

## CHAPTER 5

# REDUCING TRADE COSTS FOR LEAST DEVELOPED COUNTRIES

*Contributed by the Executive Secretariat for the Enhanced  
Integrated Framework*

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**Abstract:** *For the LDCs reducing trade is doubly important because since they start from a lower base, they can potentially derive disproportionately higher benefits compared to other countries. Thus LDCs are taking necessary measures aimed at lowering trade costs either on their own or with the support of the private sector, and some have achieved considerable success. However, they are unable to make a transformative shift because of limited institutional capacity and resource constraints. This is where aid for trade can help, as evidenced by the success achieved by various multilateral, regional and bilateral aid-for-trade initiatives. The paper shows that the impact of aid-for-trade intervention on reducing trade costs in LDCs tends to be higher when they include a robust and credible analytical work, a high level of country ownership, institutional capacity building on a sustained basis, continuous support for a sufficiently long period, resource leveraging and a co-ordinated response from donors. Moreover, such intervention can be successful if political economy challenges are appreciated, mainstreamed and mitigated.*

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## INTRODUCTION

Trade costs have become a focus of discussion within trade policy and academic circles in the recent past due to their increased visibility when it comes to reducing traditional trade barriers. In the context of rapid integration of the global economy and its significance for propelling growth, the imperative to reduce trade costs to become and remain competitive in the international and regional markets is well documented. However, this is more urgent in the context of the LDCs, where most of the exporting firms are Small and Medium-sized Enterprises (SMEs), where trade costs are reducing more slowly compared to those of their trading partners, where export diversification is an urgent need, which have the lowest level of participation in the global/regional value chain (GRVC) and which are amongst the landlocked countries and/or in fragile situations.

Realising the growing need to reduce trade costs, the LDCs have been taking various initiatives either *suo moto* or in collaboration with the private sector, although these actions alone are not likely to contribute significantly to overcome the entire range of impediments facing the LDCs. On the one hand, LDCs are taking considerable time to undertake these reforms, either because of lack of resources or due to the absence of relevant expertise. On the other hand, other countries are reforming at a much faster pace, making it difficult for the LDCs to catch up, thereby further eroding the latter's competitiveness in the global market. On the positive side, given that LDCs are starting with lower bases, the bang for the reform buck is likely to be higher for them compared to developed countries, which have almost reached the point of reform saturation.

The LDCs have also been receiving aid-for-trade support to address the issue of trade costs, among other things, from various bilateral and multilateral donors, as well as through the EIF – a multi stakeholder co-ordination framework that is exclusively devoted to building the LDCs' trade capacity. Although LDCs face a host of trade-related challenges, including alleviating their supply side constraints and building their productive capacity, the focus of this chapter is exclusively on trade costs, as this features as a predominant agenda within the broad universe of aid-for-trade support. This chapter is organised as follows:

The next section discusses why trade costs matter for the LDCs and whether there are important differences in the relative importance of trade costs for different categories of LDCs. This followed by a section that analyses trade costs in LDCs over the last ten years with a view to finding if there are any distinct differences in these costs between different categories of LDCs. The following section looks at priorities for LDCs in addressing trade costs and whether or not such priorities have changed over time. It will also identify drivers of change in cases where reform has been successfully undertaken to lower trade costs.

The penultimate section looks at the role of development partners and other agencies involved in the delivery of aid for trade by considering the evolution and flow of aid for trade, particularly in the context of the LDCs, and examining the evidence to see if aid for trade has contributed to reducing trade costs in LDCs. Based on the experience of the EIF, the section also investigates what works and what does not, as well as where improvements are needed in addressing the challenges of trade costs facing LDCs. The final section concludes.

## SALIENCE OF TRADE COSTS FOR LDCs

A relatively new generation of trade literature predicates that more than six decades of multilateral trade negotiations, a series of preferential trade arrangements and a large number of autonomous liberalisation measures have contributed to the reduction of border trade barriers, i.e. tariff barriers and quantitative restrictions to a significant extent, particularly for the exports of LDCs. This has resulted in increasing focus of researchers and policy makers towards other elements of trade costs.

