Note

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Summary

The present report contains the main findings and recommendations of the tenth session of the Committee for Development Policy, held at United Nations Headquarters in New York from 17 to 20 March 2008. The Committee addressed three major themes: achieving sustainable development goals in the context of climate change; the worsening of global economic prospects and implications for developing countries; and matters related to the identification and graduation of least developed countries.

The Committee stressed that achieving and sustaining the goals of the international sustainable development agenda requires both deep reductions in carbon emissions and adaptation policies to address the current and future consequences of global warming. Key issues for developing countries are creating incentives for economic growth along pathways that are less carbon-intensive and enhancing adaptive capacities, particularly in the most vulnerable and poor countries. An effective sustainable development strategy must be based on investment, innovation and institutional capacity. International cooperation is fundamental as the strategy will require appropriate and sufficient funds as well as technology development, transfer and dissemination. Greater coherence and integration between climate and development policies both at national and international levels is necessary.

The Committee examined the worsening global economic outl.0062.796 Tafafafafaf 2094(e)36(ao)-

Contents

Chapter I

Matters calling for action by the Economic and Social Council or brought to its attention

A. Matters calling for action by the Council

Recommendation 1: towards the implementation of internationally agreed goals on sustainable development

2. Worsening global economic outlook: reforming the compensatory finance architecture

6. Reform of the existing architecture of compensatory finance is urgently needed in view of the disruptions caused by external shocks on development and of the costs and risks of accumulating large reserves. The key features of a reformed official compensatory liquidity architecture should include fast disbursement of funds, with low or no conditionality, in proportion to the severity of shocks.

3. Developing a consistent set of criteria for the least developed countries category

7. After a thorough review of the indicators and approaches used for the identification of the least developed countries, with due account taken of economic vulnerability, the Committee reconfirmed the reliability of the current criteria and concluded they are based on the best available methods and information.

4. Supporting smooth transition strategies for graduating least developed countries

8. The Committee stressed the importance of smooth transition measures for graduating countries and reiterated its continuing support to graduated countries. In that respect, the Committee proposed that an expert group should be convened to consider the phasing out of least developed country benefits with a view to identifying some benefits to be maintained for a certain period.

5. Monitoring the development progress of Cape Verde

Chapter II

Achieving sustainable development within an environment of climate change

1. Since the Committee for Development Policy considered, in its report to the Economic and Social Council on the ninth session,[1] the challenges of climate change to the implementation of the international development agenda, the urgency of the issue has become greater and its relevance to development more manifest. In that report, the Committee stressed its concern with the lack of proper integration of climate issues into development action. The Committee has since worked towards identifying the elements that need to be incorporated into that agenda to satisfy sustainable development goals and to provide a concrete framework for operationalizing international cooperation, within the parameters set by international agreements.[2]

2. Coming after the adoption of the Bali Action Plan,[3] the Committee, at its tenth session, addressed the question of achieving sustainable development goals by looking at the key channels through which climate change can affect development and the corresponding ways of protecting against those impacts, namely through adaptation and mitigation policies, international cooperation (especially in finance and technology) and improved policy coherence.

A. Climate change and emerging challenges to sustainable development

3. Sustainable development is a process of change in which the exploitation of resources, the direction of investments, the orientation of technological development and institutional change are all compatible and enhance the needs of the present without compromising the ability of future generations to meet their own needs.

4. For developing countries, sustainable development confronts a three-dimensional threat from climate change. The first dimension relates to the implications of climate change for human development and prosperity, which are at the heart of the Millennium Development Goals. The second dimension results from the spillover of climate-related policies in the industrialized world. The third dimension relates to the implications of actions taken by developing countries themselves to adapt to and mitigate climat

Vulnerable countries: the least developed countries and the small island developing States

6. The threats of climate change will particularly affect the development prospects of the least developed countries and the small island developing States. Although such countries have contributed the least to the emission of greenhouse gases, they are the most vulnerable and have the least capacity to adapt to the effects of climate change.

7. Their vulnerabilities are related to atmospheric and oceanic warming, changes in precipitation and extreme events, and they are manifested mainly in relation to water, agriculture and food security, health, ecosystems and coastal zones. Over time, one likely outcome of climate change is the disappearance of some small island developing States as a result of a rise in the sea level. African countries are also among the most vulnerable to climate change, owing to a low adaptive capacity caused by widespread, extreme poverty and projected changes in precipitation coming on top of an already stressed situation.

