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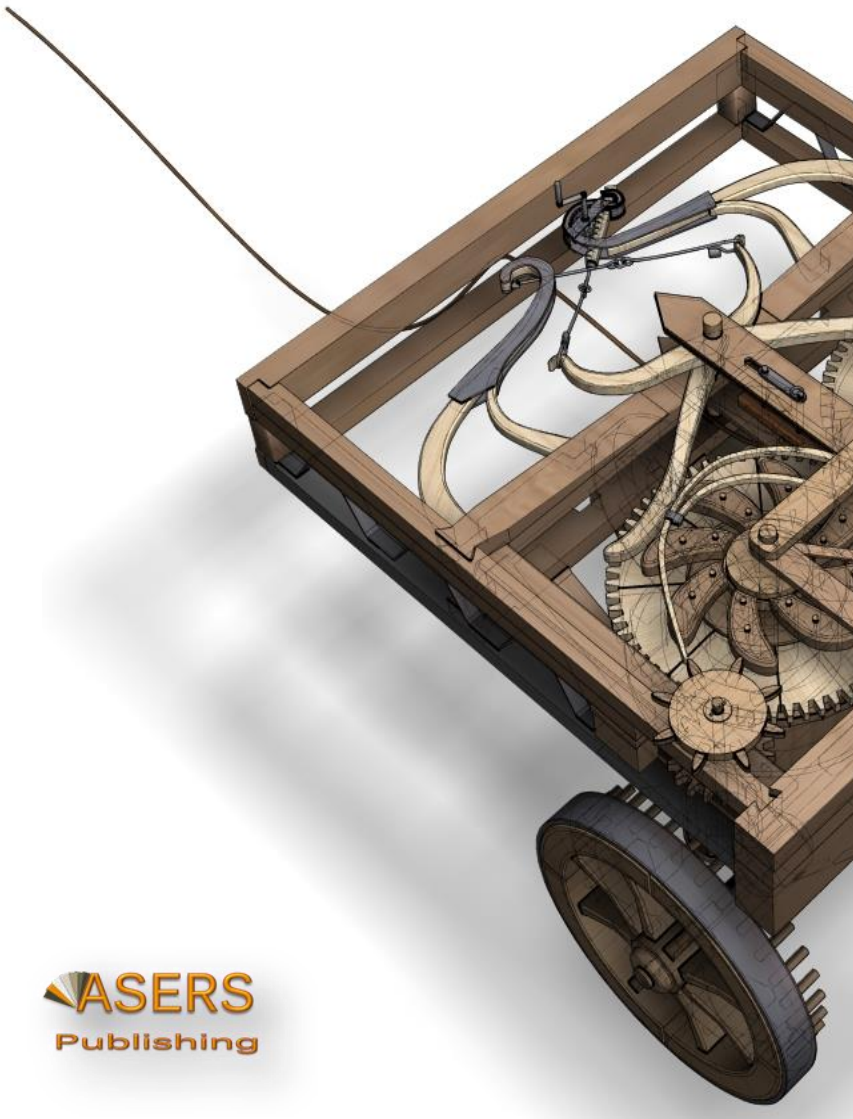

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Contents:

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Theoretical and Practical Research in Economic Fields

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SURFING ON THE TIDE? LEAST-DEVELOPED COUNTRIES TRADE DURING THE GREAT GLOBAL TRANSITION

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Abstract:

The rebalancing of global demand towards large emerging countries and the resulting long-lasting cycle of high international commodity prices had a profound impact on LDC trade. This process contributed to a wider geographical diversification of LDCs' exports but led also to a greater reliance on those highly priced commodities. LDCs remain particularly vulnerable to external shocks; the 2008-2009 global crisis and the bumpy transitional recovery that followed illustrate the fragility of the recent trends. A slowdown in the growth of large emerging countries may end the commodity "super-cycle", deepening LDCs' structural trade imbalances. In such a perspective, renewed efforts towards extensive product diversification are called for. Fostering diversification has been supported for many years by preferential market access to develop and --more recently-- to emerging countries. But preferences alone are not sufficient to improve the supply-side capabilities of most LDCs. The new business models related to global value chains offer new opportunities to LDCs for export diversification and trade facilitation is one of the key components of this diversification strategy.

Key words: Least developed countries, trade and development, 2008-2009 global crisis, preferential market access, global value chains, trade facilitation.

JEL Classification: F13, F14, F63, O19, O24

1. Introduction

Least developed countries as a group are known for being very dependent on the exports of a few primary commodities. This dependency proved to be a blessing during the commodity super-cycle which coincided with the rapid emergence of large developing countries, in particular China. For the first time in 2005 the LDC group registered a trade surplus. But it was short-lived and the trade balance reverted to deficit after the global crisis of 2008-2009.

A return to the upbeat international market conditions that prevailed in the mid-2000s is not to be expected. The Great Global Transition —an on-going process of rebalancing global sources of supply and demand— enters now into a new phase as "emerged" economies rely less on export-led growth and look more at their domestic markets as a source of effective demand. The post-crisis global transition will probably be

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characterised by a weaker global demand and lower commodity prices. Export diversification remains therefore a high priority for LDCs.

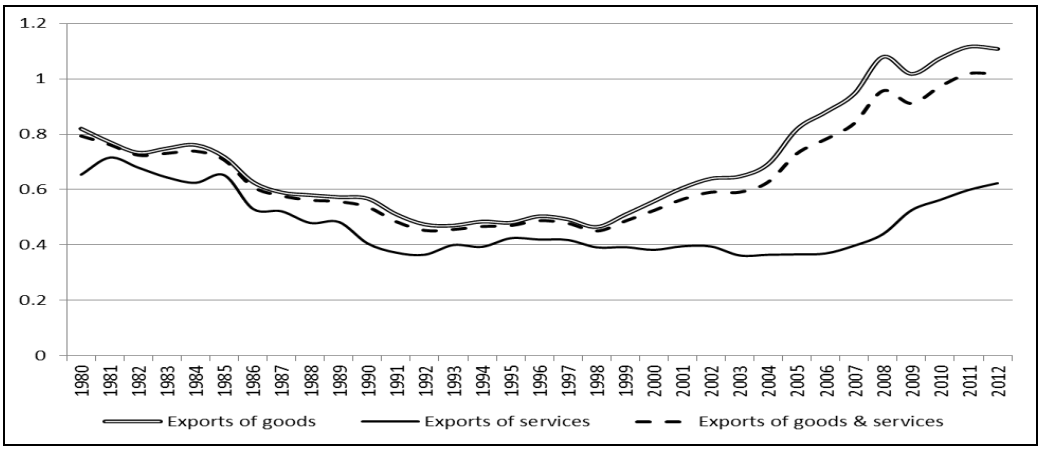
To help in this diversification on the demand-side, LDCs benefit from special and differential treatment in terms of market access under WTO rules. On the supply-side, global value chains offer new perspectives. LDCs which could not build a competitive domestic industrial base through old-style import-substitution industrial policies can now join international production networks and export particular "tasks" rather than entire finished products. In this context, trade facilitation is crucial for fostering LDCs competitiveness.

The article first reviews the main trends that affected LDCs' trade in goods and services since the early 2000s. After looking at the impact of the 2008-2009 crisis, the paper revises the potential of international value chains for export diversification and the main challenges faced by LDCs.

2. The least – developed countries and the world market

2.1. Least – developed countries in world trade

Since the early 2000s, least developed countries did more than just riding the globalization tide and they were able to increase their share in key markets. This result contrasts with a somewhat mediocre outcome in the 1980s and 1990s. LDC exports increased at an average annual rate of 21% between 2000 and 2008, to be compared with 15% for all developing countries and 12% for the world. As a result of the rapid rates set in the 2000s, the share of LDC total exports in the world corrected the decline registered since 1980 and closed at over one per cent in 2012 (Chart 1). In services, the market share of LDCs exports has yet to return to the values of early 1980s, despite a good performance after 2005.



Source: Based on WTO data.