The definition of trade costs for merchandise trade can encompass any barrier and impediment that can increase the cost of international trade. However, due to a limitation on the availability of information and data and to ensure a focused analysis, trade costs for the purpose of this chapter are narrowly defined to include costs related to border procedures and transportation and logistics for merchandise trade only. The narrow tailoring of this definition is in no way purported to undermine the significance of other elements of trade costs both for merchandise as well as services trade.

Although trade costs matter to all groups of countries, their heightened significance in the context of LDCs is explained by the following inter-related but distinct factors:

First, although trade costs are generally reducing, they are falling more slowly in low income countries (Arvis et al., 2013), a category within which a large majority of LDCs belong. ITC (2013a), which supports this argument, suggests that the average trade costs in LDCs are substantially higher than in other countries. Using costs relating to cross-border movement of a standard container, Koniger et al. (2011), for example, find that when compared to other countries LDCs on average paid 43% more to export and 54% more to import.

Second, LDCs' participation in the GRVCs is increasing but limited. ITC (2013b), for example, shows that LDCs have been gradually catching up over the past decade with their developing country counterparts in terms of their participation in GVCs as measured by exports of transformed products and imports of intermediary goods. However, there is a considerable variation within the LDCs, and the pace of their integration leaves much to be desired. In their pursuit to participate in GRVCs, LDCs face exclusionary barriers, which include factors that drive up trading costs and undermine competitiveness (ITC, 2013a). Although trade costs are not the only element that contribute to the success of LDCs in integrating themselves into GVCs, they are certainly important. Since reductions in exports as well as import costs are necessary to achieve results on this front, LDCs need to make a transformative shift towards reducing both types of trade costs, particularly the latter, which tends to be disproportionately higher in LDCs.

Third, export concentration in LDCs – both product-wise and market-wise – is much higher than in developing countries (ITC, 2013a). At the same time, the LDCs' attempt to diversify exports – both at intensive and extensive margins – has failed to produce the desired results. For example, despite several attempts by LDCs, the survival rate of new products introduced by LDCs into the regional and global markets has been low. Nicita et al. (2013), who studied the survival of the flows of LDCs' exports to 190 countries between 1993 and 2007, show that 41% of LDCs' products face extinction compared to 15% for other developing countries. This is consistent with Fernandes et al. (2013), who find that the new entry rates for countries with low per capita income are lower, and that exit rates are higher compared to relatively higher income countries.

Fourth, most LDCs are handicapped by several natural barriers that add to their trade costs. Of 31 Landlocked Developing Countries (LLDCs), 16 are LDCs. Similarly, out of 40 Small Island Developing States (SIDS), nine are either LDCs or recently graduated LDCs. Although the occurrence of natural disasters cannot be avoided, limited disaster mitigation capacity means that such disasters can have serious implications for trade costs in the LDCs. For example, the earthquake that hit Haiti in 2010 caused the collapse of the main deck of the public wharf, as a result of which the capacity of the international Port-au-Prince port was severely affected. The port now operates with only three floating docks, thereby

restricting trade potential and increasing trade costs due to delays (Haiti DTIS, 2013). As recently as mid-March 2015, the damage caused by the tropical cyclone Pam to infrastructure in the Pacific Islands Countries, such as Vanuatu, Kiribati and Tuvalu, is likely to have debilitating effects on trade costs in these countries. For example, as documented by the Asian Development Bank, in the case of Kiribati tidal surges extensively damaged the Betio-Tarawa causeway, a key transport link in the country (ADB, 2015).

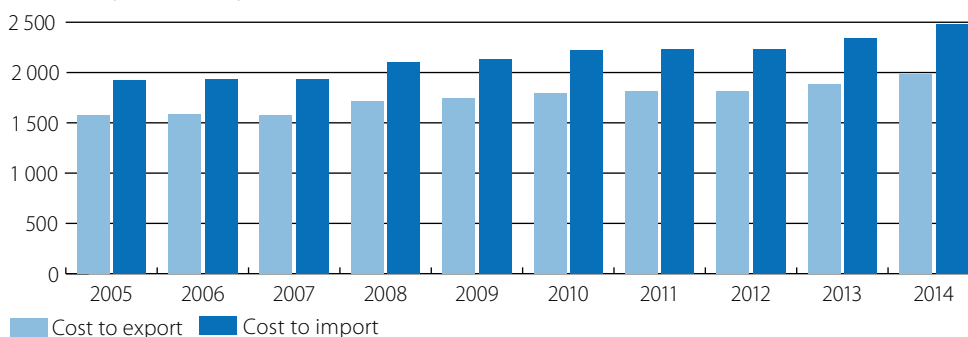
Additionally, several LDCs are vulnerable to climate changes due to: i) their location in parts of the world that are expected to be badly affected by temperature and precipitation changes; ii) a huge reliance on climate-sensitive economic sectors, such as agriculture, for generating export revenues; and iii) a limited capacity to adapt to negative external events due to a low level of economic development and stretched institutional capacity (Bruckner, 2012). Since the LDCs tend to incur higher trade costs than other countries on average due to these natural handicaps, which cannot be changed in the short run, they should focus on reducing other elements of trade costs to remain competitive in the global market.