B. Towards an integrated approach

8. The major issue in addressing climate change as an integral part of the wider sustainable development agenda is to create and provide incentives for sustainable economic growth along pathways that enhance the capabilities and options of people and societies. That implies a transition towards economies that are less carbon intensive and the enhancement of adaptive capacities in developing countries.

9. The main approach to climate policy in industrialized countries has been the cap-and-trade system. Given their growing energy needs, developing countries need a different approach to sustainable development. This approach should be based on investment, innovation and institutional capacity-building. Several developing

the calculation of equitable targets as improved environmental performance in some developed countries may have come about by a shift of carbon-intensive activities to developing countries.

Deforestation and land use

16. An issue of relevance to development is that of land use and deforestation. Those factors contribute roughly one quarter of global greenhouse gas emissions. Furthermore, increased production of biomass for fuel generation is having a significant impact on food security, on food prices and on biodiversity. Changes in land use also affect the rights of local communities whose livelihoods depended on previous use patterns of the same land. A different approach could provide a win-win solution, such as by involving local communities that depend on local forests for a living in also helping to protect and regenerate the forests while allowing the communities rights of sustainable extraction as an incentive. Many countries have successfully followed that route, leading to an increase in forest cover and stemming deforestation.

The investment approach to mitigation

17. Different climate policies have different impacts on development trajectories and hence vary in terms of impacts on climate. Rather than following traditional fossil fuel-dependent development paths as did the industrialized countries, sustainable development requires an energy transition strategy that redirects investments to greater energy efficiency and renewable energy alternatives. Such a transition needs an innovation- and investment-oriented way of shaping mitigation strategies and institutional capacity-building towards enhanced mitigation capacity.

18. The urgency of such a strategy is particularly acute for developing countries. At the global level, the costs of mitigation have been estimated at about 0.3 to 0.5 per cent of the annual world output, corresponding to additional annual investment flows of between $200 and $210 billion by 2030 for mitigation in order to return greenhouse gas emissions to current levels.[6]

The mitigation regime

19. There are three main, not mutually exclusive, policy approaches to dealing with mitigation in general and with outcomes harmful to the environment in particular: (a) creating a quasi-market to define emission rights (such as the cap-and-trade approach); (b) applying taxes to internalize the external costs of emissions (for example, a carbon tax); and (c) dealing directly with the cause of the harmful outcomes through regulation.

20. Each of the above-mentioned options implies some level of public regulation. The first two options rely on the market's correcting capacity (after redefining property rights or by changing the cost conditions with which they operate), while the third option entails more active regulation procedures as (even corrected) markets may not generate an acceptable solution (or not within an acceptable time period). Furthermore, a number of additional options that may be more effective in

[6] United Nations Framework Convention on Climate Change, "Report on the analysis of existing and potential investment and financial flows relevant to the development of an effective and appropriate international response to climate change", Dialogue Working Paper 8 (2007).

the context of developing countries appear to have been disregarded in policy discussions. Foremost among them are funding for research and development, regulation of fuel portfolios and emission levels, economic incentives, technological support and education. Given the urgent and demanding challenge the world faces, the complementary features of all those alternative channels for action must be stressed.

2. The importance of adaptation

21. A two-way relationship exists between development and adaptation. While building resilience to climate change contributes to the attainment of development, climate change negatively affects the livelihoods of people in many developing countries, especially in the least developed countries, thereby reducing their capacity to adapt. Integrating adaptation into sustainable development is therefore necessary to tackle the negative impact of climate change on development goals. The main issues for adaptation in sustainable development are set out below.

Poverty and adaptation

22. Poverty is closely related to vulnerability to climate change through (a) climate-related risks to securing well-being; (b) poverty-related constraints on adaptive capacity; and (c) poverty-related determinants of exposure. Those aspects need to be addressed if poverty reduct

forestry and fisheries, water supply, human health, coastal zones and infrastructure). A large share (from $28 to $67 billion) is needed in developing countries.

