

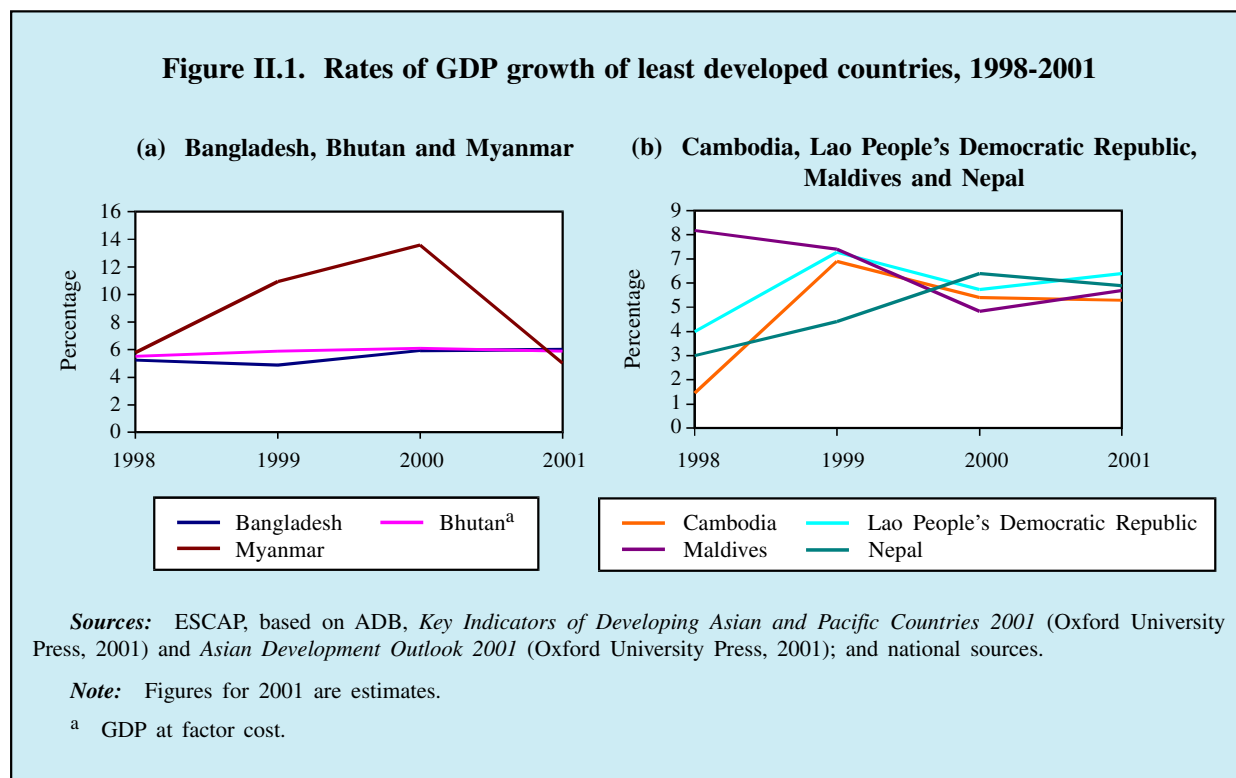
DEVELOPING ECONOMIES OF THE ESCAP REGION

Asian least developed countries¹

Overview and prospects

Economic performance in 2001 was reasonably stable

The least developed countries of Asia did not generally experience the very sharp falls in output seen in some other countries in the region and GDP growth continued in 2001 (figure II.1). The effects of flooding on agriculture were not as damaging as had originally been feared in several countries and industrial growth has held up reasonably well, particularly where hydropower development projects have stimulated construction. Tourism receipts were down in many cases, but the service sector was buoyed up in some countries by increased sales of electricity. However, signs are emerging of a delayed response to the global slowdown and the outlook for GDP growth is less bright in 2002.

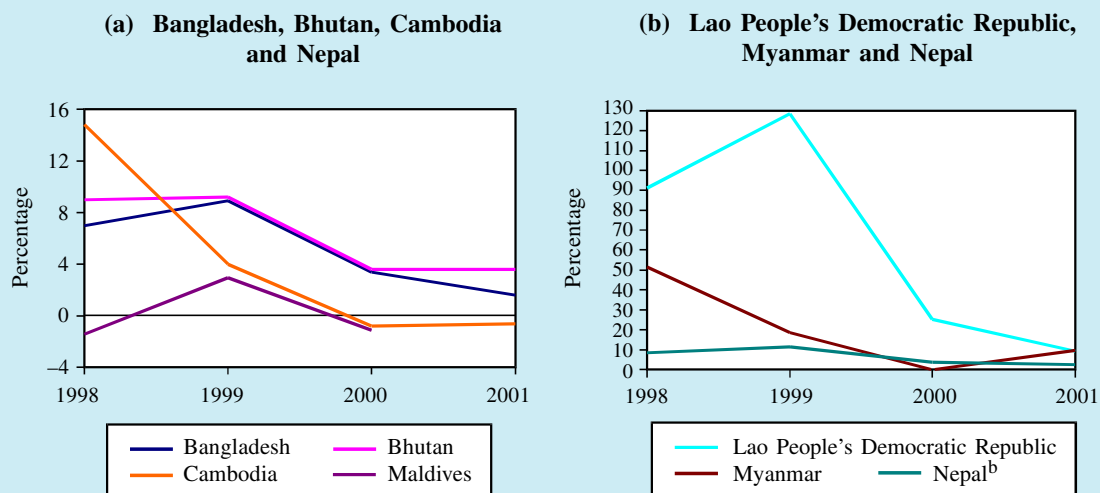


¹ The Pacific island least developed countries are discussed in a separate section in this chapter.

Consumer prices were stable or declined in most of the Asian least developed countries in 2001 (figure II.2). This was in part a reflection of declining commodity prices on world markets and improvements in the food situation in the countries of South Asia; food prices were generally stable in the South-East Asian least developed countries as well, despite widespread flooding. Some of these countries also benefited from local use of the United States dollar, as this kept import prices down. The outlook as regards inflation, however, is not so encouraging. In the South Asian least developed countries, cost-push pressures could arise from weakening exchange rates due, in turn, to large fiscal deficits or accommodative monetary policy, and increased fuel and utility charges and additional taxes. In South-East Asia, macroeconomic stabilization efforts in Cambodia and the Lao People's Democratic Republic, which have contributed to price stability in recent years, are likely to continue. However, exchange rate depreciation and increases in the prices of petroleum products and electricity will add to inflationary pressures in the medium term.

Price pressures remained weak

Figure II.2. Inflation of least developed countries, 1998-2001^a



Sources: ESCAP, based on ADB, *Key Indicators of Developing Asian and Pacific Countries 2001* (Oxford University Press, 2001) and *Asian Development Outlook 2001* (Oxford University Press, 2001); IMF, *International Financial Statistics*, vol. LIX, No. 10 (October 2001); and national sources.

Note: Figures for 2001 are estimates.

^a Changes in the consumer price index.

^b National urban consumer price index.

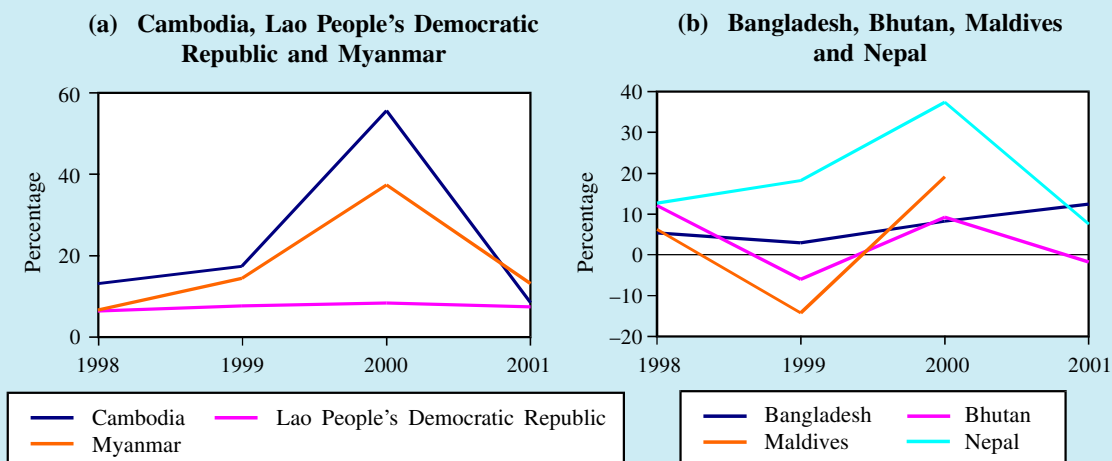
The global slowdown affected some exports

Merchandise exports from the Asian least developed countries generally grew more slowly, partly as a result of the effects of the global slowdown (figure II.3). Exports of manufactures, particularly ready-made garments, were adversely affected. Service receipts were also down as tourism suffered in many of these least developed countries, especially after the events of 11 September 2001; however, an encouraging sign was the increase in the number of Asian tourists seen in some countries. The import picture (figure II.4) was more mixed, with many countries experiencing a decrease in imports as fewer inputs were needed for the ready-made garment industry.