Fifth, given that the size of the domestic market is highly correlated with the average size of firms and exports, as Fernandes et al. (2013) point out, firms in a large majority of LDCs, where the market size is small, are likely to be SMEs. According to the study, firms from the LDCs comprised SMEs whose exports values were relatively low. These firms exported much fewer products, with most of them exporting just one product to a single market. Since these firms are unlikely to achieve economies of scale and the level of competitiveness that is required to survive in the global market, their survival rate in the international market tends to be much lower compared to the enterprises in advanced countries. Due to limited and uncertain revenues, including export earnings, the burden of higher trade costs converted into percentage terms disproportionately disadvantages the SMEs. Moreover, unlike large companies, they do not have the in-house capacity or expertise to overcome these barriers and need to hire professional agents, which further increases their trade costs (ITC and WTO, 2014; Snow et al., 2004).

The combined effect of all these factors is reflected in various global indicators, including the Doing Business indicator, the Logistics Performance Index (LPI) and the Enabling Trade Report. Figure 5.1, which is based on the Doing Business database, provides a comparative picture of trade costs incurred by LDCs – both for export as well as import in the past decade. Going by these numbers, it appears that both categories of trade costs faced by LDCs have generally increased. While the cost to export was USD 1 578 in 2005, it increased to USD 1 980 in 2014, posting an increase of 25%; the corresponding figures for imports were USD 1 928 and USD 2 484 respectively, suggesting an increase of 29 % over the past decade (Figure 5.1).

**Figure 5.1 LDCs' costs of exporting and importing, 2005-2014**

USD MILLION (2013 CONSTANT)



Source: World Bank, Doing Business database.

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Since there is considerable heterogeneity among LDCs based on their geographic location, political situation, governance status, structure of economies, natural resource endowment, institutional capacity, level of integration with the global and/or regional economies, etc., there is a sizeable variation on trade costs faced by different groups of LDCs. Moreover, it is equally necessary to take cognizance of the fact that trade costs are also affected by the willingness and capacity of the LDCs to design and implement reforms, their participation in various aid-for-trade initiatives and their participation in regional trade.

Although reducing trade costs is a worthy goal to be pursued by all the countries alike, they are relatively more important for some categories of LDCs than others due to a confluence of factors. For the purpose of this chapter, they are divided into the following categories: i) sub-regional dimension; ii) landlocked status; iii) commodity dependence; and iv) fragile situation.

### Sub-regional dimension

At a general level, LDCs are conventionally divided into three convenient sub-regions, namely sub-Saharan Africa (which includes Haiti), South Asia and South East Asia/Pacific. Based on such classification, trade costs have been increasing in the first two and reducing in the latter according to Doing Business Report figures. However, there are considerable variations in trade costs within these four groupings. Therefore, we have prepared the following detailed sub-regional groupings to present the data, which will guide our analyses: i) Caribbean; ii) Central Africa; iii) East Africa; iv) Middle East and North Africa; v) Pacific; vi) South Asia; vii) South-East Asia; viii) Southern Africa; and ix) West Africa (countries included in these sub-regions are provided in Annex 1).