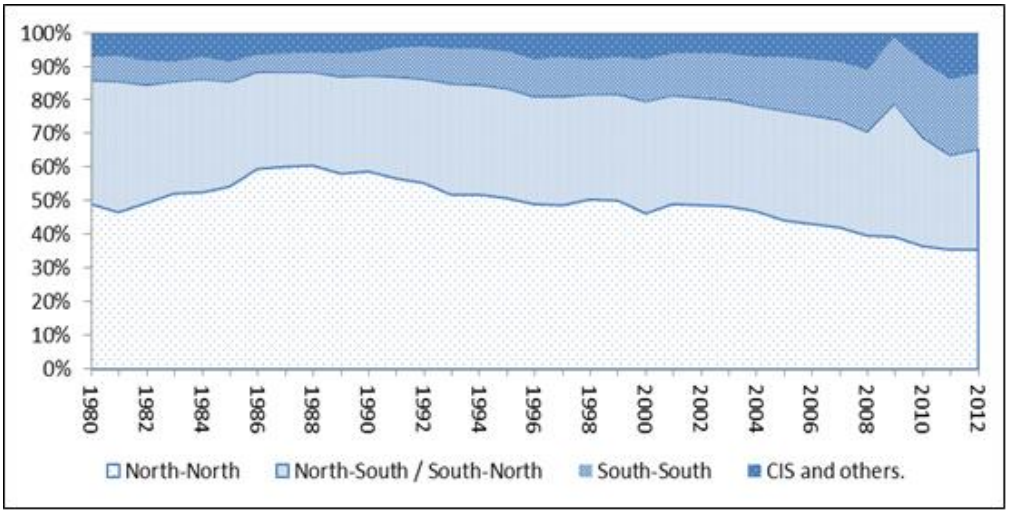
Figure1: Share of LDC exports of goods and commercial services in world exports, 1980-2012 (Percentage)

A few words of caution are called for at this stage. Most of the analysis is done from the LDC group perspective; this should not minimize the fact there is a large array of individual country's characteristics that make this group quite a heterogeneous one. If we follow some indicators, such as trade balances, this heterogeneity has increased in the most recent years. Applying exploratory data analysis techniques, Escaith and Tamenu (2013) test the classification of LDCs according to their export specialization and other economic indicators. If trade profiles vary between the various sub-groups, the eventual overall economic and social outcome, as measured by the UNDP's Human Development Index, is quite uniformly low across the group.

A large part of the 2000s success story is due to the so-called "super-cycle" of commodities when the average annual growth rate of LDCs' exports of fuels and minerals jumped to 19.5% in the 2000s as a result of both stronger demand and higher prices. Meanwhile, trade in manufactures lagged behind, even though it accelerated to 10.5%. The shift in barter terms of trade between commodities and manufacture is largely attributed to the rapid emergence of China. On the one hand, the "Factory Asia" phenomenon in global production networks has lowered the production cost of manufacture; on the other hand, Chinese imports of agricultural and mineral goods increased rapidly to satisfy its booming investment and domestic consumption.

The rise of emerging countries in the second half of the 1990s and during the 2000s was closely related to the emergence of global value chains and the delocalization of part of the manufacturing process from the North to the South. Thanks to this trend, a new middle class appeared in the emerging countries, which increased its demand for housing, goods and services. The convergence of these supply and demand factors profoundly altered the geography of trade.

The 2000s were clearly characterised by the growing share of South-South trade and the falling share of North-North trade (Chart 2). This reconfiguration is occurring while trade volumes increase in both cases, *id est*, in a win-win situation for both North and South. Between 2000 and 2008, South-South trade expanded by an annual average of 19% while the share of South-South trade in world trade increased from 11% in 2000 to 18% in 2008. On the other hand, despite a 9% average annual growth, the share of North-North trade in world shrank from 50% in 2000 to 41% in 2008.



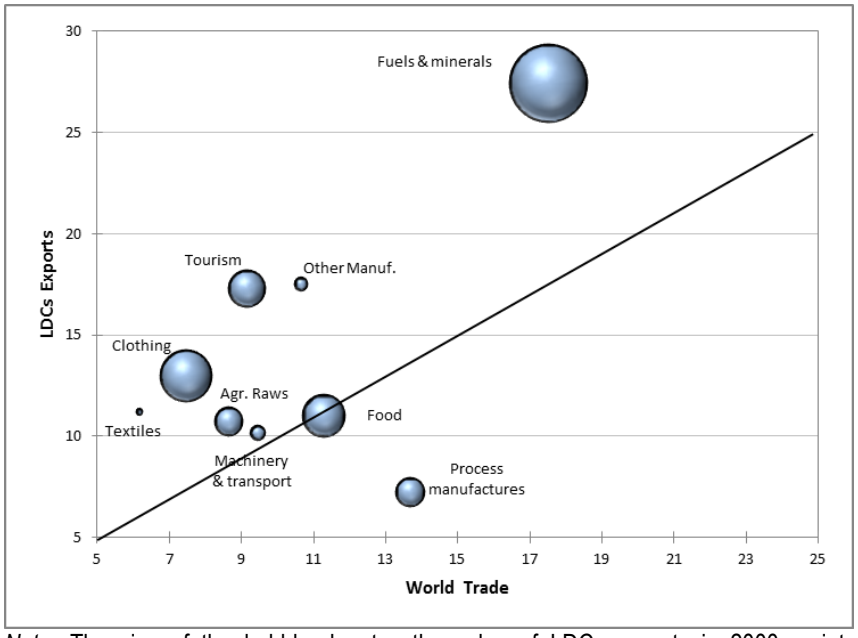
Source: Based on UN Comtrade database.

Figure 2: Geographical distribution of world trade in merchandises, 1980-2012 (Percentage)

During the 2000s, China emerged as the top destination for LDC exports. In 2012, this country absorbed 23% of LDCs' total exports, up from 9% in 2000. Actually, China represents 44% of LDCs' South-South exports. [5] The European Union accounted for 19% of LDCs' exports in 2012, down from 27% in 2000. The United States was the third destination market for LDC products with 11% in 2012 - half of the 2000 share. It should be highlighted that the relative drops in the weight of South-North exports took place in spite of 13% and 9% average annual growth of LDCs exports to the European Union and the United States between 2000 and 2012. In other term, relative gains/losses took place in a dynamic context. Charts 3 and 4 are 45° diagrams that depict the extent to which LDCs gained/lost market shares in selected products and markets between 2000 and 2008. During the super-cycle, LDCs have gained market shares in the world's most dynamic sectors (fuels and minerals) and most dynamic markets (China and India). In view of this, it is not surprising that the overall market share of LDC exports rose during this period. A more elaborate shift-share analysis [6] leads to the same conclusion, with fuels and minerals accounting for more than three-quarters of the growth of LDC exports between 2000 and 2008. The chart shows also that LDCs improved their market share in the dynamic sector of travel services (tourism).

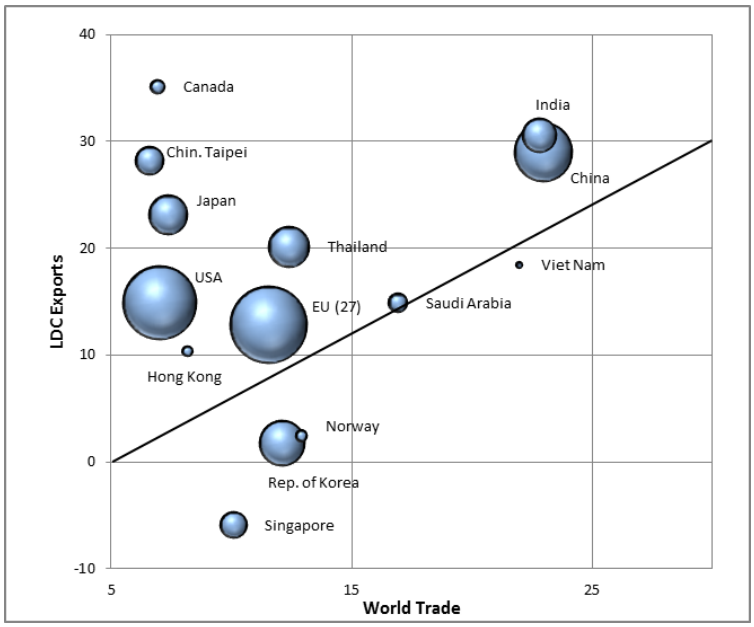
[5] As destination markets for South-South trade, other developing Asia and Africa represented 16% and 10% of LDCs exports in 2012. Intra-LDC trade is under recorded due to statistical gaps; WTO estimates indicate an average annual increase of 17% in intra-LDC trade in the last 12 years (WTO, 2013d). Due to geographic proximity, most of this trade takes place within Africa.

[6] A method used to identify the extent to which growth can be attributed to general global trends and to more distinctly national ones (such as improved competitiveness). See PIEZAS-JERBI, Ninez and Coleman NEE (2009) for further details.



Note: The size of the bubble denotes the value of LDCs exports in 2000; points above/below the 45° line denote a growth higher/lower than world average.
Source: Based on WTO data.

Figure 3: Comparative evolution of LDCs' product specialization, 2000-2008 (Annual average growth, %)



Notes: The bubble size indicates the importance of the corresponding market for LDCs exports in 2000; points above/below the 45° line are those for which LDCs have gained/lost market share.
Source: Based on WTO data.