FDI flows remained very low

Inflows of private capital for investment in the Asian least developed countries have been low. ODA flows remained stable or increased, often quite substantially, in all these countries apart from Bangladesh, where disbursements have slowed, and Myanmar, where such flows have largely been absent for many years. Official reserves remained low in most cases, and the amounts of external debt were much higher in the South-East Asian least developed countries than in South Asia. Myanmar has significant debt arrears; the level of external debt is being carefully monitored in the Lao People's Democratic Republic; and Cambodia has

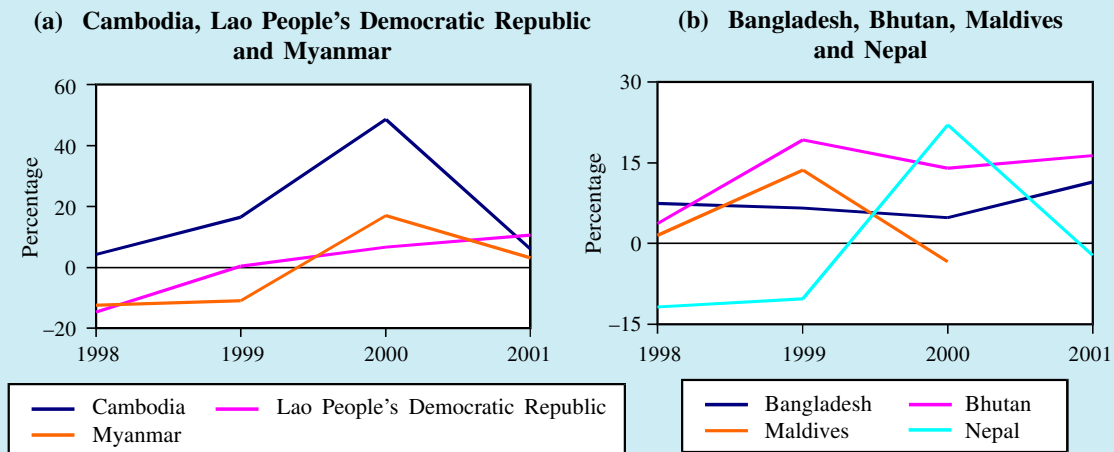
Figure II.3. Growth rates of merchandise export earnings of selected least developed countries, 1998-2001



Sources: IMF, *Direction of Trade Statistics* (CD-ROM), February 2002, *International Financial Statistics* (CD-ROM), January 2002, and web sites <<http://www.imf.org/external/np/sec/pr/2001/pr0118.htm>> and <<http://www.imf.org/external/country/index.htm>>, 18 February 2002; ADB, *Asian Development Outlook 2001* (Oxford University Press, 2001); and national sources.

Note: Figures for 2001 for Myanmar are for January-September; figures for Bangladesh, Bhutan and Nepal are for the fiscal year.

Figure II.4. Growth rates of merchandise import spending of selected least developed countries, 1998-2001



Sources: IMF, *Direction of Trade Statistics* (CD-ROM), February 2002, *International Financial Statistics* (CD-ROM), January 2002, and web sites <<http://www.imf.org/external/np/sec/pr/2001/pr0118.htm>> and <<http://www.imf.org/external/country/index.htm>>, 18 February 2002; ADB, *Asian Development Outlook 2001* (Oxford University Press, 2001); and national sources.

Note: Figures for 2001 for Myanmar are for January-September; figures for Bangladesh, Bhutan and Nepal are for the fiscal year.

completed outstanding bilateral debt rescheduling agreements. National currencies in the South Asian least developed countries showed a downward trend in 2001, in several cases affected by a similar trend in the Indian rupee. Exchange rates were relatively stable in the South-East Asian least developed countries in the first half of 2001, but showed signs of some instability thereafter. Generally however, the outlook for 2002, is for continued currency weakness.

Most of the Asian least developed countries have been grappling with issues related to economic development combined with greater equity. However, Afghanistan will have to confront the huge and pressing tasks of resettlement, rehabilitation and reconstruction for several years to come (see box II.2). Good governance is high on the policy agenda, along with wide-ranging structural reforms, to ensure a sustained focus on poverty alleviation among the least developed countries. This task has been aggravated somewhat by domestic security and stability problems in a number of Asian least developed countries. However, trade liberalization through existing or future membership in WTO provides opportunities for future growth and transformation, especially in an auspicious external environment.

Reforms are high on the policy agenda

Box II.2. Rehabilitation and reconstruction of Afghanistan^a

“By working together, we have every chance of mounting the kind of fully integrated approach to recovery that is needed to help Afghan people to reap the rewards of peace”.

– Kofi Annan, Secretary-General of the United Nations (Brussels, December 2001)

The initial conditions and circumstances

Afghanistan, one of the poorest countries in the world, was recognized as a least developed country even prior to the prolonged war and conflict of more than two decades. Its economy is heavily dependent on agriculture, with only a small share in manufacturing. Apart from the devastating war, further damage to the agrarian economy has been caused by drought over the past three years. Out of an estimated population of 25 million, about one fifth are living as refugees in neighbouring Pakistan, the Islamic Republic of Iran and other countries. The bleak socio-economic position of Afghanistan can be seen from the data and information below.^b

- GDP per capita is less than \$200.
- Four out of five people are not literate; the education system has collapsed; and enrolment rates, particularly for girls, are extremely low.
- One in four children dies before the age of 5, half are malnourished and a third of the survivors are orphans.
- The maternal mortality rate is among the highest in the world.
- Adult life expectancy is just 44 years.
- Three out of four persons lack access to safe drinking water.
- Half of the urban housing stock in major cities has been destroyed or damaged.
- Nearly one in 20 is disabled by land mines.
- An abysmal situation with regard to respect for human rights, particularly those of children and women, has existed for decades.
- There is widespread environmental degradation affecting people's livelihood, health and future prospects.

The political transition process

The Afghan Interim Administration, in place since 22 December 2001 following the Bonn Agreement, consists of 30 members presided over by Chairman Hamid Karzai. The Agreement also established a Special Independent Commission for the convening of the Emergency Loya Jirga (assembly of elders), a Central Bank and a Supreme Court. Under the Agreement, the Emergency Loya Jirga is to be convened within six months of the establishment of the Interim Authority and opened by His Majesty Mohammed Zaher, the former King of Afghanistan. The Emergency Loya Jirga will decide on a Transitional Authority, including a broad-based administration, to lead Afghanistan until a fully representative government can be elected through free and fair elections, to be held no later than two years from the date of the convening of the Emergency Loya Jirga. Lastly a Constitutional Loya Jirga, will be convened, within 18 months of the establishment of the Transitional Authority, to adopt a new constitution for Afghanistan.

^a This box is largely based on United Nations, *Immediate and Transitional Assistance Programme for the Afghan People 2002* (New York, January 2002); and ADB, UNDP and the World Bank, *Afghanistan: Preliminary Needs Assessment for Recovery and Reconstruction* (January 2002).

^b Statistics on Afghanistan's economy have not been published by the Afghan authorities for about a decade and the available data, coming mainly from international sources, are not always consistent or comparable.

The magnitude of the tasks ahead

The successful implementation of any recovery strategy is predicated on durable peace, security and political solutions for the long term.^c The main responsibilities for ensuring these requirements lie with the Afghans themselves. However, the United Nations and the international community can play an important and indispensable role in the process, in several dimensions. Donor funding requirements for 2002, detailed by the United Nations at the International Conference on Reconstruction Assistance to Afghanistan, held at Tokyo on 21-22 January 2002, amounted to over \$1.8 billion for humanitarian assistance, recurrent costs of the Afghan Interim Administration and quick-impact recovery programmes and projects. Joint estimates on reconstruction and rehabilitation made by UNDP, ADB and the World Bank indicate the need for around \$5 billion over 2.5 years, \$10 billion over 5 years and \$15 billion over 10 years. Of the \$4.5 billion pledged at the Tokyo Conference by donors for a 5-year period, commitments for the first year were in line with the funds requested by the United Nations. It is important that these pledges should be translated quickly into disbursements to underpin programme and project implementation in a transparent and coordinated manner.

The scope and focus of rebuilding efforts

There is an urgent need for sustained humanitarian assistance, reconstruction and development activities; these have to be implemented concurrently and yield interrelated and mutually reinforcing outcomes. The development approach to be pursued should be rights-based, such as a commitment to promoting and protecting human rights, particularly those of women, children, minorities and returning refugees; other principles integral to this approach include equitable participation, accountability, transparency, non-discrimination and economic and political empowerment. Moreover, the reconstruction strategy could take the form of a rolling plan that could be further developed and refined through the incorporation of experiences and lessons learned from the previous phases of implementation.

The expected return of some 5 million Afghan refugees or internally displaced persons presents a daunting challenge, including in the complex planning and allocation of future resources. The process involves both initial facilitation measures and longer-term support for the returnees and the communities to which they return. To ensure adequate local leadership, participation and ownership, Afghans at various levels have to be involved in all stages of the programmes and projects concerned, from conception to planning and implementation. This is essential not only to maximize a sense of ownership and participation but also to ensure that religious and cultural sensitivities are taken into account adequately in the process. It may be difficult to find expertise inside the country, since a whole generation has had no education and most people with useful skills have left. The very large numbers of skilled Afghans living in refugee camps constitute a pool of human capital on which to draw for the work of reconstruction. Since most women were not engaged in the conflict and had to carry the burden of agricultural work and finding the means of livelihood, their inclusion, following the provision of education and confidence-building, will be particularly important for the rapid development of the country.