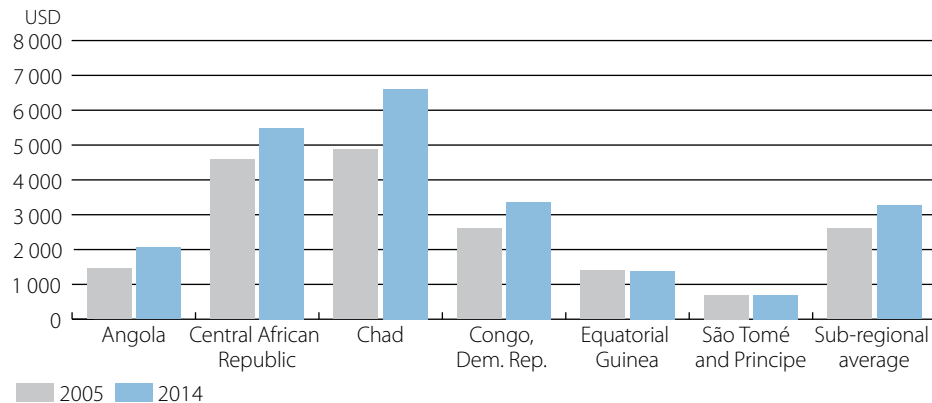
Two of these sub-regions where the trade costs faced by LDCs, as measured by import and export costs, are the highest are Central Africa and South Asia. These are precisely the regions within the LDCs that should focus more on reducing trade costs than other sub-regions. Figure 5.2 depicts the situation of the Central Africa sub-region, where the left axis is the change in export cost between 2005 and 2014 and the right axis is the percentage change. In this sub-region where six LDCs are located, the average cost of exporting for LDCs was USD 2 598 in 2005. This has increased to USD 3 200, reflecting a 23% rise over a period of eight years (Figure 5.2a). The average cost for importing increased from USD 2 524 to USD 3 441, representing an increase of 36% during the corresponding period (Figure 5.2). It is not the increase in these costs that is problematic but the base itself, which was very high to begin with. This is due to the poor state of transportation within the Central Africa region, as aptly captured by an AfDB report. Due to the presence of several landlocked countries in the region and limited air connectivity, around 80% of people and goods in the region are transported by land, yet asphalted roads represent less than 20% of the whole regional road network (Harding, 2011).

Despite the presence of coastal countries, such as Angola, Equatorial Guinea and Sao Tome and Principe, which incur much lower export costs compared to the LDC average, high costs are largely driven by landlocked countries in the sub-region, namely Chad and the Central African Republic. Although the Democratic Republic of the Congo is a coastal country in theory, it can be considered as *de facto* landlocked as it has a short coastline far from the main cities (World Bank, 2010). Chad is the country with the highest cost of exports as well as imports in the world. Its export costs are consistently higher than the sub-regional average by anywhere between 43% and 59% (Figure 5.2).

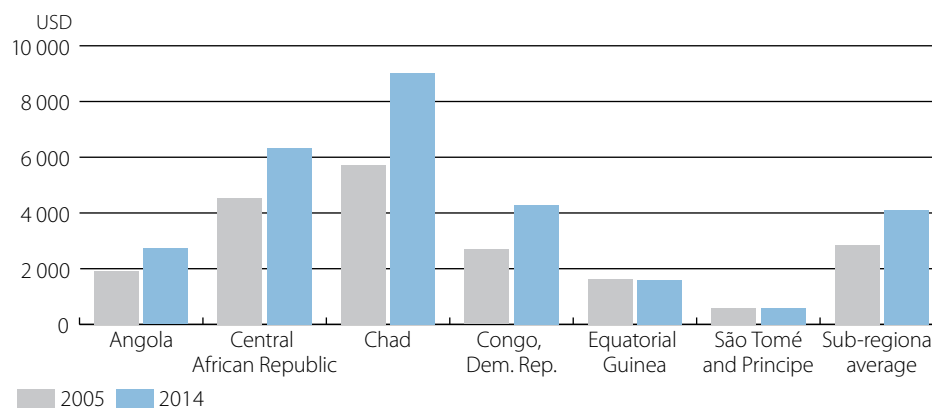
Moreover, based on the figures available for 2014 from the World Bank's Doing Business Report, it takes 70 days to export from Chad, which is the second highest next to Afghanistan, where it takes 86 days to export. In terms of time taken to import, Chad is at 90 days, again second only to Afghanistan, where it takes 91 days. It is also clear from the figures that Chad is the only country where the costs of both imports and exports have increased significantly, whereas in the case of other countries in the sub-region, costs have either plateaued or even marginally declined after 2009 (not shown in the figure).