Figure 4: Comparative evolution of main LDC markets for goods, 2000-2008 (Annual average growth, %)

The value of trade in services, a sector of particular relevance for many small LDCs, increased also at a relatively fast pace, especially after 2005. Albeit LDCs typically run a deficit in the services account, as a group they record a surplus in travel, reflecting the importance of in-bound tourism in their economies (ITC, 2013). Honeck (2012) points that, amongst the few LDCs that have graduated or are expected to do so, almost all have a strong tourist sector.

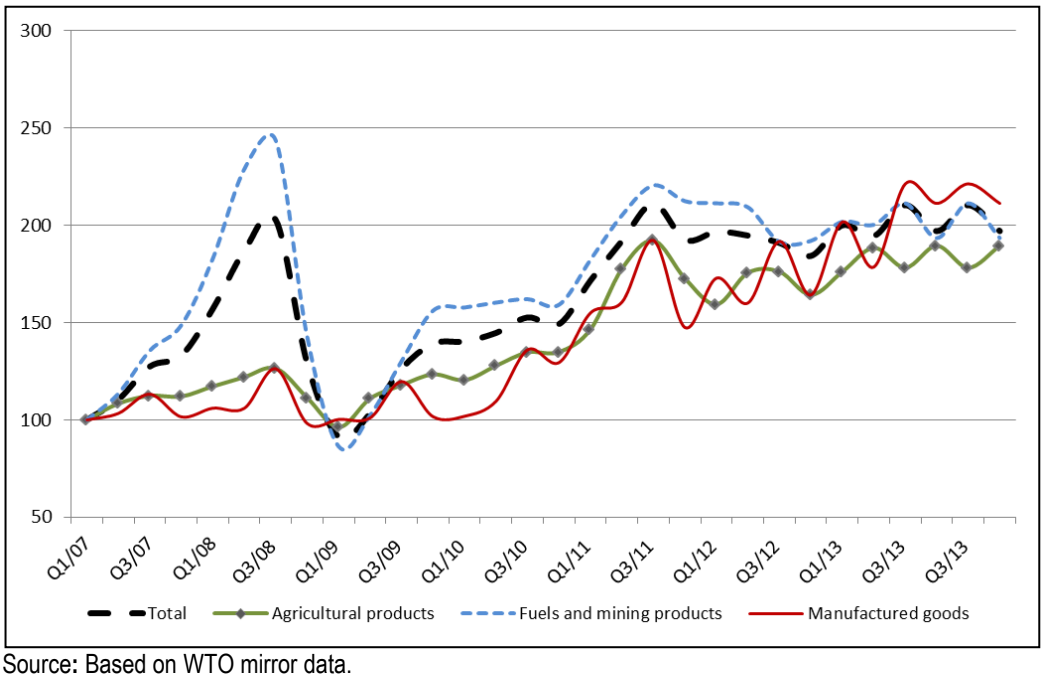
2.2. Least developed countries and the great trade collapse

The rapid increase in the total value of goods and services exported by LDCs during the 2000s came to an abrupt halt in 2008, in the wake of the global financial crisis. Global trade contracted by 22.5% during 2009. For LDCs, the main channel of contagion was through the price effect on commodities. As far as LDC exports of clothing are concerned, specialization in the low-price range of products helped some LDC producers weathering the storm, as cash-constrained consumers in developed markets shifted to the cheapest options. Bangladesh was even able to increase its exports, albeit marginally, thanks to its diversified export partners.

The market for primary commodities, such as fuels and minerals, was one of the first to bounce back but did not recuperate the high value observed immediately before the crisis. All in all, as shown in Chart 5, LDC exports of goods remained below their pre-crisis levels up to the first quarter of 2011. This underperformance is nevertheless, fully attributable to the export price of fuels and mining products. Manufactures (mainly clothing exported by Asian LDCs) fared better than other products during 2013.

Trade in commercial services has been generally more resilient than trade in merchandise. However, transportation and – to a lesser extent – travel (which includes tourism expenditure) have been significantly affected. All in all, the LDCs went through the 2008-2009 crisis reasonably well, considering the structural vulnerability of their economies and the extent of the global recession. In contrast to past crises and to other groups of countries in the world, growth remained positive for LDCs as a group and in two-thirds of individual LDCs (for a review, see Audiguier, 2012).

Recovery suffered a second negative shock in 2011 when the world economy was plagued by a series of economic, political and natural shocks. The European economy was hit by the euro sovereign debt crisis, with negative impact on its economic growth and international trade lasting up to mid-2013. In the meantime, China and most other large emerging economies were revising downward their growth expectations. After rebounding in 2010 and 2011, world trade growth remained sluggish during 2012 and 2013, not growing much over 2% in real term. All in all, the 2008-2009 crisis probably signalled a turning point in the Great Global Transition which started with China's accession to WTO in 2001. After a first period of rapid growth and profound structural changes that marked the global rebalancing between East and West, the world economy may have entered a period of slower growth.

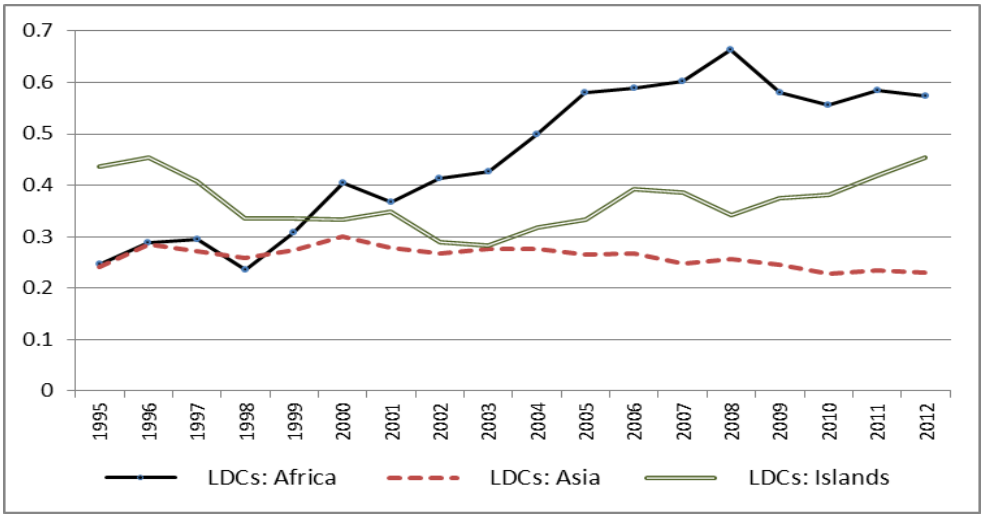


Source: Based on WTO mirror data.

Figure 5: Quarterly evolution of LDCs merchandise exports value, by major product groups, 2007-2013 (Index Q1/07 = 100)

2.3. Dynamic momentum but structural weaknesses

LDCs' income from exports is known to be particularly vulnerable to external shocks due to their lack of diversification. Export concentration is usually understood as the degree to which a country's exports are concentrated on a small number of products or a small number of trading partners. Due to the lower degree of development of their productive sectors, LDCs are heavily dependent on a few natural resources products where they enjoy some degree of comparative advantage. Even when LDCs were able to diversify into manufactures, the range of exports is usually limited to a few labour-intensive industries, mostly in clothing. For eight LDCs, the top three products accounted for more than 95 per cent of their export receipts before the 2008 crisis, illustrating the vulnerability of these economies to fluctuations in international trade. Some small island LDCs also depend very heavily on tourism receipts as the dominant source of exports.

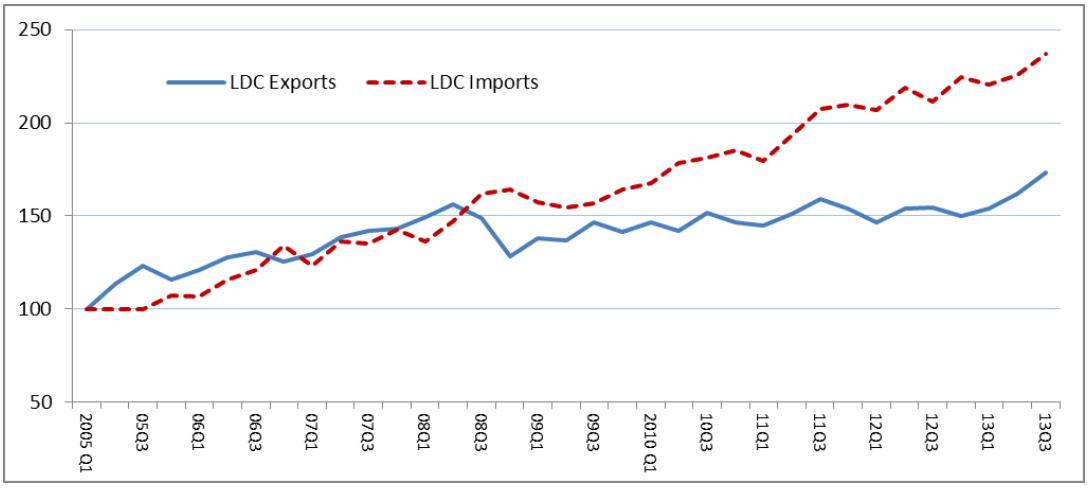


Note: Herfindahl-Hirschmann index normalised to range from 0 (minimum) to 1 (maximum).
Source: Based on UNCTAD.