The rebuilding and resettlement processes will have to start from almost nothing owing to the absence of basic services and the loss of such key infrastructure as health-care facilities, schools, transport, power and communications. Quick-impact programmes are also needed to meet short-term priorities, especially for higher food production and more extensive food transport and distribution networks. Indeed, agricultural output can potentially meet domestic food requirements as well as provide an exportable surplus. The sector therefore has to play a major role in the economic recovery process, particularly through the spread of labour-intensive, agro-based SMEs. In this connection, mine-clearance activities will not only enhance public safety but also yield valuable acreage for agriculture as well as for the rehabilitation of indispensable rural infrastructure, including irrigation.

^c Economic and social development, in turn, can help to generate support for political stability and peace.

(Continued overleaf)

(Continued from preceding page)

Labour-intensive public works projects will provide job opportunities and on-the-job training, thus facilitating the return of refugees (including entrepreneurs and skilled workers), among other multiplier effects. The creation of adequate employment opportunities is important in another context, namely the reintegration of former combatants as productive participants in the economic reconstruction and recovery of Afghanistan. Key social services such as education and health care will have to be restarted and expanded, with a focus on reaching girls and women. The short-term goals should include increased access to safe drinking water, restoration of the existing power system and rehabilitation of the main road network. To arrest environmental degradation, environmental considerations should be integrated into the planning and development of all projects.

In the medium to long term, a wide range of important institutions have to be set up or reinforced, including central banking authorities, finance, the treasury, the judicial system and statistical services. Effective public administration, transparency and accountability are important conditions for better aid coordination and absorption at the domestic level. At the same time, an enabling environment must be created for private sector development, particularly to attract and utilize productively Afghans living in other countries. Ongoing technical assistance is likely to be required in the foreseeable future to backstop the rehabilitation, reconstruction and development process in Afghanistan. It is hoped that all these efforts will make the Afghanistan of tomorrow different from the Afghanistan of yesterday.

GDP performance

Bangladesh has attained self-sufficiency in food

Economic growth in Bangladesh, where savings and investment rates have been increasing in recent years, remained stable at around 6 per cent in 2001 (table II.2). The country has made great strides in agricultural development in the last five years as a means of poverty alleviation and employment creation as well as to achieve self-sufficiency in food production; it emerged as a producer of surplus foodgrains in 2000. Agricultural production increased by 4 per cent in 2001 but total foodgrain production increased by as much as 7.4 per cent, thus exceeding the year's target. In contrast, the agriculture sector in Bhutan suffered from devastating floods in August 2000 and growth decreased to 2.4 per cent during the year from 3.0 per cent in the previous year. Although the sector continues to provide employment for almost 80 per cent of the population, its share in GDP declined to just over 32 per cent in 2000 from almost 34 per cent a year earlier.

Hydropower underpinned economic activities in Bhutan

GDP growth in Bhutan, which was close to 6 per cent in the last three years, has been driven by the construction sector as major hydropower projects were implemented. These projects, largely financed by transfers from India, have enabled Bhutan to sustain very high rates of investment, well in excess of the savings rate, which has, however, increased in recent years (table II.3). Future growth is expected to remain high as hydropower projects come on stream and electricity sales to India expand. Tourist arrivals in Bhutan increased in 2000, with revenue from tourism rising 5 per cent to almost \$10 million, but indications are that there was a fall-off in this sector in 2001. The country is, however,

**Table II.2. Selected least developed countries of the ESCAP region:
growth rates, 1998-2001***(Percentage)*

		<i>Rates of growth</i>			
		<i>Gross domestic product</i>	<i>Agriculture</i>	<i>Industry</i>	<i>Services</i>
Bangladesh	1998	5.2	3.2	8.3	4.8
	1999	4.9	3.2	3.2	5.7
	2000	5.9	6.9	4.8	5.9
	2001	6.0	4.0	9.1	5.9
Bhutan ^a	1998	5.5	1.3	7.7	6.3
	1999	5.9	3.0	12.4	4.5
	2000	6.1	2.4	10.3	5.6
	2001	5.9	..	..	..
Cambodia	1998	1.5	2.5	7.7	-0.2
	1999	6.9	4.8	12.0	5.8
	2000	5.4	-2.7	29.0	3.1
	2001	5.3	4.0	12.5	2.4
Lao People's Democratic Republic	1998	4.0	3.1	9.2	5.5
	1999	7.3	8.2	8.0	6.7
	2000	5.7	5.0	7.6	6.0
	2001	6.4	4.5	10.0	7.0
Maldives	1998	8.2	6.8 ^b	16.2	8.8
	1999	7.4	3.4 ^b	8.3	8.3
	2000	4.8	-2.3 ^b	-0.5	6.4
	2001	5.7	..	..	..
Myanmar	1998	5.8	4.5	6.1	7.0
	1999	10.9	11.5	13.8	9.2
	2000	13.6	..	..	..
	2001	5.0	..	..	..
Nepal	1998	3.0	1.0	2.3	6.5
	1999	4.4	2.7	6.0	5.5
	2000	6.4	5.0	9.1	6.5
	2001	5.9	4.0	5.1	7.9

Sources: ESCAP, based on ADB, *Key Indicators of Developing Asian and Pacific Countries 2001* (Oxford University Press, 2001) and *Asian Development Outlook 2001* (Oxford University Press, 2001); and national sources.

Notes: Figures for 2001 are estimates. Industry comprises mining and quarrying, manufacturing, electricity, gas and power, and construction.

^a GDP at factor cost.

^b Including coral and sand mining.

Table II.3. Selected least developed countries of the ESCAP region: ratios of gross domestic savings and investment to GDP, 1998-2001

	(Percentage)			
	1998	1999	2000	2001
Savings as a percentage of GDP				
Bangladesh	17.3	17.7	17.9	18.8
Bhutan	12.7	13.5	17.2	19.0
Cambodia	5.4	7.3	7.5	7.7
Lao People's Democratic Republic	14.8	16.4	14.6	15.0
Maldives	..	..	..	..
Myanmar	11.8	13.0	..	..
Nepal	13.8	13.6	15.1	16.1
Investment as a percentage of GDP				
Bangladesh	21.6	22.2	23.0	23.6
Bhutan	38.2	43.1	43.8	44.1
Cambodia	12.0	17.0	14.1	14.5
Lao People's Democratic Republic	26.8	23.6	25.1	26.6
Maldives	..	..	..	..
Myanmar	12.4	13.2	..	..
Nepal	24.8	20.5	24.3	25.7
<p><i>Sources:</i> ESCAP, based on ADB, <i>Key Indicators of Developing Asian and Pacific Countries 2001</i> (Oxford University Press, 2001) and <i>Asian Development Outlook 2001</i> (Oxford University Press, 2001); and national sources.</p> <p><i>Note:</i> Figures for 2001 are estimates.</p>				

deliberately trying to keep tourism low so as to limit environmental damage; tourists have to pay \$200 a day for food and lodging. Growth in other sectors taken together, including mining and quarrying, manufacturing and electricity, fell to 6 per cent in 2000 from 7 per cent in the previous year. In Bangladesh, industrial output picked up strongly, expanding by over 9 per cent in 2001 from 4 per cent on average in 1999-2000 as a result of rapid growth in the production of cement, cotton cloth, natural gas, paper and steel. However, the effects of the global slowdown, as well as the removal of quotas on exports from some other countries to the United States market, were making themselves felt in the ready-made garment industry. GDP performance in 2002 may be less strong than the solid growth of the last several years (table II.1). In particular, rising international prices for cotton and currency weakness are likely to raise costs and reduce competitiveness in the ready-made garment industry.

**Security problems
cloud the picture in
Nepal**

Hydropower is also an important economic stimulus in Nepal, where the completion of new hydropower projects and the production of additional power raised growth in the service sector, notwithstanding the sharp fall in tourism. As a result of the domestic security situation,

compounded by the difficult external environment, tourist arrivals were down by almost 21 per cent overall and by one third from India in 2001. GDP expanded by just under 6 per cent in fiscal year 2001, compared with 6.4 per cent in the previous year, reflecting the slowdown in agriculture and industry; the slowdown was quite significant in the industrial sector. Manufacturing was affected by static or declining production of ready-made garments, textiles, woollen carpets and construction materials. Savings and investment rates recovered in 2000-2001 after declining in 1999. However, the medium-term economic outlook depends on the performance of the world economy, and on India in particular, as well as on the resolution of internal security problems; indeed, growth is expected to decline somewhat in 2002 before recovering in subsequent years.

In addition to fishing, tourism has been the economic mainstay of Maldives because of its extensive linkage effects, including with wholesale and retail trade, construction, real estate and transport. GDP growth averaged 7.8 per cent in 1998-1999 but decelerated sharply to just under 5 per cent in 2000 as a result of a broad-based slowdown in output. Although tourist arrivals increased in that year, the average length of stay was shorter, thus limiting tourism revenue growth. GDP was projected to expand by 5.7 per cent owing to a stronger increase in tourism in 2001.

Despite the vulnerability of these countries to external shocks, the rate of GDP growth was sustained at 5.3 per cent in Cambodia in 2001 but was higher at 6.4 per cent in the Lao People's Democratic Republic. GDP had originally been forecast to increase by 6 per cent in Cambodia but the marginal decline was attributable to the impact of flooding on agriculture and of the recession in the United States on exports of garments and on tourism. GDP growth in the Lao People's Democratic Republic exceeded earlier estimates and was led by 10 per cent growth in the industrial sector and 7 per cent in the service sector. However, economic activities appear to have decreased significantly in Myanmar with GDP expanding by 5 per cent in 2001 (from almost 11 per cent recorded in 1999 and 13.6 per cent in 2000), which resulted from the effects of adverse weather conditions, such as flooding, on agricultural production, and from weak domestic and external demand. Growth in 2002 is likely to be little changed. The economic outlook in Cambodia and the Lao People's Democratic Republic is likely to be a marginal decrease in GDP growth in 2002 as these economies experience a delayed response to the current slowdown in the world, and in Thailand in particular, followed by a recovery in 2003. The savings rate increased slightly in Cambodia over the period 1999-2001, but remains comparatively very low among the Asian least developed countries. The investment rate in Cambodia, which improved sharply to 17 per cent of GDP in 1999, stabilized at around 14 per cent in the following two years.