Challenges for policy research

Chapter III

The worsening global outlook and its implications for developing countries

A. Slowdown of the world economy

1. The global economic outlook has become gloomy, along the lines of the pessimistic scenario in *World Economic Situation and Prospects, 2008*.[9] If the economy of the United States should slide into recession in 2008, world economic growth could slow from an estimated 3.7 per cent in 2007 to just 1.6 per cent in 2008 (see figure 1). Global instability will impact negatively on developing countries, with a potential to delay further the achievement of the internationally agreed development goals, particularly in the least developed countries. Low-income countries, where recent economic performance has been boosted by higher commodity prices and increased external

1. Impact on development

2. Robust economic growth in the developing world, which has been building momentum over the past five years, may cushion the world economy from a hard landing. Growth in the developing economies has been above 6 per cent per year on average since 2004, while economic growth among the least developed countries has been at 7.2 per cent per year since 2001. Still, developing country performance has, in no small part, been based on strong consumer demand in the United States. The growth prospects of developing countries are unlikely to be fully decoupled from the macrofinancial weaknesses in the United States.

3. Exports from developing countries will also likely be affected. In fact, the rate of growth of the volume of manufacturing exports from the developing world had already decelerated somewhat in 2007, particularly in China, in other parts of East Asia and in Latin America.

4. The low-income countries, and especially the least developed countries among them, will feel the impact of slower growth in the United States directly because they depend heavily on North American markets for their exports.[10] More importantly, however, the adverse effects will likely be an indirect spin-off from a slowdown in the production of manufactures in the emerging markets, particularly in East Asia, which may put an end to the commodity price boom of the past years. While it is true that the dollar depreciation and weakness of financial markets in the United States is putting upward pressure on commodity prices, as international investment funds seek positions in safer real assets, the impact of such factors may be soon outweighed by that of slower growth of world output and weaker demand for commodities.

5. The high export dependence of least developed countries on primary commodities (about 80 per cent of the merchandise exports of the group as a whole) makes them particularly vulnerable to such developments. While greater trade diversification offers a path to reduced vulnerability, late-comers are finding it more difficult to build a competitive edge in international markets. In any case, trade diversification is a long-term process, and other approaches are needed to cope with the consequences of adverse external shocks in the short and medium term.

2. High levels of reserve accumulation in developing countries

6. In response to the sharp negative effects of shocks experienced by developing countries in the 1990s and to the lack of effective compensatory mechanisms at hand, many developing countries have accumulated vast amounts of foreign exchange reserves over the past decade. That is one of the aspects that would need to be revisited in the light of policies aimed at a global demand rebalancing, as the current pattern is strongly linked to the existence of global imbalances. Most of the reserves are invested in dollar-denominated assets and thereby finance the deficits of the United States.

[10] Net fuel-exporting countries such as Angola (with 40 per cent of its exports going to the United States and Canada), Chad (75 per cent) and Equatorial Guinea (44 per cent) are cases in point. Other least developed countries also have relatively high export shares to North American markets, including Cambodia (61 per cent), the Comoros (42 per cent), Haiti (85 per cent), Madagascar (37 per cent), Maldives (40 per cent) and Nepal (27 per cent).

13. The supply of the kind of assistance described above for contingency financing requires an appropriate architecture and sufficient resources. There is an urgent need to improve existing compensatory financing mechanisms and/or design new ones.

C. Compensatory financing: broad principles and key features

14. External shocks usually have both short-term and long-term impacts, some of which can be sizeable in magnitude. Negative short-term effects are inevitable unless reserves and additional external finance are available to cushion their impact. Domestic policies can contribute to mitigation of the negative effects. The country's fiscal policy framework should thus be built on mechanisms that allow fiscal deficits to expand when a country is hit by a shock rather than contract as is usually the case (the IMF and donors should also support such mechanisms). The automatic expansion of fiscal deficits to cope with economic shocks will help to maintain economic activity and support the financing of structural policies needed to manage possible long-term effects of the shock.

15. If the shock proves to be temporary (for example, a brief deterioration of the terms of trade or a one-year episode of drought) any negative impact on growth and poverty could be mitigated to the extent that a high proportion of the costs of the shock were to be financed through the swift provision of official liquidity, which would allow imports and government spending to be maintained at normal levels. If a shock proves, ex-post, to be long-lived (for example, persistent terms-of-trade deterioration that is not reversed or repeated droughts), repayment of compensatory official liquidity should be automatically extended, to allow an orderly gradual restructuring of the economy.