Figure 6: Evolution of the concentration of LDC merchandises exports, 1995-2012

If the geographical diversification of LDCs exports improved during the past decade, the rise of commodities during the super-cycle tended to exacerbate the dependency on commodity exports, at least for the LDC countries that have large natural resources endowments. Chart 6 shows that the concentration index of African LDCs increased up to the 2008 global crisis. This is almost entirely due to the rise in the international price of fuels and minerals. On the contrary, the concentration index of Asian LDCs, which are diversifying into labour-intensive manufactures, decreased. Island LDCs are somewhere in between but they tend to rely more on services (particularly tourism) for their export revenues; a higher concentration on merchandises exports is less of an issue for them than in the case of Africa.

While African LDCs' export dependency increased because of the super-cyclical commodity price hike, it should not be understood as a structural regression or a bad thing by itself. This is a windfall gain which can translate into structural improvements if used for developing infrastructure or fostering productive investment in tradable goods and services production. On the other hand, the vulnerability to export price fluctuations is a real issue, because the LDCs as a group have recorded trade deficits, with the exception of a few years that immediately preceded the global crisis of 2008-2009. This structural deficit, symptom of supply shortcomings, micro-economic inefficiencies and economic imbalances, develops into acute economic and social issues when export earnings drop while imports include a large share of essential goods such as fuels or food whose demand is inelastic.



Source: Based on UNCTAD and WTO data.

Figure 7: Quarterly evolution of LDCs export and import volumes, 2005-2013 (index 2005 Q1 = 100).

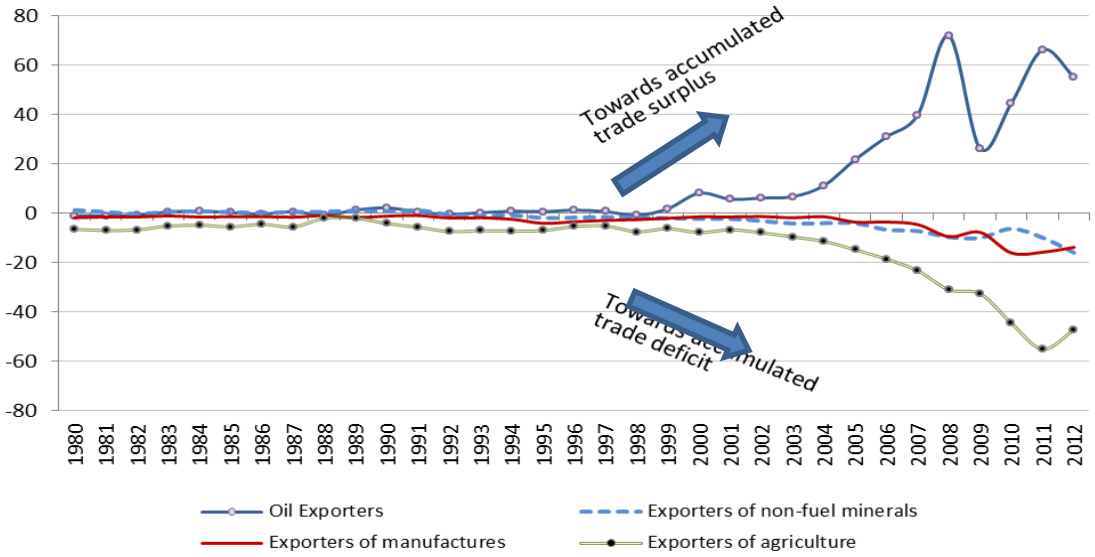
The risk is compounded if, after a commodity price bonanza, the windfall gains are treated as a permanent income shift that increases the structural demand for imports. It may have been the case on the basis of the limited statistical information available. While import and export volumes tend to move together up to the 2008-2009 crisis, a decoupling took place after the crisis and merchandises imports have been growing faster than exports (Chart 7). In such a situation, the end of the super-cycle would translate into growing trade deficits that would prove unsustainable.

The deficit is particularly high for manufactures, followed by agricultural goods (Table 1). The heterogeneity between sub-groups exploded in the 2000s. The oil exporting sub-group was the only one to post trade surpluses in the 2000s, although this was not even the case for all countries within that group. Trade balances of mineral and manufacture exporters became somewhat equilibrated in the 2000-2008 period, albeit these groups incurred trade deficits towards the end of the period. The super-cycle was obviously not such a good thing for LDCs that are net importers of fuels and minerals; they saw their trade balances becoming increasingly negative, with the largest trade deficits being among the agricultural exporters and the LDCs without a clear export specialization.

Table 1: LDCs trade balance in goods by merchandise groups, 2000-2012 (billion dollars)

	2000	2005	2006	2007	2008	2009	2010	2011	2012
Total merchandise	-7.3	-4.7	2.9	3.6	6.0	-26.0	-7.0	-4.3	-18.4
Agriculture [a]	-1.9	-5.3	-6.6	-9.3	-15.2	-14.4	-17.6	-23.4	-23.8
Fuels	10.5	37.2	47.5	62.8	87.7	52.3	64.0	76.3	78.0
Non-fuel minerals	1.1	3.3	6.6	8.0	10.0	7.8	13.2	16.4	16.4
Manufactures	-17.5	-39.3	-48.6	-59.3	-78.7	-74.8	-89.1	-107.9	-116.3

Note: Trade balances refer to FOB valuation on both export and import sides. [a] Includes forestry and fishery products.
Source: WTO.



Source: Based on WTO and UN Comtrade database.

Figure 8: LDCs merchandise trade balance by export specialization, 1980-2012 (Billion dollars)

Separating the price and volume effects provides some additional insights into what has been behind these divergent trends (Table 2). Whereas most exporters enjoyed similar export growth in terms of volume, they fared quite differently when it came to the evolution of the average price of their merchandises exports (defined as the average unit value of their total exports) and their year-to-year fluctuations (12% in average for manufacturers vs. 50% for fuel exporters). A completely symmetrical picture emerges when looking at the import side: annual average rate of growth of volume varied significantly across LDC sub-groupings while import prices rose at a more comparable rate. The corollary is that the evolution of the barter terms of trade – positive in the case of fuel and mineral exporters, negative for the rest – goes some way to explain the different trade balance trajectories. Moreover, it is worth pointing to the wide heterogeneities within the different groups in terms of the year to year fluctuations of volume and prices of their traded goods, as indicated by the coefficient of variation.

Table 2: LDCs' exports and imports: evolution of volume, unit value and value, 2000-2012 *(Percentage)*

	Volume		Unit Value		Value	
	YoY variation [a]	*Coef .of variation* [b]	YoY variation	*Coef .of variation*	YoY variation	*Coef .of variation*
Exports						
LDC Group	8	31	10	44	16	59
of which:						
Agricultural exporters	8	28	7	35	13	54
Fuel exporters	7	31	12	50	17	63
Mineral exporters	10	31	9	41	18	63
Manufacture exporters	10	39	2	12	12	48
Other exporters	5	15	8	34	10	38
Imports						
LDC Group	10	38	6	26	15	54
of which:						
Agricultural exporters	10	35	6	26	14	53
Fuel exporters	13	46	5	21	17	58
Mineral exporters	12	40	6	25	17	61
Manufacture exporters	6	22	6	30	12	50
Other exporters	4	*18*	7	*31*	11	*42*

Notes: [a] Average annual rate of growth over the 2000-2012 period of total merchandise exports for LDCs group and by export specialization sub-groups. [b] Standard deviation divided by average variation.
Source: based on WTO and UNCTAD data.