Economic growth in Maldives has been on a lower trend in recent years

Steady economic growth in Cambodia and the Lao People's Democratic Republic

Flooding has affected agriculture in several least developed countries in South-East Asia

The severe floods in Cambodia in September and October 2000 damaged nearly a third of the rice fields and destroyed transport infrastructure and irrigation facilities. The output of the agriculture sector decreased by 2.7 per cent in 2000 but was forecast to expand by 4 per cent in the following year, with rice accounting for nearly one third of total agricultural value added. Rice production was expected to rebound by almost 10 per cent in 2001, after a fall of almost 4 per cent in 2000, as the flood-borne alluvial soil contributed to increased productivity. However, that productivity remained considerably below that achieved by neighbouring countries, partly as a result of inefficient farming techniques and limited irrigation facilities. Forestry production contracted by a third in 2000 following the crackdown on all forms of illegal logging and the decline is expected to continue for some time. The fisheries sector, which derives most of its output from the Tonle Sap lake, grew remarkably in 2001 as the official auction to private individuals of 495,000 hectares of fishing lots was revoked to give the poor better access to common fisheries resources. Flooding in 2000-2001 also affected agriculture in the Lao People's Democratic Republic, causing agricultural output to slow to 4.5 per cent in 2001. In Myanmar, heavy rains during the dry season harvest affected rice production adversely but the output of other crops was not seriously affected. Overall growth in agriculture has also been handicapped by shortages of fertilizer and other inputs. The monopoly of State enterprises in such export crops as rice, rubber, cotton and teak has constrained private sector participation and export growth in Myanmar.

More Asian tourists visit Cambodia

The industrial sector of Cambodia, where output grew 29 per cent in 2000, consists mainly of manufacturing activities (79 per cent), which are largely concentrated in Phnom Penh, and construction (19 per cent). The slowdown in major overseas markets hit garment exports, which account generally for 70 per cent of Cambodia's exports, contributing thus to the sharp decrease in industrial growth to 12.5 per cent in 2001. Construction was expected to expand by 8 per cent in 2001, lower than the 12.6 per cent growth registered in 2000, driven in part by increased government and aid-sponsored capital expenditure. However, the service sector registered modest growth of 2.4 per cent in 2001 and, despite the events of 11 September 2001, tourist arrivals were up 40 per cent year-on-year although they fell by 18 per cent that September. Asian tourists continued to arrive, even though the number of visitors from the United States decreased.

Diverse patterns of industrial production in the Lao People's Democratic Republic and Myanmar

Value added in the manufacturing sector in the Lao People's Democratic Republic comprises mainly food processing, including the production of animal feed, beer, mineral water and rice milling and garment manufacturing. The wood processing industry grew in 2001 but the production of meat, fish, coffee, cigarettes, detergent and construction material remained stagnant or declined. In Myanmar, the manufacturing sector grew rapidly in 2000 as the production of cotton fabrics, cement, edible oils, paper and milled sugar increased in response to the Government's import-substitution strategy. The scope for further industrial

expansion may be limited, however, because of slowing domestic and external demand. In addition, power supplies have been erratic, and the increased reliance of manufacturers on imported diesel fuel for generators has raised costs significantly. Other constraints are sluggish domestic investment and FDI and the severe shortage of foreign exchange.

Inflation

In Bangladesh, the inflation rate decelerated significantly in 2000-2001, partly because of the comfortable food supply position following good harvests of cereals and liberal import of consumer goods, and partly because of weak demand (table II.4). Falling prices for commodities such as oil in world markets under the spell of recession also contributed to the decline. Consumer price inflation was 1.6 per cent year-on-year in fiscal year 2001, compared with 3.4 per cent in 2000 and 8.9 per cent in 1999.

Consumer prices stabilized with the comfortable food supply situation in Bangladesh

Table II.4. Selected least developed countries of the ESCAP region: inflation and money supply growth (M2), 1998-2001

(Percentage)

	1998	1999	2000	2001
Inflation^a				
Bangladesh ^b	7.0	8.9	3.4	1.6
Bhutan ^b	9.0	9.2	3.6	3.6
Cambodia	14.8	4.0	-0.8	-0.6
Lao People's Democratic Republic	91.0	128.5	25.1	9.0
Maldives	-1.4	3.0	-1.1	..
Myanmar	51.5	18.4	-0.1	9.6
Nepal ^{b,c}	8.4	11.4	3.5	2.4
Money supply growth (M2)				
Bangladesh	11.4	15.5	19.3	14.1 ^d
Bhutan	14.0	32.0	17.4	11.1 ^e
Cambodia	15.7	17.3	26.9	18.5 ^d
Lao People's Democratic Republic	113.3	78.4	46.0	20.0
Maldives	22.8	3.6	4.1	3.8 ^d
Myanmar	34.2	29.7	42.4	49.1 ^f
Nepal	21.9	20.8	21.8	13.0

Sources: ESCAP, based on ADB, *Key Indicators of Developing Asian and Pacific Countries 2001* (Oxford University Press, 2001), *Asian Development Outlook 2001* (Oxford University Press, 2001) and *Asia Economic Monitor 2001*, December issue (<<http://aric.adb.org>>); IMF, *International Financial Statistics*, vol. LV, No. 1 (January 2002); and national sources.

Note: Figures for 2001 are estimates.

- ^a Changes in the consumer price index.
- ^b Fiscal year.
- ^c National urban consumer price index.
- ^d January-September.
- ^e January-March.
- ^f January-June.

Food items, which carry a relative weight of 54.5 per cent in the composite consumer price index, increased by only 0.7 per cent in 2001 compared with 4 per cent and 11.8 per cent respectively in the previous two years. Monetary policy continued to be expansionary in 2001, but the growth in the broad money supply (M2) slowed as a result of reduced government borrowing (table II.4). However, the fiscal deficit widened to 6.9 per cent of GDP in 2001, while interest rates were reduced in October 2001 in a bid to stimulate investment. The large fiscal shortfall, if accompanied by high rates of money supply growth, would be likely to put pressure on the exchange rate and on consumer prices in the coming year.

***Monetary expansion
in Bhutan reflects
inflows of capital***

In Bhutan, inflation was steady at 3.6 per cent in both 2000 and 2001, despite some pick-up in prices towards the end of 2000; such overall stability by and large reflected reductions in both food and non-food prices. Large balance-of-payments surpluses have resulted in relatively high rates of monetary expansion in Bhutan in recent years, but credit growth has been sluggish, expanding at around 5 per cent annually. The growth in private sector credit was a reflection of consumer lending, as credit for other purposes was declining. Generally, banks have considerable excess reserves, reflecting the cautious lending culture of the two main commercial banks as well as the lack of investment opportunities. While the Government has avoided borrowing to finance current expenditure, the budget deficit widened to 6 per cent of GDP in 2001 as a result of increased capital spending (financed by transfers mainly from India) associated with the construction of hydropower plants.

***Improved food
supply slowed
inflation in Nepal***

In Nepal, despite surging petroleum prices, the improved supply of food products accompanied by reduced monetary growth resulted in a further deceleration of inflation in fiscal year 2001. The national urban consumer price index was only 2.4 per cent higher in 2001, as against an increase of 3.5 per cent the previous year, and was substantially below the 11.4 per cent rise in 1999. A fall in the prices of food and beverages, particularly rice, vegetable oil and ghee, contributed to bringing down the average annual inflation rate to the lowest single-digit level in the last decade. Growth in the broad money supply decelerated in fiscal year 2001, as did private sector credit growth, and in December 2001 the Nepal Rastra Bank lowered cash reserve ratios for commercial banks by an average of 1 per cent and refinancing rates by 1–2 per cent. However, investment is unlikely to post any significant increase while the security situation remains difficult. The spread between lending and borrowing rates at commercial banks is high at 5 per cent, reflecting weakness in the banking system. The budget balance deteriorated in 2001 as revenues fell with the economic slowdown and falling imports; 40 per cent of revenues come from customs duties and import taxes. Expenditure also rose because of the worsening security situation and is likely to remain high, thus putting some pressure on inflation in 2002. Increases in customs duties, taxes and other charges will add to those pressures, but inflation is likely to remain below 5 per cent as a reflection of relative price stability in India.

Falls in the prices of consumer products, such as food, beverages, tobacco, clothing and footwear, resulted in deflation in Maldives in 2000, when prices fell 1.1 per cent as against an increase of 3 per cent in 1999. Fiscal prudence has kept monetary expansion stable on a low trend, growing at an average annual rate of 3.8 per cent in the period 1999-2001. The fiscal deficit as a percentage of GDP remained around 4 per cent in 1999-2000.