16. If the shock is likely to be long lived, conditions or incentives attached to loans should tackle the source of the problem. For example, if it seems likely that the price of the main export will remain low, financial support should be given for measures such as increased investments and more competitive exchange rates to encourage and facilitate export diversification. For net fuel-importing countries, if the problem is continued high oil prices, investment in greater energy efficiency, as well as the development of alternative domestic sources of energy, should be supported. If shocks are due to recurring natural disasters, long-term prevention and adaptation policies are called for. In all of the preceding cases, structural policies to

E. Policy recommendations

21. In view of the worsening global economic outlook and its implications for developing countries, and the costs and risks of carrying large reserve holdings, the Committee makes the following recommendations regarding compensatory financing mechanisms:

(a) A reformed compensatory financing architecture should be developed to provide official liquidity and aid to developing countries suffering the negative impact of external shocks such as those from trade, natural disasters and sudden drops in private capital net inflows;

(b) The reform of the existing compensatory financing mechanisms should be conducted by taking into consideration the following aspects:

(i) IMF facilities should be significantly simplified because existing schemes are too numerous and complex. The design of loan and grant facilities should include automatic augmentations of disbursements proportionate to the terms of trade shocks;

(ii) Export shortfalls should be measured in terms of either import capacity or the purchasing power of exports. The facilities to finance shocks should include all food imports, not just cereals. A new oil facility should be activated;

(iii) All available compensating facilities should have the same attributes of speedy disbursement, scale proportionate to the shock and low conditionality to ensure coherence and optimization of the beneficial impact on the receiving countries. Lending on more concessional terms is highly desirable, especially for heavily indebted low-income countries.

Chapter IV

Issues relating to the least developed countries and the graduation process

A. Introduction

1. In preparation for the 2009 triennial review of the list of least developed countries, the Committee for Development Policy re-examined the methodology for the identification of least developed countries. The Committee was guided in its work by Economic and Social Council resolution 2007/35, in which the Council requested the Committee "to continue developing a consistent set of criteria that can be applied to all recommendations regarding the inclusion in and graduation from the list of least developed countries, with due account being taken of economic

least developed countries. It was noted that identifying least developed countries on the basis of income distribution could bias results towards countries pursuing policies that result in greater income inequality. Measures of income inequality are, moreover, not readily available for all concerned countries and are often unreliable. It was also noted that income inequality is reflected, partially and indirectly, in the human assets index. The Committee noted that similar considerations apply to the incorporation of poverty rates in the criteria.

2. Human assets index

7. The Committee agreed that the status of human capital should continue to be reflected in the human assets index by indicators related both to the level of health and nutrition and to the level of education.[12] The following four indicators (2o7 2ur 1 Td[hupl.11 -4(h

(c) Concentration of merchandise exports;

(d) Share of agriculture, forestry and fisheries in GDP;