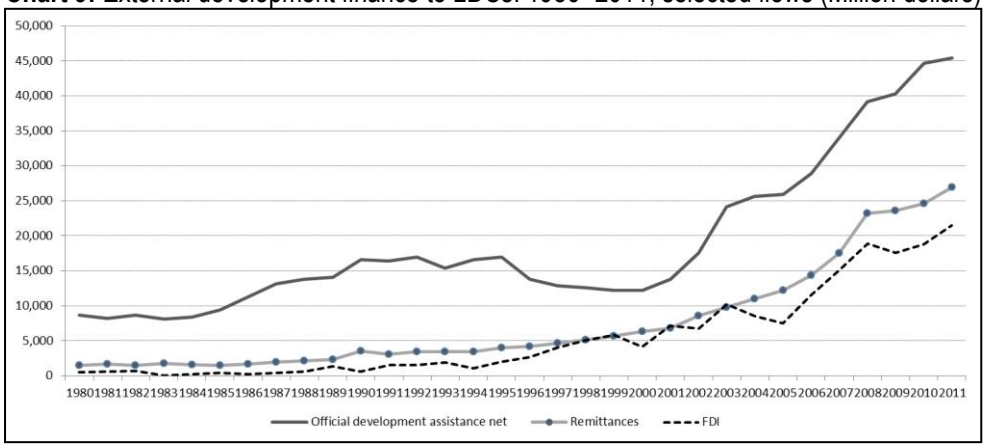
As far as services are concerned, LDCs typically run a deficit in the services account. As a group they tend to record a surplus in Travel services, once again reflecting the importance of in-bound tourism in their economies.

2.3.1. Financing the gap: role of aid and worker remittances

LDCs registered trade surpluses in 2006-2008, but from the perspective of the past three decades this was an "exception to the rule". Moreover, these positive trade balances were due primarily to fuel exporting countries and, to a lesser extent, to mineral exporters. Because LDCs cannot finance their structural deficit on private markets as do some high-income countries, these deficits could exist in the long-term without leading to unsustainable external debt only because they were financed from other external sources, such as official assistance (including debt cancellation) or workers remittances.

Although data are not available for all LDCs, Chart 9 indicates the importance of foreign direct investment (FDI), Official Development Assistance (ODA) and worker remittances. Between 1980 and 1999, ODA, remittance and FDI flows increased by an annual average of 1.8%, 7.4% and 13.4% respectively; while the corresponding growth figures for the years 2000 and 2011 were much higher at 12.6%, 14.1% and 16.1%. The global crisis affected only FDI flows, which declined by 7% in 2009. Besides its financial importance for balance of payments, FDI plays a fundamental role in transferring technology and skills to LDCs. [7] FDI caught up the lost ground in 2010 and continued to grow by a further 14% in 2011 thanks to inflows coming notably from emerging Asian economies. Albeit at relatively decelerated rates, both ODA and remittances kept growing during the crisis.

Chart 9: External development finance to LDCs: 1980- 2011, selected flows (Million dollars)



Notes: Partial coverage only; data on development assistance from private funds or official south-south partners are missing, as well as other flows of importance such as debt relief and budget support.

Source: OECD, World Bank and UNCTAD.

Remittance receipts of LDCs had nearly doubled from US$3.5 billion in 1990 to US$6.3 billion in 2000. Between 2000 and 2011, remittances quadrupled to US$27 billion. The magnitude of ODA was twice that of remittances and three times of FDI in 2000. In 2011, ODA was only one and half times bigger than remittances and double that of FDI mainly due to budgetary constraints in the developed economies. However, official figures underestimate actual flows of remittances. According to World Bank (2010), if remittances sent through informal channels are included, total remittances could be as much as 50% higher than the official record. Remittance flows have offset large trade deficits in many countries like Bangladesh and Nepal and enabled these countries to maintain a current account surplus (Mohapatra, Ratha and Silwal, 2010). Moreover, they constitute a significant complement to domestic income, about 8% of GDP in average of the LDCs in 2011 according to World Bank data. In some cases (Haiti, Lesotho, Nepal, Liberia and Samoa) remittances are higher than 20% of GDP. In addition to providing a supplement to household income, resources from remittances have been directed to investments in infrastructure, education and health, among others (Varma, 2009).

[7] In 2011, at US$21 billion, FDI flows to the LDCs accounted for only 1.3% of world FDI according to UNCTAD. More positively, FDI to the LDCs takes mainly the form of greenfield projects rather than mergers and acquisitions between existing firms.

3. Trade policy and preferential market access

LDCs have benefited from a series of preferential market access to developed countries, promoted under the "Enabling Clause" and the Generalized System of Preferences (GSP) or resulting from bilateral or regional agreements. [8] More recently, South-South trade preferences were promoted with the establishment of the Global System of Trade Preferences among Developing Countries (GSTP). In December 2005, the Sixth WTO Ministerial Conference in Hong Kong adopted a decision to extend LDCs' duty-free quota-free (DFQF) market access granted by developed countries to at least 97% of tariff lines. India became the first developing member country to announce its intention to implement the decision in April 2008; since then a growing number of developing countries have also granted specific preferences to LDCs. The utilization and effectiveness of such preferences have been intensively debated in the development economics literature (see Hoekman and Ozden, 2005 for a review).

3.1. LDC trade policy

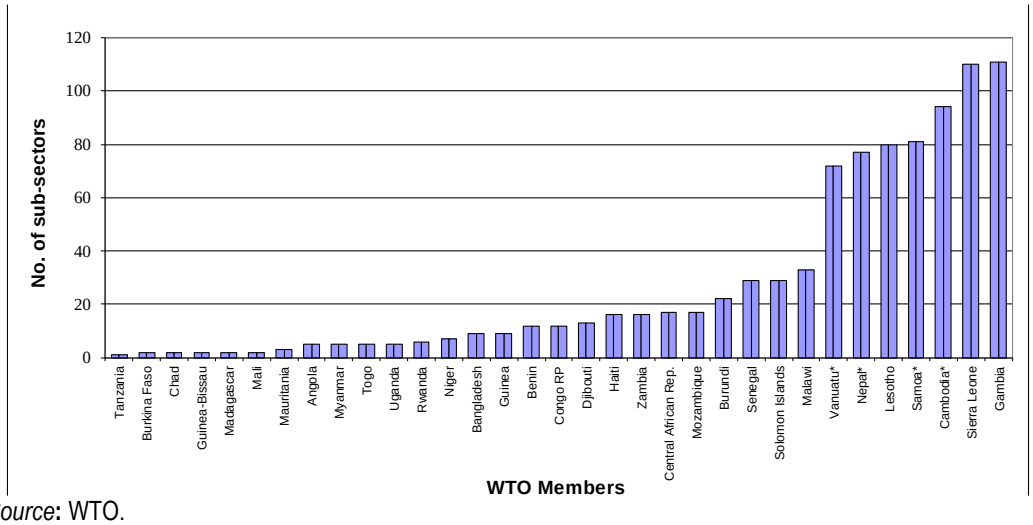
LDC tariff policy is usually characterised by high bound and applied tariffs, and incomplete binding. As shown in Diakantoni and Escaith (2009), LDCs tend to apply high duties (with some exceptions). The bound tariffs and the binding overhang (difference between bound and applied tariffs) are higher for agriculture than other products (Table 3).

Table 3: Average tariff profile of LDC countries, 2011 (Percentage)

pplied MFN Tariff [a]			Binding Coverage b		Average Bound Tariff [a]		
Total	Agriculture	Other products	Total	Non-Agriculture	Total	Agriculture	Other products
11.7	14.8	11.3	59.3	53.2	59.9	73.7	42.6

Note: [a]: ad valorem and equivalent, simple average of countries' tariffs; [b]: percentage of tariff lines.
Source: Based on World Tariff Profile 2012, ITC-UNCTAD-WTO

With respect to services, the difference between the existing (or applied, using the term used in tariff) LDC trade openness in services and their GATS (binding) commitments is now quite wide according to Gootiiz and Matoo (2009) and Honeck (2012). In order to attract FDI, many LDCs have already fully opened a wide range of services sectors. As seen in Chart 10, the number of existing GATS commitments varies widely among the LDCs by subsector, ranging from over 110 (Gambia and Sierra Leone) to only 1 or 2 sub-sectors (Burkina Faso, Chad, Madagascar, Mali and Tanzania).



Source: WTO.

Figure 10: LDCs GATS Commitments, 2012

[8] Among the specific LDC schemes are Canada's Least Developed Country Tariff (LDCT) and the EU's everything but Arms (EBA) initiatives. In addition, LDCs and other developing countries have benefited from regional preferential schemes, such as the EU's arrangement for Africa, Caribbean and Pacific (ACP) countries and the US' African Growth and Opportunity Act (AGOA) and Caribbean Basin Initiative (CBI).