In Cambodia, deflation continued in 2001, when consumer prices fell by 0.6 per cent. Prices for food, beverages and tobacco items, which accounted for half of the total goods and services in the consumer basket, fell throughout the year, with the exception of the Khmer New Year in April. However, increased duties on petroleum products and possible depreciation of the riel may lead to higher consumer prices in 2002. Inflation showed signs of accelerating in the Lao People's Democratic Republic, where the estimated annual inflation for fiscal year 2001 reached 9 per cent, and the forecast for subsequent years is even higher. Shortages of basic consumer goods, exchange rate weakness and increases in electricity prices are expected to combine to raise prices. Despite the adverse impact of flooding, which affected both countries in late 2000, rice prices remained little changed owing to large imports of rice and compensatory assistance in kind provided by donors. Government distribution of rice seeds also minimized the impact of the floods on rice production in 2001. Import prices declined owing to the strength of the dollar against the currencies of major suppliers, including Thailand. In both Cambodia and the Lao People's Democratic Republic, the cost of housing, transport and communications rose considerably, owing partly to rising labour costs.

The economy of Cambodia is characterized by a high degree of "dollarization" as a result of the lack of confidence in the domestic currency. Deposits denominated in dollars accounted for nearly 70 per cent of broad money (M2) in 2000, and the total amount of dollars in circulation is estimated to be greater than the broad money supply. Currency and asset substitution limits the effectiveness of monetary policy in Cambodia, and inflation is affected more directly by the depreciation of the riel than by monetary expansion. Broad money growth slowed in 2001 but was still in double digits, accelerating ahead of the elections as fiscal discipline relaxed. However, the riel has been generally stable, contributing to the muted inflationary pressures. Commercial banks continue to be reluctant to lend to the domestic private sector, however, preferring to acquire foreign assets. In the Lao People's Democratic Republic, monetary and credit expansion was tightened considerably in 2001 in an attempt to reduce inflationary pressures, but in that country too the effectiveness of monetary policy is hampered by currency and asset substitution. The budget deficit increased slightly in 2001 but is still considerably lower than the 11 per cent average in 1998-1999.

Deflation continued in Cambodia but the outlook is less encouraging

Currency and asset substitution is a problem common to Cambodia and the Lao People's Democratic Republic

Monetary expansion has been very rapid in Myanmar

In Myanmar, consumer prices were officially estimated as remaining virtually unchanged in 2000 as food prices were stable following the general stability in the exchange rate, improved agricultural performance and the implementation of tax-free markets, which reduced marketing and distribution costs. Large cuts in public expenditure reduced inflationary financing. The inflation rate was expected to average 9.6 per cent in 2001 owing to rising civil service wages, depreciation of the kyat and rising import prices. In addition, broad money (M2) growth accelerated from over 42 per cent in 2000 to nearly 50 per cent in the first half of 2001.

Foreign trade and other external transactions

External trade

Both merchandise exports and imports increased more rapidly in Bangladesh

Bangladesh's export earnings, at \$6.4 billion in fiscal year 2001, registered growth of 12.4 per cent compared with 8.2 per cent in the previous year (table II.5). Ready-made garments and hosiery products continued to be the top foreign exchange earners and were responsible for four fifths of total export receipts, but those sectors will be adversely affected by the loss of privileged access to the United States market. Export earnings from leather and tea increased by 30 and 22 per cent respectively. However, exports of frozen shrimp have been hit by weak demand and falling international prices. The total import expenditure of

Table II.5. Selected least developed countries of the ESCAP region: merchandise exports and their rates of growth, 1998-2001

	Value (Millions of US dollars)	Exports (f.o.b.)			
		Annual rate of growth (Percentage)			
		1998	1999	2000	2001
Bangladesh ^a	5 752	5.4	2.9	8.2	12.4
Bhutan ^a	114	12.1	-5.9	9.1	-1.8
Cambodia	1 103	13.1	17.4	55.6	8.4 ^b
Lao People's Democratic Republic	303	6.4	7.7	8.3	7.4
Maldives	76	3.4	-4.3	19.1	..
Myanmar	1 883	6.6	14.4	37.4	13.1 ^c
Nepal ^a	721	12.7	18.2	37.4	7.5

Sources: IMF, *Direction of Trade Statistics* (CD-ROM), February 2002, *International Financial Statistics* (CD-ROM), January 2002 and web sites <<http://www.imf.org/external/np/sec/pr/2001/pr0118.htm>> and <<http://www.imf.org/external/country/index.htm>>, 18 February 2002; ADB, *Asian Development Outlook 2001* (Oxford University Press, 2001); and national sources.

^a Fiscal year.

^b Estimate.

^c Figures refer to January-September 2001.

Table II.6. Selected least developed countries of the ESCAP region: merchandise imports and their rates of growth, 1998-2001

	Value (Millions of US dollars)	Imports (c.i.f.)			
		Annual rate of growth (Percentage)			
		1998	1999	2000	2001
Bangladesh ^a	8 403	7.4	6.6	4.8	11.4
Bhutan ^a	185	3.7	19.2	14.0	16.3
Cambodia	1 438	7.4	16.5	48.6	6.0 ^b
Lao People's Democratic Republic	477	-14.7	0.3	6.6	10.6
Maldives	388	1.5	13.6	-3.4	..
Myanmar	2 473	-12.4	-11.0	17.0	3.1 ^c
Nepal ^a	1 571	-11.8	-10.3	22.0	-2.2

Sources: IMF, *Direction of Trade Statistics* (CD-ROM), February 2002, *International Financial Statistics* (CD-ROM), January 2002 and web sites <<http://www.imf.org/external/np/sec/pr/2001/pr0118.htm>> and <<http://www.imf.org/external/country/index.htm>>, 18 February 2002; ADB, *Asian Development Outlook 2001* (Oxford University Press, 2001); and national sources.

^a Fiscal year.
^b Estimate.
^c Figures refer to January-September 2001.

Bangladesh (table II.6) increased 11.4 per cent to \$9.4 billion in 2001, compared with import growth of 4.8 per cent in the previous year. Major increases were recorded in imports of capital goods and in inputs for the garment and textile industries, while imports of cement, oil seeds and edible oil declined. The balance on current account was in deficit to the extent of 1.7 per cent of GDP in 2001, and this figure may increase in the medium term (table II.7), in part as the result of a widening deficit in merchandise trade, smaller net services and income receipts, lower official current transfers and lower remittances from migrant workers.

More than 80 per cent of Bhutan's trade flows and 45 per cent of those of Nepal are with India. Bhutan recorded a small decrease (1.8 per cent) in merchandise exports in fiscal year 2001 compared with a 9.1 per cent increase in 2000. Import growth accelerated to 16.3 per cent in fiscal year 2001 from 14 per cent in the preceding year, owing to the high import content in the construction of hydropower plants. Factor service payments also increased. Bhutan will continue to run a trade deficit until its hydropower projects are completed and the export of electricity to India begins. The trade deficit as a percentage of GDP increased from 17 per cent in 2000 to just over 23 per cent in 2001. The average annual current account deficit was around 27 per cent in 2000-2001.

***The economies of
Bhutan and Nepal
are closely linked to
the Indian economy***

Table II.7. Selected least developed countries of the ESCAP region: budget and current account balance as a percentage of GDP, 1998-2001

	1998	1999	2000	2001
Budget balance as a percentage of GDP				
Bangladesh ^a	-4.2	-5.4	-6.1	-6.9
Bhutan	3.0	-0.9	-3.9	-6.0
Cambodia ^a	-6.0	-4.4	-5.7	-6.2
Lao People's Democratic Republic ^a	-11.4	-10.5	-8.5	-8.8
Maldives	-1.9	-4.1	-4.0	..
Myanmar ^a	-0.4	-1.3	-0.5	..
Nepal	-5.9	-5.3	-4.7	-5.8
Current account balance as a percentage of GDP				
Bangladesh	-0.6	-0.9	- ^b	-1.7
Bhutan	-11.7	-24.4	-28.4	-26.8
Cambodia	-8.0	-9.0	-10.2	-9.1
Lao People's Democratic Republic	-10.0	-11.0	-5.4	-6.6
Maldives	-4.5	-11.1	-4.6	..
Myanmar ^c	-0.4	-0.2	..	..
Nepal	-1.5	0.1	-2.3	-1.4
<p>Sources: ESCAP, based on ADB, <i>Key Indicators of Developing Asian and Pacific Countries 2001</i> (Oxford University Press, 2001) and <i>Asian Development Outlook 2001</i> (Oxford University Press, 2001); IMF, <i>International Financial Statistics</i>, vol. LIV, No. 10 (October 2001); and national sources.</p> <p>Note: Figures for 2001 are estimates.</p> <p>^a Excluding grants.</p> <p>^b Negligible.</p> <p>^c At official exchange rates.</p>				

In Nepal, exports grew by 7.5 per cent in fiscal year 2001 as compared with 37.4 per cent in the preceding year. Exports to India grew rapidly in 2000-2001, but slowed in the second half of 2001; vegetable ghee, jute goods, acrylic and polyester yarn and thread, Ayurvedic medicine, copper wire and toothpaste were the main exports. The trade treaty with India, which gives duty-free access to Nepalese exports (except alcohol and tobacco), is currently being renegotiated owing to Indian concerns regarding rules of origin and safeguards. A major "problem product" for India is hydrogenated vegetable oil (vegetable ghee), which is made from palm oil imported from Malaysia that faces negligible duties in Nepal, unlike the heavy duties in India. Imports of palm oil increased 500 per cent in Nepal in fiscal year 2001. Exports of luxury products, such as pashmina shawls, woollen carpets and gold and silver ornaments, to other markets experienced a decline in 2001 as a result of weak demand and consumer environmental concerns in some cases. Exports of ready-made garments slumped after the opening of the United States market, Nepal's main export destination, to African and Caribbean producers.