**Figure 5.2 Cost of exporting and importing from LDCs in the Central Africa sub-region, 2005-2014**

**Cost of exporting**



**Cost of importing**



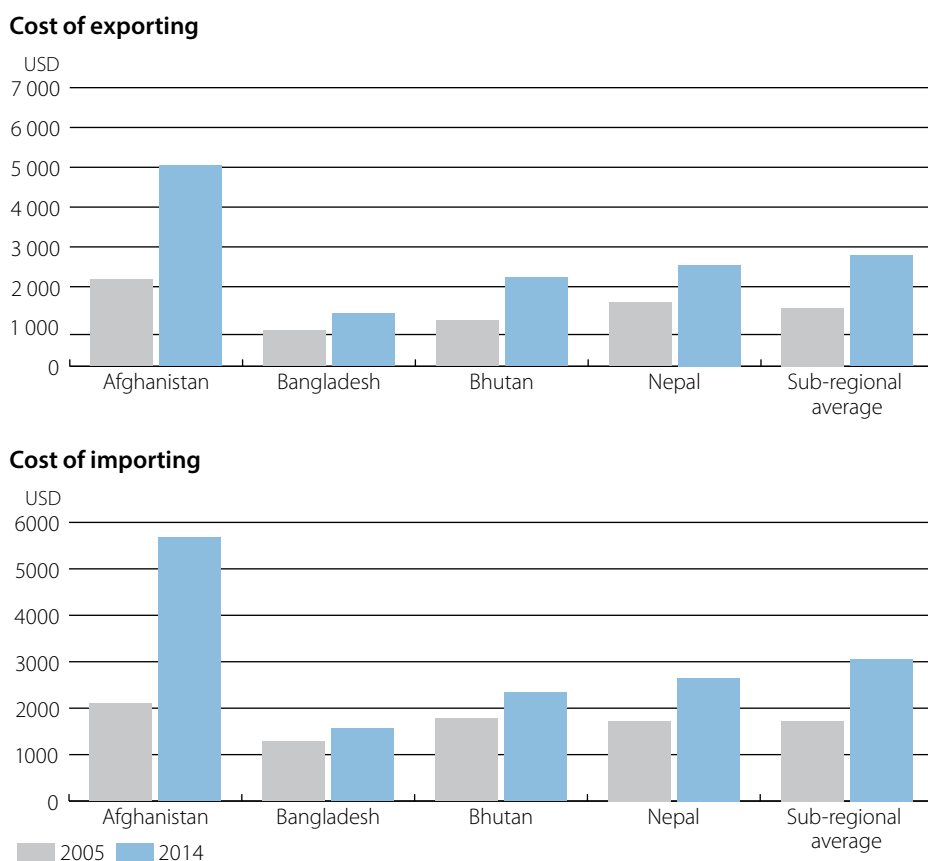
Source: World Bank.

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South Asia is a sub-region that presents a different picture. This is because the initial costs faced by LDCs are not very high, unlike in the Central Africa sub-region. However, they have increased rapidly over the years. The average costs for exporting faced by the LDCs in the sub-region increased from USD 1 458 in 2005 to USD 2 561 in 2014, reflecting an increase of 75% (Figure 5.3). Similarly, the average costs for importing, which surged from USD 1 723 to USD 2 845 in the corresponding period, represent an increase of 65% (Figure 5.3). Just like the Central Africa sub-region, where the bulk of the cost increase was due to Chad, in the South Asia sub-region, Afghanistan accounts for the majority of costs as well as the increase in costs.

Another similarity is that the high average costs are driven by the presence of three landlocked countries in the South Asia sub-region, which tend to take longer time to import and export due to internal transportation-related weaknesses, as well as weaknesses in the transit providing countries. However, unlike in the Central Africa sub-region, costs of all the LDCs in the South Asia sub-region, including a relatively better performing Bangladesh, have increased.

**Figure 5.3 Costs of exporting and importing from LDCs in South Asia sub-region, 2005-2014**



Source: World Bank.

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## Landlocked status

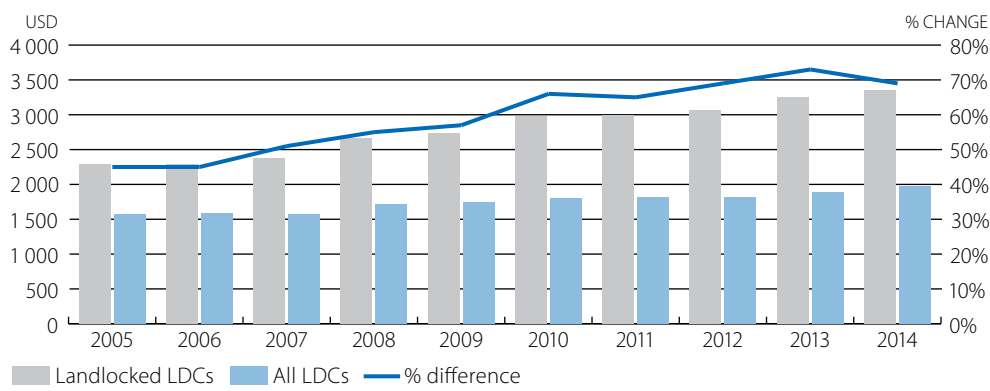
Trade costs tend to be much higher in landlocked countries compared to their coastal counterparts, and in particular the transit neighbours, for a variety of reasons. First, they need to rely on transit providing countries for international shipments – both for imports and exports. For example, as stated in the EIF supported DTIS of Malawi, which is dependent on transport corridors and ports in neighbouring countries for all of its trade, unreliable and unpredictable delivery times prevent producers from competing in regional and international markets (Malawi, 2014).

Second, typically, landlocked countries are isolated from major markets and have small economies, limited natural resources, weak institutions and a history of conflict (World Bank, 2010). Most of them fall into the bottom quintile of the Human Development Index. Third, although there has been some improvement in the domestic transportation infrastructure in the landlocked LDCs, they tend to have the lowest quality of infrastructure, which contributes to increased trade costs. For example, based on data available for a maximum of 29 LDCs, their average quality of road infrastructure on a scale of 1 (lowest) to 7 (best), was 2.37 in 2005. It increased to 3.1 in 2011 but decreased to 3.06 in 2012, only to rise marginally to 3.08 in 2013 (World Economic Forum, 2014).

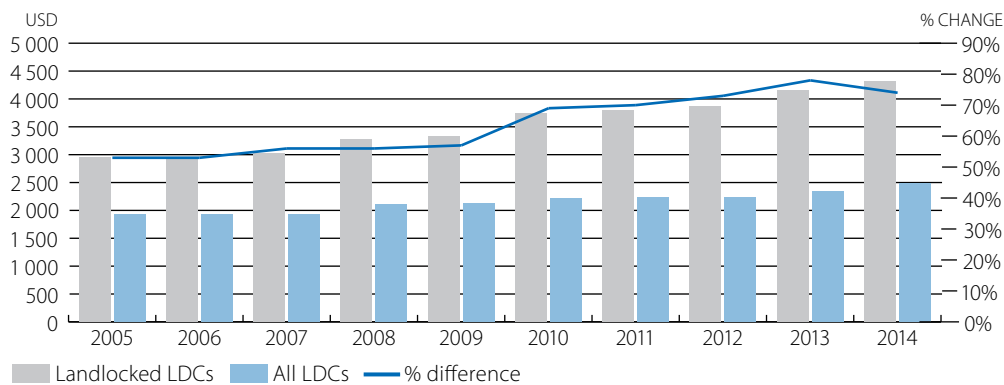
Moreover, a recent report published jointly by the World Bank and UN OHRLLS (2014) shows that LLDCs generally face much higher trade costs compared to transit coastal countries. Even among LDCs, landlocked countries tend to incur higher costs for exporting as well as importing, compared to their coastal counterparts. Figure 5.4 not only shows the higher cost incurred by landlocked LDCs compared to coastal LDCs but also the evolution of costs over the past decade. The left axis represents the export costs per twenty-foot equivalent unit container for landlocked LDCs and coastal LDCs and the right axis shows higher costs incurred by the latter in relation to the former in terms of percentage. As shown in Figure 5.4, landlocked countries suffered from higher export costs in the beginning, and their costs are rising rapidly compared to their coastal counterparts: there was a difference of 96% in 2005, increasing to 168% in the matter of a decade. It is worth noting while the export costs of landlocked LDCs increased by 46% between 2005 and 2014, coastal countries' export costs increased only by 7% during the corresponding period.