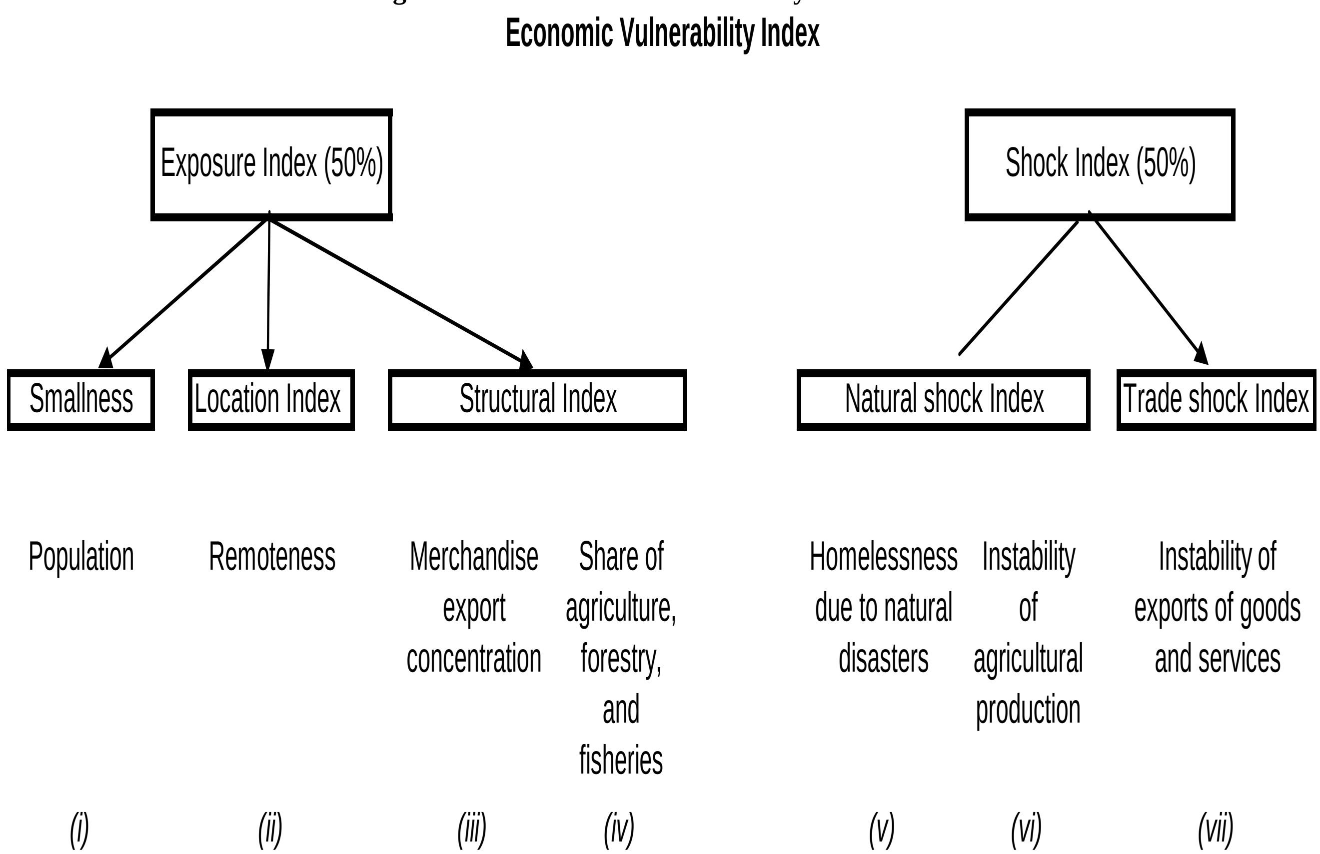
(e) Homelessness due to natural disasters;

(f) Instability of agricultural production;

(g) Instability of exports of goods and services.

The structure and weights of the composite index are set out in figure 2.

Figure 2
Structure and weights of the economic vulnerability index



11. The Committee reconfirmed that the smallness measured by population size (a) is a suitable indicator for vulnerability; most small low-income countries are situated in regions that are prone to natural disasters.

12. The Committee also reconfirmed the validity of remoteness (b) as measured by an indicator for the distance to the world market with a dummy correction for land-lockedness. In recent years most countries identified for graduation have been archipelago countries with high transportation costs and duplication of infrastructure and services resulting from geographical fragmentation. As those special features may be not reflected in a quantified indicator, it was recommended that the impact

of such specific geographical aspects on development should continue being addressed in the vulnerability profile (see section IV.D).

13. It was noted that merchandise export concentration (c) is a measure of exposure to external shocks, but that as currently applied it excludes services. In many countries exports of services, notably tourism, reach a significant magnitude. At a previous review of the criteria, the Committee had requested the inclusion of services in a revised export concentration index.[13] However, methodological differences in terms of both data collection and reporting and in classification procedures do not allow for goods and services to be merged into a new export concentration index. Accordingly, the Committee decided not to change the indicator, requesting instead that the volatility of exports of services be duly analysed in the vulnerability profiles of countries being considered for graduation.

14. Indicator (d) expresses the exposure to shocks resulting from the structure of production activities. The Committee considered that agricultural activities, including fisheries and forestry, were particularly subject to natural and economic shocks.

15. The Committee also considered whether high dependence on the tourism sector could be included as a measure of external vulnerability. Tourism is, however, not defined in the national accounts as a separate industry. A proxy for tourism could be entered into a redefined version of indicator (d), but the Statistical Division of the Department of Economic and Social Affairs indicated that there are severe data limitations. Therefore, the Committee decided that the vulnerability profiles should give due consideration to shocks in the tourist sector on a case-by-case basis.

16. The two natural shock indicators, homelessness (e) due to natural disasters and instability of agricultural production (f), are complementary in capturing natural shocks, as evidenced by the small correlation between them. The Committee agreed to retain the two natural shock indices.

17. Similarly, it was reaffirmed that the instability of exports of goods and services (g) is a good proxy for trade shocks (g). The point was raised whether worker remittances and their instability should be taken into account. However, data coverage remains inadequate, and the quantification of remittance flows is problematic since a large share of remittances is transferred through informal channels. Consequently, it was decided to leave this dimension to be addressed in the vulnerability profiles.