Total merchandise imports decreased by 2.2 per cent in Nepal in fiscal year 2001, compared with a sharp increase of 22 per cent in the previous year, affected by a tightening of standards for the issuance of letters of credit. Imports from India, in particular transport vehicles, textiles, chemical fertilizers and medicine, increased; however, reduced incentives for smuggling gold to India led to a sharp drop in gold imports. The trade deficit narrowed to 13.6 per cent of GDP and the current account registered a smaller deficit equal to 1.4 per cent of GDP in 2001. Although tourism receipts went down sharply, substantial increases in transfer receipts and grant aid offset the fall. Remittance income, estimated at 10 per cent of GDP, continues to be of major importance.

*Official transfers
offset the fall in
tourism receipts in
Nepal*

In Maldives, merchandise exports went up by 19 per cent in 2000. Despite falling international prices of fish, the export volume of canned and dried fish increased substantially. Merchandise imports fell by 3.4 per cent in 2000, reflecting the slowdown in the economy. As a result, the trade deficit declined from 45 per cent of GDP in 1999 to 39 per cent in 2000. The current account deficit as a percentage of GDP also fell, notwithstanding the sharp fall in revenues from tourism.

*Tourism also
suffered in
Maldives*

Cambodia's major exports are ready-made garments, logs and sawn timber, rubber and fishery products. In 2000, merchandise exports grew by 55 per cent, but the growth rate plunged to a little above 8 per cent in 2001. However, imports of textiles and fabrics for garment factories, oil products and machinery and electrical appliances also faltered to 6 per cent in 2001, after increasing almost 49 per cent in the previous year. Following the signing of an agreement giving Cambodia preferential access to markets in the European Union until 2002 and an increase in the volume quota to the United States in January 2002, garment exports were expected to increase, but competition from China and Viet Nam remains intense. The United States is the destination of 46 per cent of Cambodia's exports, but orders for ready-made garments fell sharply after the events of 11 September 2001, along with tourism. Owing to its low customs duties, Cambodia has become a hub for transit trade in the region, especially with Viet Nam, but such re-exports (of alcohol, tobacco, gold, pulp and paper, electrical appliances and motor vehicles, among other items) have gradually declined since their peak in 1996. Cambodia's current account deficit, excluding official transfers, decreased from 10.2 per cent of GDP in 2000 to 9.1 per cent in 2001.

*Trade deficit falls
in Cambodia*

The growth rate of merchandise exports from the Lao People's Democratic Republic decreased to 7.4 per cent in 2001, from 8.3 per cent in 2000, while that of merchandise imports increased to 10.6 per cent from 6.6 per cent a year earlier. Merchandise exports are dominated by timber and wood products, followed by ready-made garments, hydropower and coffee. The Government would like to diversify exports, as the present reliance on timber and wood products is not environmentally

*Timber and wood
products dominate
exports from the
Lao People's
Democratic
Republic*

sustainable. However, limited access to the United States market in the absence of normal trade relations has put a brake on exports of ready-made garments and the United States has moved to place import quotas on textile exports from the Lao People's Democratic Republic. The main import categories of consumer goods are construction and electrical equipment, inputs for the ready-made garment industry, motorcycle parts and petroleum products; Thailand remains an important trading partner. Import growth is likely to continue to outstrip export growth and the trade deficit was expected to reach 11.6 per cent of GDP in 2001, higher than the forecast of 10.2 per cent but still low by historical standards. However, the fall in tourism as a result of domestic security concerns and the global travel slump is likely to reduce service receipts further. The current account deficit widened to 6.6 per cent of GDP in 2001, up from 5.4 per cent in the previous year.

Imports of fuel increased significantly in Myanmar

The growth in merchandise exports from Myanmar, although still on a high trend, was considerably lower in the first nine months of 2001 at just over 13 per cent compared with 37.4 per cent in 2000. A similar deceleration occurred in import growth. There were increased exports of rice, pulses and hardwoods, as well as gas. Imports of fuel have increased significantly as a result of the partial failure of the main hydropower plant and the increased use of diesel generators. However, imports of consumer goods and fertilizer fell sharply and the trade deficit of more than \$500 million was 21 per cent lower than in 2000. The reduction in imports, and subsequently the trade deficit, resulted from the rise in the free market exchange rate and from the lower capital imports caused by the slowdown in domestic investment. Import controls were also tightened and strategies adopted to encourage import substitution as well as greater production for export.

Capital inflows, external debt and exchange rates

Donor lending has been slow and private capital inflows low in Bangladesh

Private capital inflows have generally been low in Bangladesh. FDI amounted to \$166 million in 2001, 14.4 per cent below the figure for 2000, and any increase in these investment flows will depend on an agreement to permit gas exports. Portfolio investment has been negligible. Donor lending to Bangladesh has been slower than projected as a result of limited reforms, but may now increase with the change in Government. The cumulative total of foreign aid received over the last four years was \$5.6 billion as against the projection of \$7.7 billion for the fifth five-year plan period. However, external debt outstanding at end-June 2001 was manageable at 31.4 per cent of GDP, compared with 33.5 per cent a year earlier. Debt service amounted to 8.5 per cent of merchandise exports in 2001. Total official reserves, excluding gold, which have been under pressure owing to the widening current account deficit and reduced official capital inflows, amounted to just over \$1 billion in October 2001, down

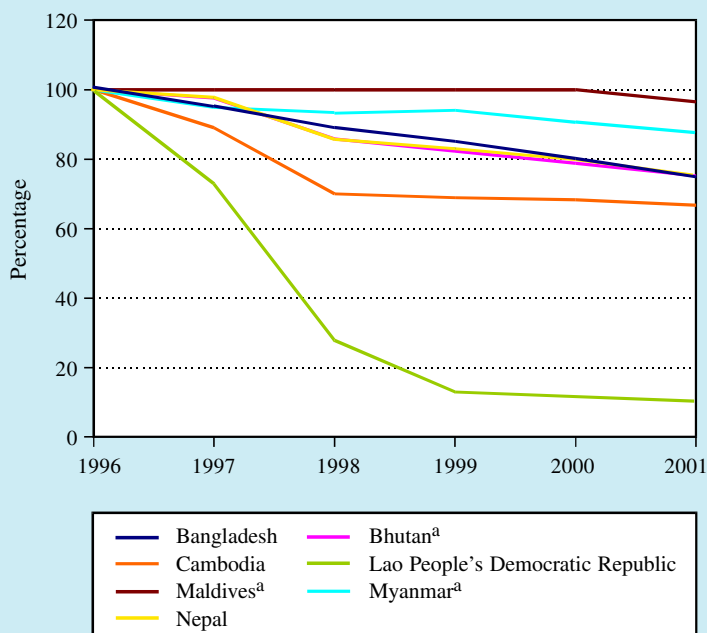
from nearly \$1.5 billion at the end of 2000. Bangladesh devalued its currency by around 11 per cent against the dollar through two revisions in August 2000 and May 2001 (figure II.5). The taka was devalued again by 1.6 per cent in January 2002, as depreciation of the Indian rupee maintained pressure on the exchange rate.

Capital inflows, mainly in the form of official aid, were more than adequate to support the current account deficit in Nepal, where nearly 60 per cent of development spending is financed by aid. Similarly, increased foreign aid to Bhutan, especially from India, has easily financed the current account deficit and the balance of payments has been in substantial surplus. Official reserves in Bhutan amounted to \$282.4 million at the end of December 2001, providing about 16 months of import cover. Total external debt, much of it on concessional terms, increased from 42 per cent

*Capital inflows
financed the
current account
deficit comfortably
in Nepal*

Figure II.5. Index of exchange rates against the United States dollar of selected least developed countries in the ESCAP region, 1996-2001

(1996=100)



Sources: IMF, *International Financial Statistics*, vol. LV, No. 1 (January 2002); and *Far Eastern Economic Review*, various issues.

Note: Figures for 2001 are estimates.

^a Figures for 2001 are January-November.

of GDP in 2000 to 53 per cent in 2001. More than half of this debt is owed to India, a major source of funding for hydropower projects and other development activities. The debt-service ratio remains low at around 4 per cent of merchandise exports. In Nepal, the outstanding external debt amounted to 49 per cent of GDP in July 2001 and debt servicing has not so far become a critical problem as most of this debt is concessional in nature. The debt-servicing ratio had been growing over the years to reach 10.8 per cent of merchandise exports in 2001. The currencies of both Bhutan and Nepal are pegged at par to the Indian rupee, which circulates freely in both countries. Changes in the values of the Bhutanese ngultrum and the Nepalese rupee are a reflection of exchange rate movements in the Indian rupee. The exchange rate peg has proved beneficial in terms of predictability and convenience, particularly as trade and other links of both countries with India have been very strong.

Maldives has also benefited a great deal from donor assistance, which averaged over 8 per cent of GDP annually during the 1990s. However, foreign exchange reserves at the end of 2000 were only sufficient to pay for 4.3 months of imports of goods and services and total external debt was around 36 per cent of GDP in 2000. The exchange rate, which has been fixed since 1995, was devalued by approximately 8.8 per cent against the dollar in July 2001.

FDI has fallen considerably in Cambodia and Myanmar

In both Cambodia and Myanmar, FDI flows declined from the peaks reached in 1996, from \$294 million to an estimated \$125 million in 2000 in the case of Cambodia and, even more dramatically, from \$2.8 billion to less than \$60 million in Myanmar in fiscal year 1999. These flows are likely to have been even lower in 2001 as a result of the regional economic slowdown. Singapore, the United Kingdom, Thailand and Malaysia were among the largest investors in Myanmar, with oil, manufacturing and tourism attracting the most foreign investment. The industrial sector, mainly garment factories, accounted for 40 per cent of total investment approvals in Cambodia, followed by tourism and infrastructure, which accounted for 29 and 26 per cent respectively. Key constraints on private capital flows to Cambodia include inadequate infrastructure, security problems, a weak legal system, shortage of skilled labour and the lack of skilled managers. To remove distortions while protecting revenues, the Government of Cambodia is reviewing incentives provided to investors, as well as taxes.

ODA increased sharply in Cambodia and the Lao People's Democratic Republic

Official aid (including concessional loans) to Cambodia increased significantly, by 36 per cent to \$344 million in 2000 from the previous year. Although total external reserves (excluding gold) rose to \$569 million at the end of November 2001, or over 13 per cent higher than the end-2000 value, this was sufficient to finance only four months of imports. ODA in the Lao People's Democratic Republic, of which nearly three

quarters were grants, was expected to reach \$386 million in 2001, an increase of over 16 per cent from the previous year. Gross official international reserves declined by 12 per cent to \$124 million at the end of August 2001, after rising steadily in 2000, reflecting the drawing down of reserves through bank financing of the overall budget deficit during the second half of the fiscal year 2000. In contrast, Myanmar's limited access to concessional loans has led to increased reliance on commercial credits, particularly from China, for capital goods imports. However, there was a small increase in aid from Japan in 2001. Official reserves at the end of July 2001 were estimated at \$239.5 million, or the equivalent of less than two months of import cover.

The Lao People's Democratic Republic and Myanmar are the only least developed countries in the region that qualify for debt relief under the Heavily Indebted Poor Countries Initiative of the World Bank and IMF (box II.3). However, governance problems have hampered discussions on this initiative. Myanmar's external debt amounted to \$5.6 billion in 2000, or slightly lower than the peak of \$6 billion reached in 1999. Repayments to ADB and the World Bank were suspended in 1998 and total arrears to those agencies amounted to 40 per cent of external debt in fiscal 1999. However, all bilateral debts have been repaid as the country has focused its debt-servicing efforts on commercial credits. In the Lao People's Democratic Republic, total external debt was equivalent to 73.4 per cent of GDP in 2000, leading to a debt-service ratio of 9.2 per cent of exports of goods and services. In view of its limited debt-servicing capacity, external borrowing is now being closely monitored through the newly established debt-monitoring unit to ensure a sustainable debt burden.

Despite the external debts incurred over the years, Cambodia's debt burden is considered to be sustainable in terms of the Heavily Indebted Poor Countries Initiative because much of it is concessional. However, the total external debt, over half of which was concessional, amounted to 65.3 per cent of GDP in 2000. The completion of outstanding bilateral rescheduling agreements was expected to allow debt-service payments to remain at less than 5 per cent of goods and services receipts over the medium term.

Exchange rates against the United States dollar in Cambodia and the Lao People's Democratic Republic and in the free market in Myanmar remained relatively stable throughout 2000, in contrast to the significant depreciation of their currencies in recent years. In Cambodia, the official exchange rate adjusts to movements in the flexible parallel market exchange rate with a spread below 1 per cent and remained in the range of 3,800-3,900 riels to the dollar throughout 2000 and the first half of 2001. As in the case of currencies in other countries in the subregion, the

***Heavy external debt
in the Lao People's
Democratic
Republic and
Myanmar***

***Exchange rate
stability in 2000
gave way to greater
uncertainty in
South-East Asian
least developed
countries***

Box. II.3. Implementation of the Programme of Action of the Third United Nations Conference on the Least Developed Countries

The Programme of Action for the Least Developed Countries for the decade 2001-2010 was adopted at the Third United Nations Conference on the Least Developed Countries, held at Brussels from 14 to 20 May 2001. Subsequently, it was noted in the report of the Secretary-General entitled "Road map towards the implementation of the United Nations Millennium Declaration"^a that the next steps in support of the 49 least developed countries would include implementing a global version of the European "Everything but arms" trade programme; increasing ODA; fully implementing the enhanced Heavily Indebted Poor Countries Initiative; and pursuing measures to promote the cancellation of official bilateral debt. In addition, the Declaration adopted by the fourth WTO Ministerial Conference, held at Doha, Qatar, in November 2001, urged integration into the WTO work programme of earlier multilateral trade commitments as well as those made at the Third United Nations Conference on the Least Developed Countries. Finally, the agreed draft text of the Monterrey Consensus prepared for the International Conference on Financing for Development scheduled to be held at Monterrey, Mexico, from 18 to 22 March 2002, reaffirmed that ODA to least developed countries should be equivalent to 0.15-0.20 per cent of developed country GNP.

Development assistance and debt relief

ODA to least developed countries grew from 19 to 22 per cent of the aid flow from DAC member countries from 1999 to 2000, compared with 27 per cent in 1989-1990. At its High-level Meeting held in April 2001, DAC agreed to untie ODA to least developed countries to the greatest extent possible as at 1 January 2002, while ensuring adequate ODA flows to those countries as well as reinforcing partner country responsibility for procurement and the ability of the private sector to compete for aid-funded contracts.^b However, technical cooperation and food aid were an exception, as such untied assistance could present problems for some donors. All in all, untied ODA could amount to some \$5.5 billion, or about 70 per cent of all bilateral aid to least developed countries.

The enhanced Heavily Indebted Poor Countries Initiative would help to reduce the debt stock of 22 countries qualifying for debt relief to manageable levels and enable them to access international finance. Nevertheless, it may take those countries several years to meet the required conditions, while several debt-stressed least developed countries are not defined as heavily indebted. DAC member countries have therefore decided to expand the process so as to provide additional debt relief.^c In particular, the period between the decision and completion points has been compressed and the associated relief provided at an early stage so that it can take effect more quickly. Debt relief under the Initiative, however, represents a very small share of DAC members' annual net ODA, since the total debt relief will be implemented over several years. Lowered repayments to international financial institutions made from debtor countries' own net income derived from other loans and forgiveness or rescheduling of the principal of bilateral ODA loans do not enter ODA data.

The final draft of the Monterrey Consensus reiterated that ODA should comprise 0.7 per cent of developed country GNP and that 0.15-0.20 per cent should be allocated to least developed countries. Donors were also urged to meet their commitments to increase assistance and establish information systems to monitor the use and effectiveness of their ODA. At the same time, it was emphasized that bilateral and multilateral development agencies should take the necessary steps to make their aid programmes more efficient and responsive to the needs of recipient countries, to assist these countries in carrying out further institutional reforms so as to increase transparency and interactive dialogue.

^a A/56/326.

^b OECD, "Untying aid to the least developed countries", Policy Brief (*OECD Observer*, July 2001).

^c OECD news release, "ODA steady in 2000; other flows decline", 12 December 2001.

Trade

The implementation of the “Everything but arms” trade initiative from 5 March 2001 and the integration of the development agenda into the Ministerial Declaration adopted by the fourth WTO Ministerial Conference are among the more notable recent events. Under the trade initiative, the European Union accorded duty- and quota-free access for essentially all non-military exports (except sugar, rice and bananas) from the 49 least developed countries. The concession will be maintained for an unlimited period of time and is not subject to periodic renewal, unlike the generalized system of preferences. In view of the difficulties in enforcing rules of origin compliance, the European Union furthermore granted the benefit of a regional cumulation for all exports from Cambodia and the Lao People’s Democratic Republic as well as from least developed country members of the South Asian Association for Regional Cooperation.

As from 1 April 2001, some 99 per cent of industrial products (including all textiles and clothing items) from least developed countries can enter Japan duty- and quota-free. The number of items under such treatment would be increased in step with progress in the current WTO round of multilateral trade negotiations and the impact on domestic industry. Meanwhile, a study was carried out by UNCTAD and the Commonwealth Secretariat on the gains to those countries if Canada, Japan and the United States followed the lead of the European Union as regards the “Everything but arms” trade initiative.^d The results indicate that those countries would benefit from both improved terms of trade and better allocation efficiency, including in structural export diversification. However, ancillary enhancement of the technical and institutional infrastructure in least developed countries would serve to maximize the widened market access thus available. In this context, in the report of the Secretary-General, “Road map towards the implementation of the United Nations Millennium Declaration”, other developed countries were urged to follow the lead set by the European Union.

The development dimension of trade was one of the major themes of the Ministerial Declaration adopted by the WTO Ministerial Conference in November 2001. The Declaration urged countries to integrate trade policies into national development policies for poverty reduction, upgrade production and export capabilities and improve the effectiveness of the generalized system of preferences by reducing administrative and procedural complexities. The WTO Subcommittee on Least Developed Countries was therefore requested to design a work programme taking into account the trade issues contained in the Programme of Action of the Third United Nations Conference on the Least Developed Countries. In addition, the Declaration expressed firm commitment to the objective of duty-free, quota-free market access for products originating from least developed countries as well as to the implementation of measures to further widen market access for those exports.

The WTO Ministerial Conference, recognizing that technical assistance and capacity-building were core elements of the development dimension of the multilateral trading system, endorsed the New Strategy for WTO Technical Cooperation for Capacity Building, Growth and Integration. The objectives were to assist least developed countries in adjusting to WTO rules and disciplines, implementing obligations and exercising the rights of membership, including drawing on the benefits of an open, rules-based multilateral trading system. The Declaration noted the need for a coherent policy framework and timetable to ensure effective and coordinated delivery of technical assistance from bilateral donors as well as international and regional intergovernmental institutions. In this connection, the Declaration endorsed the Integrated Framework for Trade-related Technical Assistance to Least Developed Countries as a model for trade development; and development partners were requested to increase their contributions to the Integrated Framework Trust Fund significantly. The European Union, for example, has already committed 49 million euros for trade-related technical assistance and economic development cooperation for the period 2002-2006.