**Figure 5.4 Export and import costs of landlocked LDCs vis-à-vis coastal LDCs, 2005-2014**

#### Export costs



#### Import costs



Source: World Bank.

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Import costs, as shown in Figure 5.4, further expose the precarious situation of the landlocked LDCs compared to their coastal counterparts. Import costs for landlocked were much higher to begin with, and the cost difference between the two groups was 120% in 2005. This figure increased to 180% in 2014. As with the variation between export costs in the two different periods, the import costs increased by exactly 46% in the case of LDCs between 2005 and 2014, whereas the cost increase in the case of coastal countries was limited to 12%. Even within the same geographical sub-region, the cost for coastal countries is much lower compared to that of landlocked countries, as seen from Figure 5.2 as well as Figure 5.3.



There are a number of reasons that explain exceptionally high trade costs incurred by landlocked LDCs. First, a feature that is endemic to landlocked LDCs is that these are among the poorest of the poor countries in the world, with low human development indicators, as noted above. Therefore, it is only natural that resource constraints – financial, human and technological – act as the major barrier to upgrading infrastructure, where they tend to be the weakest. This can be one of the reasons why trade costs tend to inversely correlate with the level of income (World Bank and UN OHRLLS, 2014).

Second, the death of distance postulation appears highly exaggerated if we look at the situation of landlocked LDCs, not least because their export as well as import consignments have to travel on an average between 1 112 km and 1 494 km to and from the nearest port (World Bank and UN OHRLLS, 2014). While a part of these distances falls within their own territory, over which they have some control, a large majority of the distance lies within the territory of their transit neighbour(s), over which they have no influence.

Third, related to the second factor discussed above, transit neighbours of most landlocked countries themselves are not among the countries with the most efficient road and port infrastructure, which makes the transit process extremely burdensome and time consuming. They might be marginally less bureaucratic than their LDC counterparts, but are more bureaucratic than the global average. Some of their ports are congested by their own freight traffic, let alone providing the opportunity of seamless movement for the freight of the neighbouring landlocked countries. The DTIS of Bhutan, a country that is dependent on transit traffic through India for access to sea and third country markets, provides testimony to this predicament. Bhutan, which relies on the Port of Kolkata for the transit of its seaborne trade, finds its trade performance hampered by operational delays in the port, a lengthy clearance procedure and frequent strikes en route (Bhutan, 2012).

Similarly, the 2014 DTIS of Malawi documents that unreliable and unpredictable delivery times prevent producers from competing in regional and international markets. The 2012 Burundi DTIS highlights customs delays and high costs in the ports of Dar es Salaam (Tanzania) and Mombasa (Kenya), through which Burundi trades. This is reflected in transport and logistics costs that reach approximately 40% of export prices of agricultural products in Burundi, according to some estimates. The peace and security situation of the transit neighbours also affects transit time and cost, as posited by Faye et al. (2004). This is highlighted in Burkina Faso's 2007 DTIS, where it shows that unrest in Côte d'Ivoire and the disruption of the principal corridor to the coast resulted in increased trade costs.

Fourth, the existing governance and institutional arrangements of the road transport sector in most landlocked countries, where oligopoly is the predominant market structure, provides the breeding ground for cartel and anti-competitive practices to thrive. While this leads to supernormal profits for the truck operators, traders are obliged to pay more than what they would pay in a competitive market structure (Teravaninthorn and Raballand, 2009). The DTIS of Burkina Faso presents this predicament in a slightly different manner by highlighting the fact that transport companies in the country are chosen because they are next in line, not because they perform. Moreover, the air transportation sector, which seems to provide a more efficient, albeit costly, alternative to surface transportation, is also heavily protected in some landlocked countries. This is because, as Borchert et al. (2012) found, the pay-offs from protection for well-organised vested interests are likely to be higher in these countries as these countries tend to have weaker checks on policy makers' tendency to favour vested interests at the expense of public welfare. This results in a serious lack of competition in the transportation sector and the unwillingness of policy makers to liberalise it due to political economy considerations.

Fifth, high transit overheads, including superfluous services and bribes, affect a range of landlocked LDCs, which must rely on the regulatory and administrative structure and practices of their transit neighbour. Burdensome paper requirements, clearance procedures and loading and unloading can be extremely time and resource consuming for traders from landlocked countries. In order to avoid this cost, most of them hire clearing and forwarding agents, which are experienced in transit operations at a relatively higher costs (Snow et al., 2003). Although bribery and corruption is not endemic to transit providing countries, complicated and opaque procedures at the border, including documentary requirements and numerous security checking points often result in a high level of bribery.

For example, in West Africa, as documented by Ben Barka (2012:6), bribes collected by various agencies, including customs, police, gendarmerie and other uniformed services, range from USD 3 to USD 23 per 100 km.. In the case of Burkina Faso, although Snow et al. (2003) do not provide any numbers, they argue that rigorous police checkpoints in the trade routes not only cost time, but often money in the form of bribes. The frequent road-side demand for bribe payment was also highlighted in the earlier version of Burkina Faso's DTIS completed in 2007.

## Commodity dependence

According to UNCTAD's classification, more than half of the LDCs (27 out of 48) are dependent on commodities (agriculture, fuels and minerals) for their exports. Since commodities are bulky products, overall trade costs for their exports tend to be higher than light manufacturing. In order to calculate the trade costs, we rely again on the export-cost data derived from the Doing Business Report for the period 2005 to 2014. Since most of the commodities exporting countries do not import raw materials and export commodities in more or less raw form, we decided to not include costs for importing.

In order to identify commodity exporting countries, we follow UNCTAD's (2010) classification, which divides the countries into various categories of commodity exporters, as presented in Table 5.1. Of the 25 countries included in the list, data for two countries, namely Somalia and Tuvalu, were not available. Therefore, the analysis below is based on the data of the following countries.

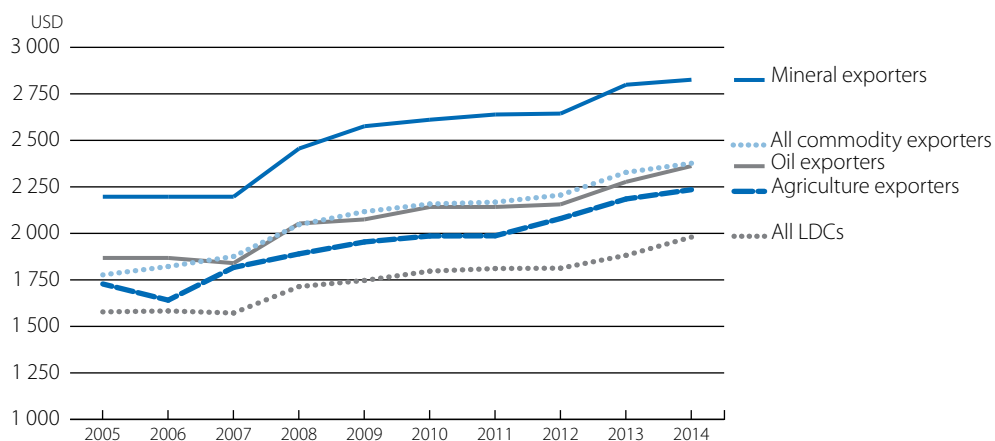
**TABLE 5.1 Commodity-exporting LDCs**

<b>Agricultural exporters</b>	Afghanistan, Benin, Burkina Faso, Guinea-Bissau, Kiribati, Liberia, Malawi, Solomon Islands and Uganda
<b>Mineral exporters</b>	Burundi, Central African Republic, Democratic Republic of the Congo, Guinea, Mali, Mauritania, Mozambique, Niger, Sierra Leone and Zambia
<b>Oil (fuel) exporters</b>	Angola, Chad, Equatorial Guinea, Sudan, Timor-Leste and Yemen

Source: UNCTAD (2010).

Figure 5.5 depicts the cost of exporting incurred by all three categories of commodity exporting LDCs, as well as all the countries included in Table 5.1, for which data are available. For the purpose of benchmarking, the average for all LDCs is also included. As shown in the figure, commodity exporting LDCs in general face higher export costs compared to the LDC average, and mineral exporting LDCs face the highest export costs. This is followed by oil exporting LDCs and agriculture exporting LDCs.

**Figure 5.5. