsidies and a permanent solution on public stockholding practices. Furthermore, no concrete decision was made on matters related to special and differential treatment provisions, and the G90 proposal and its revised version could not get priority. The Ministerial agreed on TRIPS waiver but covered only COVID-19 vaccines and excluded treatments and tests, and the limited exemption agreed comes with more monitoring and reporting requirements than under existing rules.

Finally, in the procedural part, members have expressed some dissatisfaction, particularly on transparency and inclusivity in the negotiations and decision-making while concluding the final deal of the MC12. For instance, Members received some texts negotiated by small groups in 'green rooms' just a few hours before the closing session and there was not sufficient time to digest the final text for Members not part of the green rooms.

In addition, despite spending more than two decades and holding many rounds of negotiations and Ministerial Conferences, the WTO could not deliver any substantive outcomes under the Doha Development Agenda, except for a few areas, at MC12. It was a missed opportunity in this regard.

Above all, considerable and sustained efforts are needed in the post-MC12 period to ensure the delivery of the Geneva package in reality. ■

The author is Counsellor/DPR (Commerce) at the Permanent Mission of Nepal to the UN and other International Organizations in Geneva. Views are personal.

Accelerating energy transition in Asia-Pacific through green power corridors

Cross-border power system integration is a key tool that can enable a faster and affordable transition while maintaining high levels of energy security.

Matthew Wittenstein

The Asia-Pacific region is increasingly the driver of global economic growth and energy demand. The region is responsible for more than 50 percent of global greenhouse gas emissions, and more than 80 percent of the projected growth in global demand for coal will come from countries in Asia and the Pacific.[1] According to the Asian Development Bank (ADB), developing Asia will account for 43 percent of global energy demand by 2030, with China and India together accounting for nearly two thirds of that amount.

At the same time, there is growing momentum for the energy transition, driven by a combination of policy, economics, and technological innovation. Many countries in the region have committed to achieving net-zero greenhouse gas emissions in the coming decades and to significantly increase the share of renewable energy in the power system. India, for example, has announced plans to develop 500 gigawatts (GW) of renewable energy capacity by 2030,[2] and to achieve net-zero carbon emissions by 2070.[3] Many countries have also committed to phasing down, or fully phasing out, coal-fired generation, with initiatives such as the Powering Past Coal Alliance (PPCA) and ADB's Energy Transition Mechanism (ETM) working to turn these pledges into reality.

At the same time, fundamental shifts in global energy markets are strengthening the economic argument for energy transition. Tight fossil fuel supplies driven by COVID-19 recovery and the war in Ukraine have led to a significant increase in the price of coal, natural gas, and oil, while the cost of photovoltaic (PV) solar, wind turbines, and batteries continues to decline. In fact, while increased commodity prices are affecting renewable energy costs as well, according to the International Energy Agency they remain competitive compared to fossil fuel alternatives.[4]

There is every reason to believe, therefore, that the countries of Asia and the Pacific will continue to see significant growth in the development of renewable energy resources, which are abundant in the region. However, these resources are unevenly distributed and are often located in remote areas, far from the demand centres where they are most needed. This is particularly challenging for densely populated countries with limited potential for domestic renewable energy development, but also for countries with significant domestic resource potential that expect to see significant growth in energy demand in the coming years from continued economic development and the expansion of electricity access.

For all of these countries, the need to accelerate the energy transition must be balanced with the need to keep energy costs affordable to consumers while also ensuring reliable access to electricity. Cross-border power system connectivity is a tool that countries can use to meet these three often conflicting goals simultaneously.

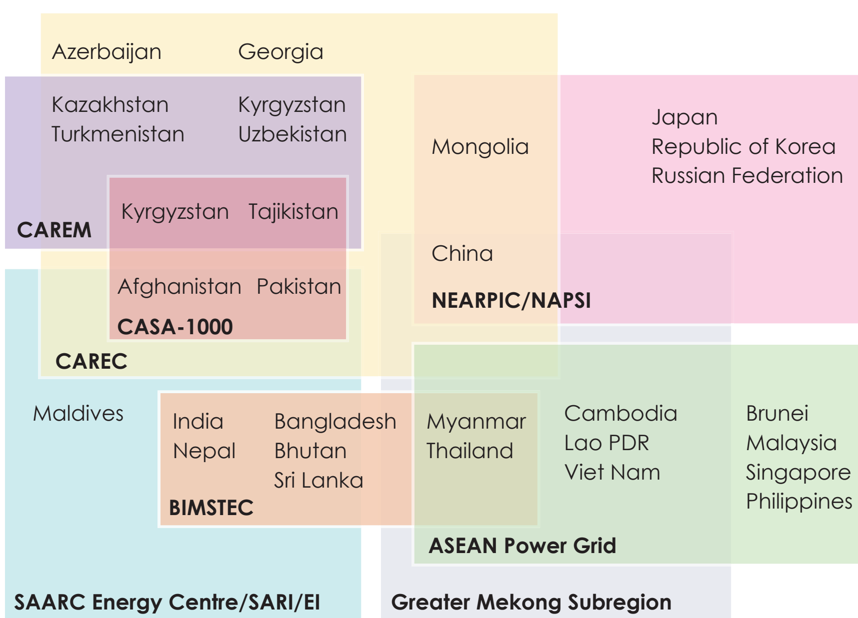
From an economic perspective, power system connectivity can enable access to lower-cost energy resources, can allow for the export of electricity and therefore the potential to earn export revenues, and can support larger investments than would otherwise be justifiable, thereby allowing developers to take advantage of increased economies of scale. From the perspective of energy security, connectivity increases resource diversity, both in terms of the number of available resources and also the type, making systems more resilient to both unexpected outages and interruptions to specific fuel supply chains. Finally, connectivity enables sustainability by giving countries access to regions with relatively higher potential for renewable energy and enables the integration of variable renewables through so-called "resource smoothing", whereby natural variations in weather patterns average out over larger distances, making it easier to balance solar PV and wind generation.

Many countries in Asia are already collaborating on energy issues. In some cases, these efforts focus on energy collaboration in the context of broader connectivity or economic integration efforts, such as the South Asian Association for Regional Cooperation (SAARC) and the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC). In other cases, these efforts focus more narrowly on power system connectivity, including the South Asia Regional Initiative for Energy Integration (SARI/EI) and the Central Asia-South Asia 1000 (CASA-1000) project (Figure 1). Countries in the region are also collaborating on power connectivity issues with regional or even global scope. ESCAP member States, for example, participate in the Expert Working Group on Energy Connectivity, which meets periodically to discuss practical actions for accelerating power system connectivity in the Asia-Pacific region.[5] And, at COP26, the UK and Indian governments jointly launched the Green Grids Initiative – One Sun, One World, One Grid (GGI-OSOWOG), which brings together a range of stakeholders and complementary initiatives to increase investments in grid infrastructure linked to the deployment of renewable energy.[6]

The numerous, at times overlapping, set of initiatives support collaboration on energy issues across a wide range of countries, but progress on power system connectivity in the Asia-Pacific region remains relatively limited. Most cross-border interconnectors are operated on a bilateral, often unidirectional basis, and, in contrast to other parts of the world, there are no power pools or other mechanisms that support multilateral power trading. In addition, while there is increasing attention to the role of power system connectivity in supporting energy transition, the main driver of cross-border connectivity has historically been economic (access to lower cost resources) while concerns over energy security remain a major obstacle to further development.

Nevertheless, countries in the region recognize the potential role of power system connectivity for sustainable development, in particular in the context of Sustainable Development Goal 7 (SDG7): access to affordable, re-

Figure 1 Select power system connectivity and energy cooperation initiatives in Asia



Source: UNESCAP

Figure 2 The Regional Road Map on Power System Connectivity strategies

Planning	• Develop a regional master plan • Coordinate cross-border transmission planning
Financing and development	• Mobilize investment in cross-border infrastructure
Operations	• Move toward multilateral trading and competitive markets • Co-ordinate cross-border system operations
Cross-cutting	• Build trust and political consensus • Develop intergovernmental agreements • Coordinate, harmonize, and institutionalize policy and regulatory frameworks • Build capacity and share information, data, best practices • Ensure coherence of connectivity with the SDGs

Source: UNESCAP

liable, sustainable and modern energy for all. In 2021, at the 77th Commission session of the United Nations Economic and Social Commission for Asia and the Pacific (ESCAP), member states endorsed the Regional Road Map on Power System Connectivity, which contains a vision, a set of principles, and nine strategies for increasing power system connectivity in support of sustainable development. These strategies cover areas such as planning, financing cross-border infrastructure, operating interconnected systems, and various cross-cutting issues (Figure 2).

Many of these strategies relate to general challenges that face all efforts to connect power systems across borders, such as the need to coordinate transmission planning, the challenge of mobilizing investments in cross-border infrastructure, and moving toward multilateral power trading. One in particular, however, focuses on the need to ensure the coherence of energy connectivity initiatives and the Sustainable Development Goals.

To implement this strategy, ESCAP is working with its member states to develop a framework to inform and guide connectivity projects, in the form of a "Green Power Corridor". A Green Power Corridor is a vision for sustainable power system connectivity that has three main principles: connectivity projects should support sustainable development; align with national policy objectives; and build off of existing work (Figure 3).

Sustainable development in this context means primarily targets set under SDG7, including increasing the share of modern renewables and access to modern energy sources. But it can and should also include other sustainable development objectives, such as climate action (SDG13), good health and wellbeing (SDG3), and decent work and economic growth (SDG8). So, for example, connectivity projects that support renewable energy integration should be prioritized over projects that connect to coal plants, while connectivity projects that increase renewable energy integration, improve air quality, and create jobs should be prioritized most of all.

The Green Power Corridor concept is underpinned by six building blocks or elements necessary for the successful development of sustainable cross-border connectivity projects. These are supportive institutional frameworks (for example, to support regional planning or organize a power exchange); an infrastructure backbone (high-voltage transmission lines); enabling financial arrangements (such as the potential to include private and climate finance, and clear cost allocation and recovery mechanisms); supportive regulatory frameworks (to enable flawless and efficient operations, transparent power trade, and equitable distribution of benefits); social acceptance (to ensure public support); and, underpinning each of these, political accord (to ensure consistent and strong support across all participating governments).

This framework is still under development, and many core issues will need to be addressed before governments are able to consider adopting it. Nevertheless, certain key elements can already inform and accelerate cross-border connectivity projects in the region.

First, there is a need for countries to develop more cross-border power system infrastructure. As a starting point, countries should do more to coordinate their power system plans. Even simply sharing plans on a regular basis can help identify opportunities for increased cross-border connectivity, for example, to take advantage of a planned generator that will be located near a border.

More complicated but equally important is supporting regulator collaboration to enable more harmonization of regulations and standards. Even in the absence of cross-border connectivity, countries can benefit from the best practices and lessons learned from countries that have, for example, deployed higher shares of renewable energy or leveraged auctions to lower renewable energy costs. In the specific context of cross-border integration, however, harmonization is critically important to ensure the stable and efficient operations of integrated systems.

Countries should also leverage innovative financing mechanisms to develop grids. Again, this is useful even in countries that are focusing only on domestic development, as increased investments in grid infrastructure will be necessary to integrate higher shares of renewable energy. According to the IEA, grid investments will need to triple by 2030 in order to be on track to meet longer-term net-zero targets.[7] While some of these investments could be built with public financing, as the majority of projects in Asia-Pacific are today, increasing investments to the required levels will require additional sources of capital.[8]

Where cross-border grid infrastructure is in place, countries should look to increase cross-border power trade. Bilateral trade could be improved, for example, by developing standardized power purchase agreement (PPA) templates or otherwise harmonizing the method of entering into and managing bilateral purchases.

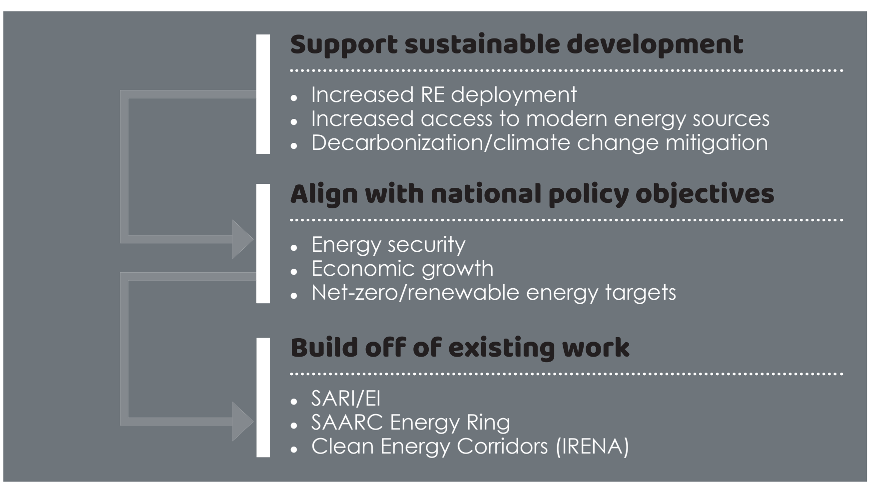
Countries should also look at how to increase the flexibility of cross-border trading. As the share of variable renewables in power systems increases, the need for flexibility will increase as well, in particular, to balance the natural fluctuations of wind and solar PV. Moving from unidirectional to bidirectional trading is one way to address this, so that power can flow where it is needed, but this should in addition be linked to more flexible contract structures that don't include, for example, large take-or-pay clauses or that otherwise restrict the ability of system operators to utilize cross-border trade as a source of system flexibility. Related to this point, countries should also work to develop multilateral power trading, to allow for more optimal allocation and utilization of resources across multiple jurisdictions.

Finally, countries should leverage and as necessary develop supportive institutions. Regular communication is foundationally important for enabling increased connectivity, and countries therefore should organize regular meetings of relevant stakeholders. Sector-focused bodies, such as the South Asia Forum for Infrastructure Regulators (SAFIR), are also important, as they enable not only regular communication but can also organize useful activities such as capacity building and training exercises. These organizations also provide a strong foundation upon which to build in order to develop institutions with more formal roles to play, such as setting market rules or helping to manage the settlement of power trade.

The Asia-Pacific region is increasingly the driver of global economic growth and energy demand, which means the Paris Agreement targets can only be met if the energy transition succeeds in this region. Meeting net-zero emissions targets will require a significant increase in investments in renewable energy technologies, in particular wind and solar. The energy transition is accelerating in the Asia-Pacific region, but the scale of investment needs, combined with the unequal distribution of renewable energy resources in Asia and the Pacific, makes it difficult, if not impossible, for countries to decarbonize entirely on their own. At the same time, policymakers must ensure that power remains affordable and secure even as the energy transition accelerates. Cross-border power system integration is a key tool that can enable a faster and affordable transition while maintaining high levels of energy security. While there are many initiatives in the region working to support power system connectivity, more must be done to increase investments in grid infrastructure and enable more cross-border power trade to enable the integration of higher shares of renewable energy and the energy transition more broadly. ■

Mr. Wittenstein is Chief of Section, Energy Connectivity, at the UN Economic and Social Commission for Asia and the Pacific (UN ESCAP).

Figure 3 **Guiding principles of the Green Power Corridor Framework**



Source: UNESCAP

Notes

1. ADB. 2022. “Asia and the Pacific is the Frontline of the Climate Change Battle.” *Asia and the Pacific’s Climate Bank. Asian Development Bank.* https://www.adb.org/climatebank.
2. Ministry of Power. 2021. “India takes one more step to reduce carbon emission and reduce the cost of power to consumers. Ministry of power allows bundling of renewable to replace thermal power under existing PPAs.” Press Release, 16 November 2021.
3. BBC. 2021. "COP26: India PM Narendra Modi pledges net zero by 2070.” *British Broadcasting Corporation*, 2 November 2021.
4. IEA. 2022. *Renewable Energy Market Update*. Paris: International Energy Agency.
5. UNESCAP. 2022. “Expert Working Group on Energy Connectivity.” *UNESCAP.* https://www.unescap.org/our-work/energy/ewg-on-energy-connectivity.
6. UN Climate Change Conference UK 2021. 2021. “Green Grids Initiative-One Sun One World One Grid: One Sun Declaration.”
7. IEA. 2021. *Net Zero by 2050.* Paris: International Energy Agency.
8. See: UNESCAP. 2022. “Attracting Private Finance to Transmission in the Asia-Pacific Region.” UNESCAP Working Paper, 14 June 2022.

Implications of LDC **graduation for Nepal**

Nepal must use international and multilateral forums to pursue post-graduation interests, including continuation of the use of LDC-specific provisions for a specific period.

Nepal is graduating from the least developed country (LDC) category in 2026. While graduation is an important milestone in Nepal's development journey and a testament to the socio-economic progress the country has achieved, the fact remains that Nepal is graduating without meeting the per capita income criterion. Furthermore, graduation means losing a host of international support measures offered by the international community aiding Nepal's development. Formulating a transition strategy to ensure a smooth, sustainable and irreversible graduation requires an understanding of the implications of graduation in the areas of market access, development cooperation, and trade-related policy space.

Implications for market access

A major implication of LDC graduation is the loss of preferential market access available through LDC-specific schemes under the Generalized System of Preferences (GSP) and other arrangements. About two thirds of Nepal's exports are absorbed by India, and the bilateral trade treaty is not tied to LDC status.

Tariff increases

After graduation, Nepal's exports will face tariff increases in other major potential destinations. While the European Union (EU), the United Kingdom (UK), and Turkey provide a transition period of three years after graduation, Nepal will face new tariff regimes in other preference-granting countries post-graduation. For some products, the next-best tariff regime offers the same tariffs as the LDC tariff regime, while for others the new tariffs will be distinctly higher. There is low awareness among exporters of the likely tariff changes.

While in the US market, which is the second largest market for Nepal's exports, the tariff increase is relatively low (1.5 percentage points), it is especially pronounced in the EU market (5.7 percentage points). If Nepal becomes eligible for the EU's more generous GSP+ regime, which provides duty-free market access almost on a par with the LDC-specific Everything but Arms

(EBA) scheme, the tariff increase is negligible. A similar argument is applicable to Turkey and the UK, which also offer GSP+ like tariff regimes. Tariff increase is relatively large in Nepal's other export destinations—China, Japan, and Canada. Tariff increase is zero in the case of Australia and Norway as their next-best schemes offer significant duty-free coverage whereas Switzerland will see a negligible increase in applied tariffs.

A major export sector that faces the highest increase in tariffs is the clothing sector (6.7 percentage points), but the increase will be much lower under the GSP+ like regimes (1.4 percentage points). In the textiles sector, representing the largest share of exports to preference granting countries, tariff increase will be 2.6 percentage points under the ordinary GSP regime and 0.7 percentage point under the GSP+ like regime.

Nepal's private sector is worried about increases in tariffs and fear a severe impact given that Nepal's production cost is higher than in competing countries—the cost of production in the apparel sector is about 26 percent higher than that of neighbouring countries, as per the Garment Association of Nepal.

Nepal struggles to utilize available trade preferences. Around 62 percent of Nepal's exports to preference-granting destinations are eligible for LDC-specific preferential treatment, but less than three fourths of these eligible exports enter utilizing LDC-specific preferences. The low or moderate utilization rate of preferences in some markets (e.g., China, South Korea, the US, and Japan) blunts the projected impact on exports of increases in tariffs. In some destinations, a huge proportion of current exports face zero duties even without being granted any preferences (e.g., two thirds of exports to the US), implying zero tariffs for products after graduation.

Under the Agreement on South Asian Free Trade Area (SAFTA), Nepal will face a significant increase in tariffs for refined soyabean oil and palm oil. These products have emerged as top export items bound for India. However, the sustainability of these exports is questionable given that they are based on the differential in tariffs on imported raw materials between Nepal and India.

Estimates of impact on merchandise exports

Nepal's merchandise exports could fall by 2.5-4 percent as a result of increased tariffs upon graduation. Exports to the EU are expected to see the largest losses, assuming that Nepali exports will face ordinary GSP instead of GSP+ whereas the impact will be the lowest in the US, among major markets. The clothing and textile sector will see the largest impact.

This underscores the importance of securing access to the GSP+ and the GSP Enhanced Framework schemes in the EU and the UK, respectively. The EU's newly proposed GSP for the period 2024-34 requires ratification and effective implementation of 32 international agreements, adding 5 agreements to the current 27 international conventions. Nepal has ratified 25 of these conventions, one has been signed but not ratified while another has been neither signed nor ratified. It is yet to sign and ratify one of the additional five conventions included in the EU's proposed revision to its GSP scheme.

Rules of origin

Graduation will lead to Nepal facing more stringent rules of origin in preference-granting countries, such as the EU, Turkey, the UK, Canada, Australia, and the Russian Federation, among others. In particular, apparels will have to meet a double transformation requirement compared to the single transformation requirement for LDCs. This may pose a serious obstacle to exporters despite the product getting a preferential tariff rate in the next-best schemes (e.g., zero duty under the EU's GSP+ scheme). Readymade garment exporters express concerns they may not be able to meet the double transformation requirement even if alternative schemes offer preferential tariffs. Moreover, not all exporters are aware of the change in rules of origin.

Under SAFTA, after graduation Nepal's trade will face more stringent rules of origin provisions. Given the current export structure, this might not be concerning; however, the more stringent rules of origin could be an obstacle to expanding Nepal's exports by utilizing SAFTA preferences in future.

Services

Much of Nepal's services exports are in the travel and tourism sector, which have been taking place without any connection to the LDC services waiver at the World Trade Organization (WTO). The waiver allows granting of preferential market access to services and their providers from LDC members. The impact of losing access to the waiver is expected to be marginal. However, it could represent a missed opportunity if it is operationalized in future.

Implications for development cooperation

Official development assistance (ODA) is an important source of finance for the Government of Nepal (GoN). ODA amounts to about a quarter of annual public expenditure. Two multilateral development partners, the World Bank (WB) and the Asian Development Bank (ADB), provide more than half of the ODA received by Nepal. Bilateral ODA, including that provided by the EU, accounts for about 42 percent of ODA.

Bilateral aid

Geopolitical considerations, and bilateral relationships determine bilateral ODA. LDC status is not a criterion in the provision of ODA from most major bilateral sources of aid to Nepal. Overall, the volume and terms and conditions of bilateral ODA will not be significantly affected by graduation.

The concessionality of loans from Japan and the Republic of Korea is tied to LDC status, among other factors. A country has to be low-income as well as an LDC to qualify for the most concessional loans offered by Japan. As Nepal will not fall under any category upon graduation, the window of accessing the most concessional loans from Japan will be closing. Loans from South Korea will become less concessional, too. Most bilateral ODA to Nepal is in the form of grants (an average of about 75 percent during 2014/15-2019/20). There is no evidence or indication that graduation will change this significantly.

Developed countries have committed to providing 0.15-0.2 percent of their GNI as ODA to LDCs. This aid commitment is targeted at LDCs as a group, not individually. Thus, even if Nepal upon graduation is excluded from the aid target specific to LDCs, as a developing country it will be eligible for aid from developed countries pledging to provide 0.7 percent of GNI as ODA to developing countries.

Multilateral ODA

Per capita income is a main criterion used by multilateral institutions. The World Bank has been providing concessional loans through the International Development Association (IDA) to Nepal. World Bank lending is based on GNI per capita, not LDC status. However, with Nepal having moved into the lower-middle-income category from the low-income category, and as its per capita increases further, the level of concessionality of loans from the World Bank is likely to decline. Still, the loans will be highly concessional, relative to borrowing from international capital markets. It is to be noted that this is not due to LDC graduation per se.

Another major multilateral development partner—Asian Development Bank (ADB)—categorizes countries into three groups—A, B and C—based on their creditworthiness, GNI per capita and also considers country's LDC status for providing concessional loans, ordinary capital resources or market-based resources. Nepal is currently in Group A receiving concessional assistance-only group. However, since Nepal has crossed an income cut-off, it is likely to graduate to Group B in ADB's classification, where loans are less concessional but still carry more favourable terms and conditions than those in international capital markets. The shift from Group A to B normally takes four years. Moreover, graduation to another lending group involves close consultation between the ADB and the recipient country.

Other sources of aid

The United Nations Development Programme (UNDP) and the United Nations Children's Fund (UNICEF) are mandated to provide a certain portion of their core resources to LDCs. This is allocated to the LDCs as a whole and not individually. Hence, graduation from the LDC category could potentially affect a portion of resources dedicated to the country in the subsequent budget cycle. However, the UNDP has been mandated to assist graduating countries in achieving a smooth transition; thus, its funding for Nepal may not be immediately affected.

Graduation will also impact access to the LDC Fund (LDCF) under the United Nations Framework Convention on Climate Change (UNFCCC), the United Nations Capital Development Fund (UNCDF), and aid for trade under the WTO's Enhanced Integrated Framework.

Implications for trade-related policy space

The implications of graduation for Nepal's policy space can be viewed through three lenses. First, Nepal stands to lose flexibilities that LDCs are entitled to in implementing policies related to, inter alia, trade, industrial development and health. Second, Nepal may be unable to continue with policies that run afoul of WTO rules because these policies are likely to come under greater scrutiny. Third, the pressure to liberalize trade at the WTO and regional forums could further reduce Nepal's policy space to protect domestic industry as well as cause revenue loss.

Way forward

GoN should prepare a smooth transition strategy in consultation with all stakeholders, consistent with its periodic development plan. Such strategy must identify a comprehensive and coherent set of activities by taking into account the loss of LDC-specific international support measures and emerging opportunities.

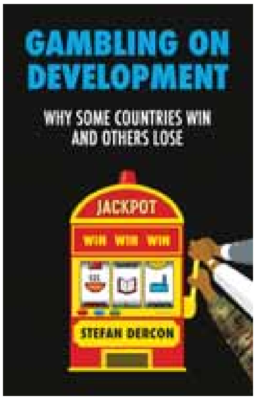
The first order of business should be to promptly study the appropriateness of acceding to the remaining international conventions necessary for accessing GSP+ of the EU. It should launch a dialogue with the EU and the UK for accessing GSP+ and the Enhanced Framework. In addition, Nepal should initiate a dialogue with other preference-granting countries, seeking an extension to LDC-specific concessions and preferences for at least 3-5 years following graduation. In addition, Nepal should lobby for lenient rules of origin for LDCs for a period sufficient for the private sector to adjust to the new rules of origin.

To realize the vast untapped export potential, the government should prepare trade strategies, in consultation with the private sector, to strengthen the competitiveness of the economy, upgrade exporters' capabilities, diversify export products and markets, simplify and streamline processes to attract more foreign direct investment and encourage enterprises to participate in regional/global value chains. Such policies may also help compensate for the loss of LDC-specific international support measures.

GoN should explore new forms of finance, including blended finance, public-private partnerships, private philanthropies and co-financing, among others, and work with development partners for new forms of support mechanisms such as dedicated funds for graduated countries, disaster insurance, and technology transfer mechanisms.