The Declaration was also concerned at the difficult trade issues facing small, vulnerable economies and the need for more speedy and easy procedures for WTO accession negotiations. While several least developed countries have been negotiating for accession, only the Solomon Islands has joined the organization since its establishment in 1995. The European Union has proposed a number of facilitation measures for those countries, although the proposals have yet to be endorsed by other WTO member countries.

^d UNCTAD and Commonwealth Secretariat, *Duty- and Quota-free Market Access for Least Developed Countries: An Analysis of Quad Initiatives* (UNCTAD/DITC/TAB/Misc.7).

(Continued overleaf)

(Continued from preceding page)

Follow-up mechanism

The need for an effective and highly visible follow-up mechanism for coordinating, monitoring and reviewing the implementation of the Programme of Action has been well recognized. The Secretary-General, in his report on the subject to the General Assembly at its fifty-sixth session,^e proposed the establishment of an Office of the High Representative for the Least Developed Countries, Landlocked Developing Countries and Small Island Developing States to follow up the implementation of the Programme of Action.

^e A/56/645.

riel came under pressure in the third quarter of 2001, but stabilized thereafter. The Government is seeking to maintain the exchange rate at 3,950 riels to the dollar in 2002, but this will depend on a variety of both economic and non-economic factors. In the Lao People's Democratic Republic, the kip depreciated in 2000-2001, in line with the weakening of the Thai baht, increased demand resulting from the year-end budgetary expenditure, and a higher trade deficit. The exchange rate is now managed more flexibly and the margin between the bank and the parallel market rates is to be kept under 2 per cent. The parallel market rate was 9,475 kips to the dollar at the end of February 2002. The market rate in Myanmar, which depreciated significantly in 2001 and reached 750 kyats to the dollar in February 2002, continues to diverge very considerably from the official rate of 6.7 kyats to the dollar. A flexible exchange rate regime which unifies the official exchange rate with the market exchange rate and that for foreign exchange certificates is necessary in order to improve resource allocation and minimize rent-seeking behaviour. The transition to such a regime, however, will require external financing to meet the short-term costs.

Key policy issues

Good governance tops the policy agenda of the Asian least developed countries

Good governance is essential if Governments are to combat poverty, deliver services efficiently and equitably and ensure sustained human development. The donor communities, including multilateral funding agencies, are increasingly giving importance to improving governance and efficiency in the public, corporate and financial sectors and, by extension, to the more effective mobilization and utilization of aid and other resources for development and transformation. To this end, Governments have implemented a series of policy reforms aimed at establishing a

strong foundation for long-term economic growth and alleviating poverty. Strengthening and streamlining the public sector is an essential element of those strategies, so that greater resources can be devoted to developing the physical and social infrastructure needed to foster private sector development. Further development of this sector is important for generating employment opportunities, while greater effort is also needed to improve the quality of human resources so that people can take advantage of new opportunities.

Economic growth and poverty alleviation efforts in Bangladesh have been constrained by a large and unprofitable public sector. Multilateral aid agencies have stressed the need for government reforms and privatization of State-owned enterprises and State-run banks. Bangladesh is highly dependent on ODA and such external resources financed 44 per cent of the fiscal deficit in 2000/01. The new Government, which is seen as more committed to reform, has formed a 13-member Administrative Reform Commission, which, has submitted a report containing a total of 137 recommendations for implementation in phases. The Commission touched upon several administrative matters, including issues concerning transparency in public administration, accountability and improvement in the service delivery of autonomous bodies, the establishment of an effective body to stop corruption in all tiers of administration, the reduction of delays in project implementation and the use of modern technology for governance.

The Government of Bhutan has adopted a cautious approach to development, choosing to preserve its traditional culture and pristine environment and improve the health and educational standards of the population, in addition to raising incomes. This policy focus is referred to as increasing “gross national happiness”. The country has undertaken major structural reforms, including corporatizing government departments (in telecommunications), privatizing State enterprises (in trade, cement and banking), abolishing State monopolies (petroleum distribution), and putting the legislative framework in place for a modern, market-based economy. The Private Sector Development Committee has been formed, but to date there have been limited signs of private sector growth and development. The country’s difficult terrain and limited all-weather transport links, the small local market and limited effective demand are further impediments to private sector development. Such development is becoming a pressing issue as it is proving difficult to generate jobs for a longer-lived and better-educated population which no longer finds subsistence farming attractive. The Government is seeking to limit expatriate employment and to increase spending on developing human resources in the private sector.

Increasing “gross national happiness” is the goal in Bhutan

Poverty remains widespread among subsistence farmers in the rural areas of Nepal

Nepal is another country in which the overwhelming majority of the population relies on subsistence farming and lives in rural areas, where poverty is widespread. Progress in structural reforms has been limited so far, and most loss-making State-owned enterprises have still not been privatized. Donor impatience with the slow pace of implementation is threatening continued support. However, steps have been taken to reform the civil service and develop a comprehensive poverty reduction strategy. Nepal Rastra Bank is implementing a \$35 million financial sector reform programme with World Bank support. The two largest banks, one entirely State-owned and the other 41 per cent owned by the State, were technically insolvent and are now being managed by international firms of accountants to turn them around. The independence of the central bank has been increased and it has been given greater supervisory and regulatory authority. Prudential banking norms, on a par with international standards, have been introduced. However, civil disturbances may threaten the stability of the Government, making reforms more difficult to implement and forcing reductions in social spending to accommodate increased security costs.

Cambodia and the Lao People's Democratic Republic have embarked on major reforms

Both Cambodia and the Lao People's Democratic Republic are in receipt of three-year arrangements under the Poverty Reduction and Growth Facility of IMF. Cambodia is still undergoing reconstruction following a lengthy civil turmoil and transition from a centrally planned to a market-based economy. Reforms have so far concentrated on trade, banking, the private sector and public administration. Military demobilization, which has reduced the drain on public finances, and improvements in forestry management have also been important achievements and there was a moratorium on logging beginning on 1 January 2002. However, illegal logging continues to be a problem. Cambodia's Interim Poverty Reduction Strategy Paper recognizes that poverty alleviation depends on the realization of its growth potential, which hinges on political stability and improvements in physical and human resources. Cambodia more than doubled its spending on education between 1998 and 2001 and is committed to increasing this spending even further in 2002. However, weak capacity is seen as constituting a risk to programme implementation, and technical assistance along with donor support and debt relief, are seen as being necessary for success.

The challenge of poverty alleviation is particularly difficult in the Lao People's Democratic Republic

The approach to reforms has been more cautious in the Lao People's Democratic Republic, a landlocked country with a small and dispersed population, 80 per cent of which still live in rural areas. This makes the challenge of poverty alleviation particularly difficult. The focus of the Interim Poverty Reduction Strategy Paper is on macroeconomic stabilization and reform of State-owned commercial banks and enterprises, promotion of the private sector and improvement of public sector finances. VAT is to be introduced in 2003. Technical

assistance may also be needed to enhance public expenditure management and transparency in the context of greater decentralization, so as to sharpen the poverty focus. Deepening the financial sector and reducing dependence on agriculture, while ensuring domestic security, are additional challenges.

In contrast, economic policy in Myanmar has been dominated by central planning aimed at import substitution. Agriculture and energy are priority sectors and self-sufficiency in food production is seen to be important for social stability. Market-based reforms may be necessary to sustain growth. Myanmar has reduced its fiscal deficit entirely through cuts in expenditure. As a result, spending on education in Myanmar declined to just 0.6 per cent of GDP in 2001, and that on health fell to 0.2 per cent of GDP. While in principle all citizens have access to free health care in public hospitals, in practice funding levels are inadequate to deliver these services. As a result, privately funded education and health systems have been set up to provide these services to those who can afford to pay. Given Myanmar's infrastructural needs, additional cuts in capital and social spending may lead to lower medium-term growth prospects.

Bhutan, Cambodia, the Lao People's Democratic Republic and Nepal have yet to accede to WTO; such accession presents both opportunities and challenges and is a key policy issue. Qualifying for this new trading regime calls for further reductions in tariff and tax rates with significant implications not only for the level of protection enjoyed by the domestic industries but also for government revenues. Quotas for garment exports to Canada, the European Union, Norway and the United States will cease when the Multifibre Arrangement is phased out on 1 January 2005. The ready-made garment industry, which has been the largest exporter in some of the least developed countries, will have to face the challenge of surviving in a competitive market. Preparing the least developed countries to join WTO will require vigorous national capacity-building and information dissemination for the necessary awareness creation. In contrast, although Myanmar is a member of both ASEAN and WTO, investment sanctions, the withdrawal of preferential trade privileges and consumer boycotts have dimmed its prospects for using trade effectively as a vehicle for economic growth.

At the subregional level, the three least developed countries of South-East Asia have doubled efforts to bring their finance, investment, commerce and trade sectors into alignment with ASEAN standards. Trade liberalization, particularly within ASEAN, could have significant benefits for these countries, as preferential access can be used to generate export growth and investment from other countries; this is discussed further in box II.6.

Myanmar continues to effect import substitution but limited resources constrain spending on the social sectors

Regional and global trade and economic cooperation present both opportunities and challenges

Membership in ASEAN and AFTA gives added impetus to reform efforts