3.2. Preferential market access

In terms of market access conditions for their exports, LDCs benefit from lower tariff duties for their merchandise exports, either because they tend to export on tariff lines with low MFN tariff (fuels and minerals) or thanks to preferential schemes. As shown in Table 4, the situation varies according to the markets of destination (developed vs. developing economies) and the type of exported products. On agricultural products, the average margin of preference over MFN treatment (6 percentage points) granted to LDCs exports is similar for both developed and developing countries. Nonetheless, the resulting best tariff remains much higher when the products are shipped to developing countries (7.6%) rather than industrialised ones (2.2%). On non-agricultural products, the situation is reversed. LDCs exports to other developing countries benefit from very low margin of preference, yet the best tariff applied is usually lower (1.1% in average) than in developed countries (2.3%).

This apparent paradox is explained by the different product composition of South-North and South-South LDCs exports. True preferential treatment, after discounting those tariff lines that are not dutiable under the common MFN treatment, is considerably lower for exports to developing countries as only a few emerging countries have operative preferences in place. Low applied duties on South-South trade results from trade being largely dominated by exports of primary commodities (fuels and minerals) that have a very low MFN tariff while South-North exports are more concentrated on those processed goods and other manufactures that benefit from higher preference margin (4.2 percentage points).

Table 4: Exports of LDCs to developed and developing markets, per sector and duties faced, 2011 or closest year (Million dollars and percentage)

Market of destination	Sector	Trade value (Mn$)	MFN tariff average [a]		Preference	Best tariff	DutyFree Imports	
			Simple	Weighted			% of TL	% of Value
Developed countries	Agriculture	3,467	51.0	8.2	6.0	2.2	99.6	98.6
	Other	45,503	5.3	6.4	4.2	2.3	90.9	86.1
Developing countries	Agriculture	4,069	15.4	13.5	5.9	7.6	54.5	61.8
	Other	65,310	8.6	1.6	0.6	1.1	56.3	81.1

Notes: a: Traded tariff lines only.
Source: Based on World Tariff Profile 2012, ITC-UNCTAD-WTO

3.2.1. Facilitating trade and operationalizing market access preferences

All the above mentioned indicators based on best applicable tariffs are established on the hypothesis that available preferences are fully used by the exporters. This may not be the case for a number of reasons; ranging from ineligibility –due to non-conformity to some criteria such as rules of origin or non-tariff measures– to excessive administrative cost to benefit from the preferential scheme. Other limitations are closely related to supply-side issues rather than pure trade questions. For example, sanitary and phytosanitary standards (SPSS) are often an obstacle for agricultural exports to developed countries. Using the example of Senegal, Mbaye and Gueye (2014) relate how the issue of pesticide residues has become an issue for African exports to Europe over the past several years.

The specificity, design and application of rules of origin can make it difficult for LDC exporters to benefit from preference schemes. Strict rules of origin (or regional cumulation) were justified on the ground that they help in promoting integrated production structure in the recipient country. This aim is now questioned as manufacture production is increasingly performed in the context of global industrial networks (Zedillo *et al*, 2005; Jara and Escaith, 2012). This is a particular problem in textiles and apparel, which are key exports for LDCs, as recalled during the 9th WTO Ministerial in 2013. Looking at agriculture, Bureau *et al*. (2006) find that the overall rate of utilization for non-reciprocal preferences is high in the case of the EU and the USA (89% and 87%) thanks, in part, to the various options offered to exporters that allow avoiding the most demanding schemes. When exporters to the EU or the US have the choice, they favor Cotonou in the case of EU, or CBERA in the case of the US. Controlling for tariffs, the authors infer that administrative requirements, rules of origin or predictability of

the respective regimes are potential determinants of the choice between regimes, Bureau, Jean Claude, Raja Chakir and Jacques Gallezot (2006).

Thanks to leaner administrative procedure and simpler rules of origin, utilization rates of preferential treatment in developed countries have steadily improved in the past decade and are now at an average of 90 %. No data are available yet for the utilization of preferences granted by developing countries. It is often stated that preferences lower than 4 percentage points do not materialize in significant competitive advantages and lead to low preference utilization. On this last point, however, recent research shows that they may still matter below such threshold. Keck and Lendle (2012), using US import data, find that utilization rates remain often very high, even for very small preferential margins. Measuring the actual impact of preference remains an empirical debate due its statistical complexity. Disdier *et al*. (2013) develop a dedicated database for 1996 and 2006 and find that the impact on LDCs and non-emerging developing countries was more at the intensive margin than at the extensive one (export diversification). Besides the empirical debate, the fact that preferences are generally fully utilised by exporters tend to suggest that these preferences have positive effects.

Another constraint for diversification is that better LDC preferences, even when fully utilized, are counterbalanced by higher transaction and transportation costs that reduce LDCs' competitiveness vis à vis their main competitors. Trading involves a series of transaction costs — delays, documents and administrative fees — that increase domestic prices. When these costs are significantly higher than those of the competitors, as it is often the case in LDCs, they may lead to loss of market share or missed business opportunities. These costs are part of the supply constraints that frequently reduce the international competitiveness of LDCs and limit their trade potential.

The comparison of transaction costs confirms that LDCs face a comparative disadvantage when exporting goods (see low income countries in Table 5). According to UNCTAD (2007) CIF/FOB difference for Africa was 10 per cent in 2005, compared to a world average of 6 %. ECE (2003) reviews a series of transport cost studies for developing countries and conclude that a large part of the disadvantages faced by Southern Africa has to do with transport costs; this problem being particularly acute for landlocked countries. As mentioned by Djankov *et al* (2010), each additional day that a product is delayed prior to being shipped reduces trade by more than 1%. The delays are particularly damaging for time-sensitive goods, such as perishable agricultural products, which are of particular interest to LDCs as they are both labour intensive and high value-added

High international trade costs are usually correlated with poor inland transportation infrastructure which reduces not only the potential for international trade but also dampens the possibility for small producers in remote areas to tap the potential of regional markets. The issue is particularly acute for Sub-Saharan Africa (Buysa *et al*., 2010) but is also representative of the situation of most large LDCs,

Cross-border bottlenecks such as border procedures, cumbersome documentation or complex and mismanaged regulations reduce the competitiveness of LDCs exports. They act like a tax on the income of the exporters who are "price takers" and cannot include the higher transaction costs into their bidding prices. The problem, as we shall see later, is compounded when LDCs intend to diversify by joining global value chains. Delays in delivery and the necessity to maintain high inventory levels to cope with them run against the core management model of international supply chains, based on just-in-time and minimum buffer stocks. Indeed, the issue was deemed serious enough for the WTO to devote its entire 4th Global Trade Review of Aid for Trade in 2013 to the role of trade facilitation in helping LDCs joining global value chains[9].

Table 5: Logistics Performance Index by country grouping, 2012

Country grouping [a]	LPI [b]	Customs	Infras-tructure	International shipments	Logistics competence	Tracking & tracing	Time-liness
High income	3.55	3.36	3.56	3.28	3.5	3.65	3.98
Upper middle income	2.82	2.49	2.54	2.86	2.71	2.89	3.36
Lower middle income	2.59	2.23	2.27	2.66	2.48	2.58	3.24
Low income	2.43	2.19	2.06	2.54	2.25	2.47	2.98

Notes: [a]: According to World Bank specifications; [b]: Logistics Performance Index (LPI) is the weighted average of the country scores on six key dimensions: Efficiency of the clearance process by border control agencies; Quality of trade and

[9] "Fourth Global Review of Aid for Trade: Connecting to value chains" 8-10 July 2013, Geneva.

transport related infrastructure; Ease of arranging competitively priced shipments; Competence and quality of logistics services; Ability to track and trace consignments; Timeliness of shipments in reaching destination within the scheduled or expected delivery time. The index ranges from 1 to 5, with a higher score representing better performance.

Source: Logistics Performance Index: Connecting to Compete 2012, World Bank.

Trade facilitation is vital for LDCs as it will reduce costs for traders. It will also boost intra-regional trade, which is often the first exporting step for small and medium sized domestic firms. It is particularly important for African least developed and low-income countries, many of them being land-locked. For these landlocked countries, the average customs transaction costs was almost 240% higher than other LDCs in 2012; and it took more than 40 days to ship a container, compared to the already long 27 days necessary to get things done in other LDCs.

Table 6: LDCs cost to export, 2010 and 2012

	Cost to export (US$ per container)		Documents to export (number)		Time to export (days)	
	2010	*2012*	*2010*	*2012*	*2010*	*2012*
Total LDCs	1818	1860	7.6	7.6	33.8	32.5
- Landlocked	2885	2977	8.6	8.5	44.6	42.4
- Non-landlocked	1230	1244	7.1	7.1	27.9	27.0

Source: Based on World Bank data

Besides trade facilitation, the overall reduction in tariff barriers obtained through MFN or preferential agreements means that additional issues such as non-tariff barriers, compliance with sanitary and phyto-sanitary standards, are getting more and more attention.

4. The way ahead: export diversification and trade in tasks

While LDCs "surfed" relatively well through the Great Trade Collapse of 2008-2009, their next challenge is the probable conclusion of the "super cycle" that kept the international prices of most commodities at historically high levels. The second phase of the Great Global Transition is driven by further changes in the sources and origin of global demand, in particular the shift in the main sources of China's growth. The reduction of public investment in infrastructure and heavy industry in this country may reduce the growth of imports of minerals and fuels, driving down their international prices. The future of oil prices is further obscured considering that the USA is progressively becoming self-sufficient thanks to the exploitation of new sources of gas. This reversal will/may catch the LDCs in a situation of renewed external vulnerability, as their trade balance has returned into negative territory after the 2008-2009 crisis.

In order to avoid returning to the boom-and-bust pattern that characterized their growth in the past, it is increasingly necessary for LDCs to diversify their exports into new (labour-intensive) activities. One traditional determinant of trade performance for least-developed countries is product and market diversification. Services, in particular tourism, are an example of such diversification. In the case of merchandises, this strategy has more recently been enriched with additional possibilities created by the changes in consumer preferences ("trade in varieties"), on the one hand, and the way manufactures production is now organised along global supply chains ("trade in tasks").

Our first option for product upgrading is tapping the new potential created by consumers' demand for varieties to increase revenue per unit of output. Quality control (such as reducing pesticide content and improving handling and storage facilities, as suggested by Mbaye and Gueye, 2014 in the case of Senegal), labelling and branding are being used by producer of agro-food products to extract a better price from their traditional exports. "Trade in varieties", including organic farming certification and labels of origin, allows small producers to benefit from niche markets and should now be considered as export diversification.

The other option is the possibility of joining global production networks and exporting particular "tasks" rather than entire finished products. Trade in tasks and global value chains are among the important markers of international trade in the early 21st century; Jara and Escaith (2012) review the implications on global governance, trade policy and trade statistics. By accelerating the transmission of technology and know-how, this trend contributed greatly to the rapid industrialization of emerging countries in the past 15 years. Actually, most of

the East Asian miracle can be attributed to trade in tasks; and even China's rapid march towards industrialization relied on global supply chains (see WTO and IDE-JETRO, 2011).

Yet, with a few exceptions, connecting to global production networks in order to benefit from these new opportunities is a formidable challenge for most LDCs. The usual points of entry for LDCs into global value chains are agro-food, clothing and tourism sectors. Nevertheless, as highlighted by P. Lamy (WTO, 2013b), in a new global world where connection to industrial networks is the key to industrialization, least developed countries are also the "least connected countries". With these caveats in mind, the overall picture is not negative when looking at the trend of intermediate goods imports. LDCs imports of such goods have increased from US$18 billion in 2000 to US$87billion in 2012, which represents an average annual increase of 14% in comparison to the world average of 8%.

Using network analysis, Escaith and Tamenu (2013) analyse the topology of LDC trade in imports of intermediate inputs and in exports of final goods. They observe the rise of China as a key supplier of intermediate inputs to LDCs during the 2000s. Even if EU27 remains the lead supplier of LDCs (many of them being in Africa), its dominant position was much eroded between 2000 and 2011. Surprisingly, the USA is not such an important source of supply for LDCs, even in 2000. The 2011 trade network is less “dense” than in 2000, pointing towards a better geographical diversification of LDCs sources of supply. Yet, trade in intermediate inputs is very heterogeneous within the LDC group. Bangladesh is by far the largest LDC importer of intermediates (US$21 billion in 2012, up from US$5 billion in 2000), followed by Angola (US$8 billion in 2012). Bangladesh alone accounted for 24% of LDCs total imports of intermediate goods in 2012.

South-North trade remains predominant when it comes to LDCs export market of the labour intensive products (agri-food and manufactures) that are typically the result of GVCs. EU27 is the most important trade partner for this type of exports and USA’s role is also prominent. China’s imports, though growing during the decade, remains secondary while India emerged as one of the main regional importers of LDCs final goods during the 2000s.

Besides tracking trade flows of intermediate and final goods, countries' and sectors' participation in global value chain is given by a new measure of trade called "trade in value added". Using inter-linked input-out matrices, the idea is to track down for each industry in each country the use of domestic and imported inputs, in order to estimate the foreign and domestic content of output, including exports (see OECD and WTO, 2012 for a presentation of the methodology). The OECD-WTO Trade in Value-Added (TiVA) database is intensive in the use of trade and structural data and it relies only on official data sources. For this reason, only one of the 57 countries covered (Cambodia) was an LDC at the time of writing this document. But the results obtained on this country are illustrative, even if they cannot be counted as representative.

Cambodian exports of manufactures are concentrated on "clothing", by far the major manufacturing sector represented in LDC exports (60% of LDCs' manufactured products, WTO 2013b). The foreign value-added content in Cambodian exports of clothing, estimated at 63% in 2008 is much higher than what is observed for developing economies and the world average (around 25%). 10 This high share reflects the fact that LDCs usually insert themselves in GVCs thanks to their comparative advantage in terms of labor cost for assembling or processing imported intermediate components. This processing trade, typically done in "Export Processing Zones" relies on imported inputs to produce and export goods for lead foreign companies. For other developing countries that have been moving-up on the value-chain ladder, 75% of their exports in "textiles and textile products, leather and footwear" were based on domestic value added. Moreover, while most of the domestic value added of Cambodia's textiles and clothing exports were destined for final consumption, two-thirds of other developing countries exports were further processed in other countries, showing a deeper insertion as upstream suppliers in international supply chains.

The UNCTAD-Eora dataset that was developed for UNCTAD (2013), extends trade in value-added calculation to 187 countries. In contrast to WTO-OECD TiVA, Eora uses an algorithmic approach to fill data gaps when actual statistics are missing (for a review of the methodology, see Lenzen *et al*., 2012). On the basis of these estimates, the foreign content of LDCs exports (an indicator of supply chain vertical integration) is low (14%) in average of all industries, only half the world average (28%).11 For comparison, the group of developing

[10] The "Foreign value added content of exports" corresponds to the inputs that were imported to produce the exported goods and services, net of any domestic content that could have been incorporated in the production of these inputs.

[11] It may be counter-intuitive to use foreign input content in exports (or "vertical specialization", as in Hummels *et al*. 2001) as an indicator of product sophistication and insertion in global value chains. This paradox is only apparent; manufacture (often considered as "high value-added" activity) is in fact characterized by low added-value per unit of output compared to

economies relies on foreign content for 25% of the value of its exports, a proportion that climbs to 30% in East and South East Asia.

LDC suppliers face significant obstacles at most stages for entering and then moving up the value chains. The result of an OECD-WTO survey on the main obstacles identified by private and public stakeholders when joining a GVC were presented at the 4th Global Review of Aid for Trade: Connecting to Value Chains (WTO, 2013b). While value chains are inherently sector-specific, some horizontal conditions across sectors determine firms' abilities to economically upgrade and connect to value chains. 12 Contrary to what is often believed, low production costs do not always substitute for quality when it comes to attracting lead-firms' contracts. 13 Among the main obstacles that LDC firms face in connecting to value chains, more than half of the partner countries identified inadequate domestic infrastructure as the foremost issue, followed by access to trade finance and compliance with SPS or technical standards. Support through better market access, feature high among LDC suppliers (identified as such in 73% of the responses to the survey) as well as among lead firms (44%). Lead firms cited trade facilitation measures (44%) as the most crucial area where support would be effective in bringing LDC suppliers into value chains. Other major areas of support cited are in labor force training (51% of LDC suppliers) and improving public-private dialogue with national authorities (43% of lead firms).

In the context of global value chains, where costs are only one factor of competitiveness to be complemented by just-in-time delivery and reduced logistic and transaction costs, trade facilitation is taking an increasing role in fostering export diversification. In contrast to the more traditional export-led policy, improving import efficiency is also an area that requires additional attention; since in a global production network, access to competitive imports is a key component of the trade strategy. As highlighted by the result of the 4th Global Review, too frequently aid-for-trade programmes fail to exhibit sufficient concerns about this dimension of competitiveness. But border facilitation is just one factor of the new policy equation. From the GVC perspective, investment and trade are inextricably intertwined and other behind-the-border considerations (often referred to as "WTO +" or "WTO X" measures governing market and investment behavior, regional trade agreements, intellectual property regime and business facilitation policies) become particularly relevant (WTO, 2011 and UNCTAD, 2013). Moreover, as highlighted in Milberg and Winkler (2013), insertion in GVCs should not be seen as a risk-free panacea: in a market characterized by quasi-monopolistic organizations, competitive advantages and lead-firms' strategies may change rapidly.

Conclusion:

A perceptible shift in LDC trade has taken place in the past decade, thanks to the rebalancing of global demand towards large emerging countries and the resulting long-lasting cycle of high international commodity prices. This process resulted in a wider geographical diversification of LDCs' exports but contributed to a higher concentration of exports revenues on a few basic commodities. The latter is most entirely due to a price effect. Indeed, trade statistics show some successful example of diversification in labour-intensive activities, such as textiles and clothing or services, particularly tourism.

From a quantitative perspective, the picture that emerges so far from the changes to the sources of global trade and growth that resulted from the Great Global Transition is positive for the LDCs in both absolute and relative terms. The LDCs' total exports of goods and commercial services registered an annual average growth of 15.5% between 2000 and 2012; higher than other developing economies whose corresponding exports increased on average by 12% per year during this period.

Notwithstanding some progress in market and product diversification, LDCs' trade remains concentrated on a few products, increasing the fluctuation of export revenues due to variation in international prices. The vulnerability is accrued when considering that, with the exception of 2006-2008, the LDCs as a group have systematically recorded a trade deficit. Actually, net trade balances started diverging dramatically in the early

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primary or tertiary sectors. Upstream industries (agriculture, mining) that rely less on domestic or imported inputs have typically much higher value-added coefficients (up to 100% in the case of subsistence agriculture which does not use commercial inputs such as fertilizers or improved seeds).

[12] The exercise conducted by OECD and WTO was based on self-assessments from 80 developing countries and 52 bilateral and multilateral cooperation agencies. On the business side, 524 supplier firms in developing countries and 173 lead firms were surveyed. The survey includes sector-specific issues for agro-food production, tourism, textiles and apparel, information and communication technology, transport and logistics.

[13] Better said, price and quality can be substitutes, but only up to a certain point. Sutton (2012) shows that wage adjustments cannot fully compensate for poor levels of productivity and quality. More generally, trade in "varieties and qualities" are features that weight more and more on export diversification and product up-grading.

2000s, reflecting a deeper heterogeneity in the situation of individual countries. Fuel exporters record persistent trade surpluses while the non-fuel LDC exporters have to resort to external resources to finance their growing trade deficits. Their merchandise export revenues cover does not cover more than 57% of their merchandise imports. The situation is particularly acute for LDCs that specialize in agricultural exports.

The 2008-2009 global crisis and the bumpy recovery that followed illustrate the fragility of the recent trends. A slowdown in the growth of large emerging countries and a more inward oriented economic policy in China and other "emerged" economies may put an end to the unprecedented commodity "super-cycle" that lifted the value of LDCs exports since 2003. From such a perspective, renewed efforts towards product diversification are called for.

The efforts of diversifying away from minerals and fuels to labour-intensive products such as agriculture, textiles and clothing has been supported for many years by preferential market access to developed countries. More recently, emerging countries have also been granting such preferences to LDCs product. Despite the worldwide trend of lowering external tariffs through MFN or regional preferential treatment that gradually erodes LDCs margin of preferences, a closer analysis reveals that these countries still benefit from significant preferences, in particular in agriculture.

In the face of changes in consumer behavior, fostering quality control, labelling and branding are some of the options available to diversify at the intensive margin. The objective here is to upgrade by tapping the new potential of niche markets for traditional agro-food exports ("*trade in varieties*"). The rapid development of international production networks as part of the new business model of global value chains offers also new opportunities for export diversification on "*trade in tasks*" at the extensive margin. Because the activities focus on a small part of the value-chain and is often developed in cooperation with lead firms, this new form of industrialisation is particularly relevant for alleviating the supply-side constraints that limit LDCs' export diversification.

On the other hand, competition is fierce and GVC participation cannot materialize without a proper conducive environment. For many LDCs, one of the main obstacles for joining GVCs remains deficiencies in trade and transport facilitation which entail high cost for importing the necessary inputs and exporting the processed goods. Active trade facilitation programmes offer new options to LDCs for joining GVCs. Trade facilitation is also important for improving producers' income, because the price they receive for their products is partly determined by the cost of moving the goods from the farm to the end-markets. For those, like Bangladesh or Cambodia, that have already been able to join these global production network, up-grading towards higher "value-added" activities requires more encompassing horizontal policies.

Finally, in the on-going Doha Round negotiations, the special and differential treatment of LDCs has received increasing attention since 2008. Notwithstanding the difficulties in reaching a global agreement on the various issues to be negotiated, the "LDC package" appeared as a low-hanging fruit. Besides, agreeing on trade facilitation, the WTO members confirmed in December 2013 at the 9th Ministerial Conference in Bali, the importance of trade facilitation and Duty-Free and Quota-Free market access for LDCs. The challenge now is to operationalize such special and differential treatment in a way that enables recipients to eventually graduate out of the LDC category.

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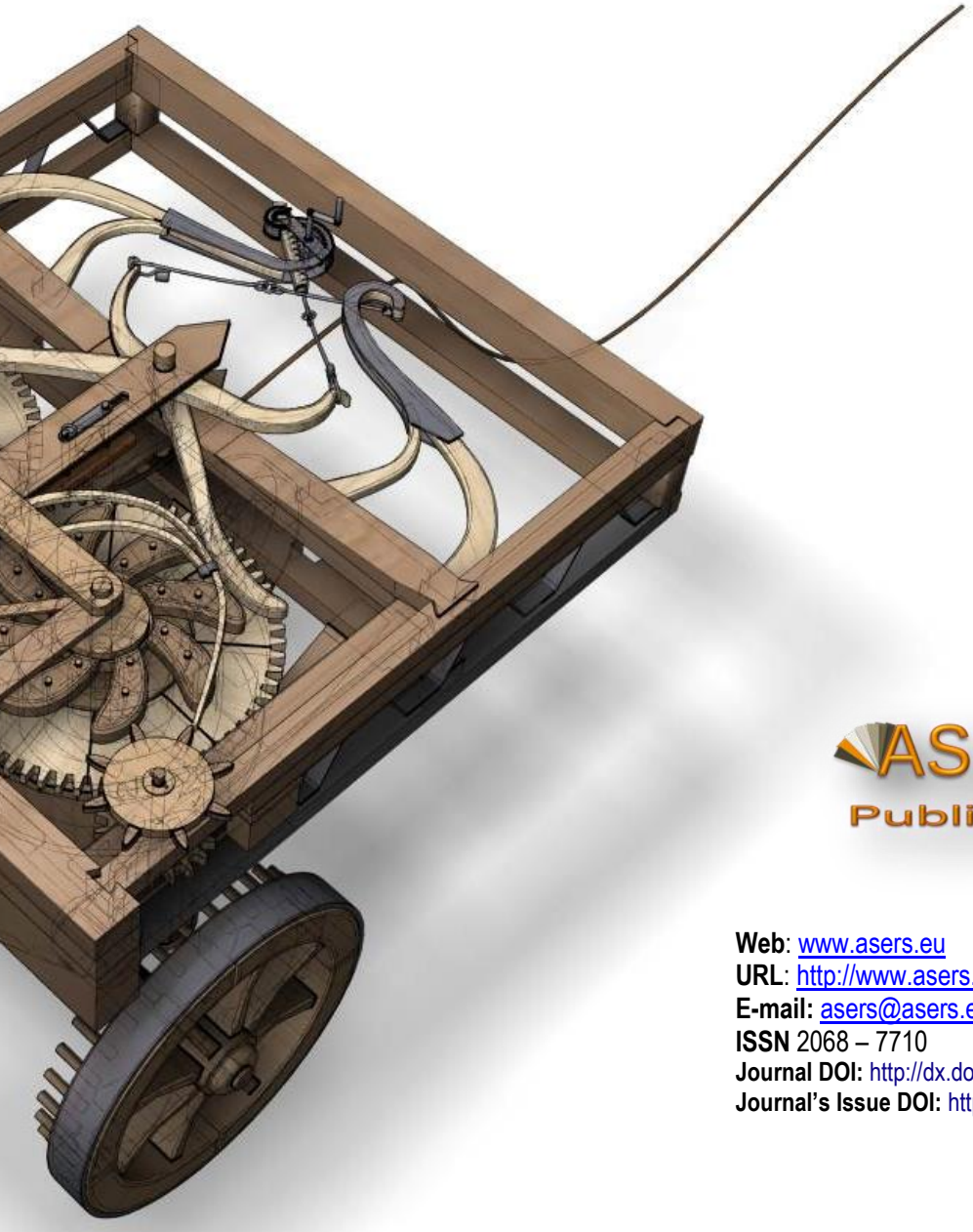

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