18. The Committee also assessed to what extent the EVI adequately reflects the environmental factors of vulnerability. It was noted that the natural shock sub-index captured the incidence of adverse environmental phenomena as an observed event, but one which is also likely to recur in the future.

19. The Committee recalled that it had previously reviewed the issue of environmental vulnerability as a structural impediment to growth[14] and reconfirmed

[13] *Official Records of the Economic and Social Council, 2002, Supplement No. 13* (E/2002/33), para. 138; and *Local Development and Global Issues: Report of the Committee on Development Policy on the Fifth Session* (United Nations publication, Sales No. E.03.II.A.3), paras. 21 to 24.

[14] At the request of the General Assembly, the issue of considering an environmental index was discussed at length. It was agreed at the time to distinguish clearly between economic vulnerability and ecological or environmental vulnerability. See *Official Records of the Economic and Social Council, 2002, Supplement No. 13* (E/2002/33), para. 146.

that the addition of components related to climate change challenges was relevant only if they reflected a structural handicap to growth.

20. The economic vulnerability index already includes components that capture sources of economic vulnerability generated by the natural environment. The risk that natural shocks can affect growth is reflected in the EVI both through the natural shock index (with its two components, homelessness and instability of agricultural production) and the exposure index. The trade shock index also captures, to some extent, risks to growth caused by natural shocks.

21. While climate change is already affecting some countries, different countries will face different impacts, and it would be important to specify whether and how bdient.to growtoh

condition for graduation. However, it was found that it would run counter to the logic of the criteria for designating least developed countries. A high EVI score does not by itself prevent a country from achieving a steady development path, as evidenced by sustained and increasing GNI per capita and high levels of the human assets index in countries which have a high EVI. Therefore, the Committee concluded that the fulfilment of the EVI criterion should not be made a compulsory requirement for graduation.

26. At the same time, the Committee reiterated the importance of flexibility, that is, the criteria should not be used mechanically, particularly in situations where country indicators are very close to inclusion or graduation thresholds (“borderline cases”). In those cases, a combination of the structural handicap criteria (HAI and EVI) could be applied.[17] Such consideration would make198 TdpArg5(at it would ratTJ0.0814 Tw 17.9rg5(

to development financing, international trade and technical assistance. The effective implementation of the impact assessments would require that the Department of Economic and Social Affairs be able to draw on the cooperation of donor countries, international cooperation agencies, trading partners and the country concerned.

E. Smooth transition for graduating countries

economic vulnerability. Finally, the Committee encouraged Cape Verde and its development partners to make full use of the future meetings of the consultative mechanism (Grupo de Apoio à Transição) to obtain support for the country's economic transformation agenda.

Chapter VI
Organization of the session

1. The Committee for Development Policy held its tenth session at United Nations Headquarters from 17 to 20 March 2008. Twenty-one members of the Committee as well as observers from several organizations within the United Nations system attended the session. Annex I contains the list of participants.

2. The Department of Economic and Social Affairs of the United Nations Secretariat provided substantive services for the session. The Chairperson of the Committee opened the session and welcomed the participants. Subsequently, the President of the Economic and Social Council addressed the Committee and stressed the importance of the Committee's contribu

Annex I

List of participants

1. The following members of the Committee attended the session:

Ms. Bina Agarwal
Mr. José Antonio Alonso
Ms. Lourdes Arizpe
Mr. Tariq Banuri
Mr. Olav Bjerkholt
Mr. Kwesi Botchwey
Ms. Gui-Ying Cao
Mr. Ricardo Ffrench-Davis (*Chairperson*)
Ms. Stanislawa Golinowska
Mr. Patrick Guillaumont
Mr. Philippe Hein (*Rapporteur*)
Mr. Hiroya Ichikawa
Ms. Willene A. Johnson
Ms. Amina Mama
Mr. Hans Opschoor

Annex II

Agenda

1. Inaugural session.
2. Adoption of the agenda and organization of work.
3. The least developed countries: refining the criteria, the graduation process and follow-up.
4. The sustainable development agenda and climate change: implementing the internationally agreed goals and commitments in regard to sustainable development.
5. Current financial turmoil and implications for developing countries.
6. Other matters.
7. Future work of the Committee.