The implications of LDC graduation should be disseminated at the grass roots across the country. At the same time, Nepal must use international/multilateral forums to pursue post-graduation interests, including continuation of the use of LDC-specific provisions for a specific period. ■

This piece is excerpted from the study 'Nepal's graduation from the LDC category: Implications for international trade and development cooperation' undertaken by SAWTEE.



Road to development

Title: Gambling on Development: Why Some Countries Win and Others Lose
Author: Stefan Dercon
Publisher: Hurst
ISBN: 1805260081

Kshitiz Dahal

The field of economics has offered myriad solutions for economic backwaters to engender economic growth and development, albeit competing at times. Stefan Dercon's *"Gambling on Development: Why Some Countries Win and Others Lose"* offers a novel perspective on this perennial question—why some countries are able to rapidly uplift the living standards of many and root out extreme forms of poverty in a short time, and why others fail? Whatever the ingredients for economic development may be, the recipe for igniting development cannot work without a successful development bargain—the elite's commitment to economic growth and development—argues Dercon in his book. In other words, the path of rapid development is only possible when the local elites go beyond their mere self-enrichment and 'gamble for development'—it is a gamble because development is a messy process and the results are not guaranteed.

The book articulates its thesis through three major parts. Part I provides a quick tour of the prevalent ideas in development thinking, covering a great many economists of modern times. Dercon explains that these popular ideas often compete with each other, fail to form a consensus on "where to start, who should act, and at what level", and most importantly, fail to clearly explain why a diverse group of countries have been able to accelerate their development. The crux of this section, and the book, is that development can take off only when the elites of the country—those in the political, economic, and social spheres who wield decision-making powers or can influence the decisions—settle on a 'development bargain', i.e., choose and commit to the path of economic growth and development as the optimal long-term path, out of many elite bargains possible. Dercon provides three essential features of such a bargai: the presence of durable political and economic deals, a sensible state that takes on appropriate roles, and the presence of course correction through learning from mistakes.

The second part of the book applies the framework of the development bargain to explain real-world examples of development successes and failures, and the ones that show signs of evolving. Through these examples, the book showcases its other important propositions such as the development bargain can emerge in countries that vastly differ in historical, political, economic, and social aspects; and, the development bargain can emerge irrespective of initial state capabilities.

The last part of the book takes a jab at the current global approach to the development problem, which, according to Dercon, is the tendency to reduce development to merely a finance problem. The book argues that international cooperation and financial aid, while never a central solution to development problems, can play an auxiliary role. Countries with a presence of the development bargain can successfully leverage international cooperation and financial aid to their advantage, and hence deserve significant attention from international donors; and in the case of countries where the development bargain is not in place, the aid could be used in a way that could incentivize the emergence of a development bargain.

Two insights from the book appear particularly encouraging. First, a country may start with any level of state capability to kick start development if there is a substantial commitment among elites. Second, there may be ways by which international cooperation and foreign aid could play a significant supportive role in catalyzing development.

The book does an excellent job of convincing readers of the momentous role of the 'development bargain' in igniting development. However, it does not elucidate enough as to how the development bargain can be engendered. It baffles readers looking for plausible ways to accelerate economic growth and development in a country like Nepal, which, according to the book, achieved an elite bargain that led to the cessation of a decade-long civil war, without a destructive regime change, but an elite bargain, that in its core, is not a development bargain. Likewise, does foreign aid risk sustaining the current non-developmental elite bargain, or is it indispensable to nudge the state towards a development bargain? The book offers no clear explanations, and perhaps there are no clear explanations. In spite of this, it remains a brilliant book. ■

Central Bank Digital Currency

The first challenge for digital currency is cyber threat and central banks need to address this adequately so that society can benefit from digital currency.

Swastik Aryal

The digital revolution has been characterized as a fusion of technologies that is blurring the lines between the physical, digital, and biological spheres.[1] Digitalization has reached many aspects of production processes and has touched many corners of daily activities. A budding new sector has been currency and money. As cryptocurrencies, such as Bitcoin and Etherium, are trying to find a solid ground as legal tender, central banks around the world have begun exploring their own digital currencies. While some have already launched their own digital currencies, some have begun trials and others are in the process of formulating policies. Although there are quite a few countries that are trialling central bank digital currencies (CBDCs), the concept still seems ambiguous. Perhaps due to early stages in the trial periods or due to policies being under formulation, the concept still seems unclear.

What exactly is a central bank digital currency?

The simple answer to this question is that CBDC is the digital version of a country's physical currency.[2] CBDCs are digital tokens issued by a central bank and are pegged to the value of a country's fiat currency. CBDCs would have full faith and complete backing of the government that issues them.[3] A CBDC is simply a digital form of the currency that consumers and financial institutions currently use.

Why are countries exploring digital currencies?

With the introduction and rise of digital and crypto currencies like bitcoin and tether, the world seems to be moving towards digitization of money rather quickly. The concern with privately issued digital currencies like bitcoin is their volatility. The central bank-introduced digital currency, on the other hand, will not witness that issue as the digital token is pegged to the fiat currency. The main goal of CBDCs is to provide businesses and consumers with privacy, transferability, convenience, accessibility, and financial security. CBDCs can also decrease the maintenance cost of a complex financial system, reduce cross-border transaction costs and lower cost options to those who use alternative money transfer methods.[4]

Will digital currencies replace cash?

In theory CBDCs will replace physical money, but central banks of some countries and regions such as the European Union have actually stated that a digital currency would complement, rather than replace, physical cash.[5] The use of cash, however, would decrease significantly after CBDCs come into full effect. Many countries actually witnessed the decrease in the use of physical money during and after the COVID pandemic.

Types of central bank digital currencies

There are two types of CBDCs: wholesale, used by financial institutions; and retail, used by consumers and businesses. Wholesale CBDCs are similar to reserve holdings in a central bank.[6] Use of monetary policy tools by the central bank can set interest rates of CBDCs. Retail CBDCs on the other hand are government backed digital currencies which consumers and businesses can use to trade for goods and services.

Pixabay

State of digital currency in the world

Many countries are exploring and developing their own CBDCs. As already mentioned, some countries are ahead in the race toward digitizing their currencies than others. Nigeria, Jamaica and the Bahamas are some of the countries that have already launched its digital currencies. Similarly, China is set to launch their digital currency soon. Countries like the United States of America, United Kingdom, Japan, India and South Korea, among others are in the exploring, researching and development stage of digital currency. Following the development of neighboring countries in exploring digital currencies, the central bank of Nepal, Nepal Rastra Bank (NRB), carried out a study to identify appropriate policy goals and design for CBDC in Nepal.

Digital currency in Nepal

Nepal Rastra Bank has carried out a comprehensive study on CBDC. The study has analyzed the digital currencies already in use as well as recommended a CBDC design for Nepal.

The study recommends a CBDC design facilitating retail use, with the use of an intermediated architecture and a semi-centralized ledger providing both account-based and token-based access, as the most appropriate design choice in the context of Nepal. To ensure better access, sound resilience, and wider inclusion of the payments, and cost-efficient currency management, such a CBDC system should seamlessly interoperate with other regulated private payment systems, pay no remuneration on CBDC holding, should be available round the clock for use, have a holding limit, and be programmable for broader usage options.[7]

Furthermore, to develop a digital currency in Nepal, the study recommends the creation of a dedicated team to look after CBDC, formulate strategic plans for CBDC, conduct a detailed feasibility study, ensure an adequate legal framework, select appropriate policy goals, adopt a robust CBDC system, build NRB's capacity, coordinate with other supporting agencies, increase public awareness, continue to promote digital banking and simulate a prototype before the launch of the digital currency.

Nepal is not in a rush to launch a CBDC. For now, Nepal is learning from the best practices of countries that have developed and launched a digital currency. Similarly, Nepal will first observe how countries in South Asia as well as China proceed with their digital currency.[8] Given that there are big challenges surrounding digital currencies, a observe, analyze and develop method can be beneficial.

Table **CBDC design choice recommended for Nepal by its central bank**

Key design parameters	Choices	Remarks
Purpose of use case	Retail	Supports better access and inclusion
Architecture	Intermediated	Supports easy customer onboarding
Infrastructure or ledger	Semi-centralized	Supports better resilience and control
Access design	Account-based	Supports whole allocation to BFIs
	Token based	Supports better financial inclusion
	Interoperable	Supports better access, resilience, and inclusion
Instrument characteristics	Non-remunerative	Reduces currency management cost
	24/7 available	Supports better access and resilience
	Quantity capped	Avoid disintermediation risk
	Programmable	Provides broader usage options

Source: Nepal Rastra Bank

Challenges and benefits

The first challenge for central banks to issue a CBDC is cyber threat. The World Economic Forum warns that the risk from counterfeiting, theft and network failure could have more catastrophic consequences with digital money. As cryptocurrencies have been a key target of hackers and thieves, a central bank-backed digital currency would likely attract the same crowd.[9] In some countries, lack of trust in the central bank was a challenge. Due to low trust in the central bank of Ecuador, its digital currency, launched in 2017, was cancelled after three years.[10]

Research on CBDC needs to address the challenges adequately so that society can benefit from digital currency. CBDC can increase financial inclusion by improving access to money. Similarly, digital currency can provide a backup for unavailability of cash and boost the resilience of the financial system. As cash is easily untraceable, a digital currency can improve transparency of money flow. ■

Notes

1. Schwab, K. 2016. "The fourth industrial revolution: what it means and how to respond" World Economic Forum, 14 January 2016.
2. Masterson, V. 2022. "What are central bank digital currencies?" World Economic Forum, 31 August 2022.
3. Seth, S. 2022. "What is a central bank digital currency (CBDC)?" Investopedia, 19 March 2022.
4. *ibid.*
5. *ibid.* Note 2.
6. *ibid.* Note 3.
7. Nepal Rastra Bank. 2022. Central bank digital currency (CBDC): identifying appropriate policy goals and design for Nepal. Concept paper, Currency management department, NRB. August 2022.
8. Tassev, L. 2022. "Nepal prepared to issue digital currency, drafts necessary amendments." *Bitcoin News*, 7 August 2022.
9. *ibid.* Note 3.
10. *ibid.* Note 2.

Roundtable discussion on "overcoming barriers to growth entrepreneurs"

SOUTH Asia Watch on Trade, Economics and Environment (SAWTEE) conducted a roundtable discussion on "Overcoming barriers to growth entrepreneurs" to examine the present state of and gaps in the support system in Nepal for startups and growth-potential existing businesses, including those eyeing export markets on 29 November. The objective of the discussion was also to identify the types of focused support needed for startups and how different support agencies from private and public sectors should be engaged to build a well-connected ecosystem to help startups to grow.

In his presentation, Mr. Shashi Bhattarai, Co-founder and Director, Knowledge Holding International Pvt. Ltd., highlighted the dearth of incubators at academic institutions in Nepal, which has not let the startup and entrepreneurship culture flourish. Mr. Prem Luitel, Under Secretary, Ministry of Industry, Commerce and Supplies, mentioned that the government is simultaneously drafting a Startup Policy and an SME Policy to assure a healthy ecosystem for startups and business ventures. The roundtable saw the participation of entrepreneurs, academics, government representatives and finance and investment experts. ■

Preparedness of Nepal's pharmaceutical sector

SOUTH Asia Watch on Trade, Economics and Environment (SAWTEE) and Third World Network (TWN) organized a workshop on "Preparedness of Nepal's pharmaceutical sector in the face of LDC graduation" on 26 July.

The event was organized to identify the major policy and institutional challenges for the optimal use of flexibilities available under the Trade-Related Aspects of Intellectual Property Rights (TRIPS) of the World Trade Organization and suggest the way forward in the context of Nepal's graduation from the category of the least developed countries in 2026.

SAWTEE brought together relevant stakeholders—from policymakers and the pharmaceutical industry to health professionals and civil society—to analyze the strengths and weaknesses of the pharmaceutical industry in Nepal to face product patent protection; identify the preparedness of the pharmaceutical industry to make use of other TRIPS flexibilities; identify the major policy and institutional challenges for the optimal use of TRIPS flexibilities; and suggest the way forward. ■

Perspectives on food security

CUTS International organized a hybrid Panel Discussion titled "Civil Society Perspectives on Food Security: Taking Policies from Glass fronts to Grassroots" at the South Asia International Economic Law Network (SAIELN)'s Third Biennial Conference on Food Security and International Law: Critical and Interdisciplinary Perspectives, in Kochi on 20 December..

The session saw panelists share their experiences and the pioneering work of their organizations in grassroots agriculture. The Panel was supported by Professor Leila Choukroune, Director of the University of Portsmouth Thematic Area in Democratic Citizenship and co-Chair of SAIELN. It was moderated by Dr. Veena Vidyadharan, Fellow, CUTS International, who noted in her introductory remarks the multi-dimensional nature of food security, and how civil society organizations (CSOs) have a very important role to play in many of these aspects.

The discussion touched upon points such as the challenges and prospects of organic farming, issues relating to technology and access to the public distribution system, and the extent to which Free Trade Agreements and Bilateral Investment Treaties should start dealing with granular details touching upon these aspects. ■

Twenty-fifth Sustainable Development Conference

THE Sustainable Development Policy Institute (SDPI) organized its Twenty-fifth (25th) Sustainable Development Conference (SDC) from 5–8 December 2022 in Islamabad, Pakistan. The overarching theme of the Silver Jubilee Conference was Sustainable Development in Unusual Times: Building Forward Better. Under the overarching theme of sustainable development, the conference discussed various pertinent issues such as economic recovery, achieving the sustainable development goals (SDGs), climate change, food security, trade and energy, among others, in the thematic sessions.

A key outcome of the conference was policy recommendations revolving around geoeconomics of Pakistan, challenges in achieving the SDGs, trade policies for climate change mitigation, central banking for inclusive development, strengthening climate diplomacy in South Asia and building resilience through community engagement, among others.

The conference saw participation of researchers, scholars, academicians, private sector organizations, development partners and media. ■

GI system for tea

THE Institute of Policy Studies of Sri Lanka (IPS), in collaboration with the Center for International Research for Agriculture Development, Agence française de développement and Sri Lanka Tea Board, organized a series of regional workshops on 'Implementing Geographical Indication (GI) System for Ceylon Tea' on 22–30 November 2022 in seven tea growing regions in Sri Lanka. The workshops were attended by a large number of stakeholders in the tea industry including tea factory owners, tea exporters, Tea Small Holdings Development Authority, Tea Research Institute, Tea Smallholding District Societies and researchers. ■

Regional conference on suitable seeds for food security

SOUTH Asia Watch on Trade, Economics and Environment (SAWTEE), Kathmandu and Fridtjof Nansen Institute (FNI), Norway jointly organized a two-day regional conference from 2 November to 3 November 2022 on Suitable Seeds for Food Security to disseminate the findings of the study “Suitable seeds for food security in fragile states” and initiate a discussion around seed security and climate change. Additionally, the conference was organized to bring a South Asian perspective in fostering regional cooperation for food security and discuss the role of policy, legal and institutional frameworks in conservation of and access to suitable seeds. Dr. Kristin Rosendal, Senior Researcher, FNI, highlighted in her presentation that food security depends largely on access to a broad variety of suitable seeds since good quality food plants that are adapted to changing climate are necessary to fight climate change.

Photo Concern

Similarly, Dr. Vibha Dhawan, Director General, The Energy and Recourses Institute (TERI), India, shared that intellectual property rights (IPR) protection of genetic materials for plant breeders is needed for us to effectively stimulate innovation and secure returns on investments in genetic improvement.

The two-day conference saw discussions on topics such as 'Fostering Regional Co-operation for seed security: South Asian Perspective', 'Changes in EU Seed Regulations – Global Trends', 'Financing Climate Change Adaptation' and 'Impact of COVID-19 on Agri Input Chain'. The event saw participation of researchers, academics, policymakers, representatives of farmers' bodies, consumer rights activists, organizations working on climate change adaptation, and media, among others from Bangladesh, India, Nepal, Pakistan, Sri Lanka and Norway. ■

sawtee

South Asia Watch on Trade, Economics and Environment (SAWTEE) is a regional network that operates through its secretariat in Kathmandu and member institutions from five South Asian countries, namely Bangladesh, India, Nepal, Pakistan and Sri Lanka. The overall objective of SAWTEE is to build the capacity of concerned stakeholders in South Asia in the context of liberalization and globalization.

www.sawtee.org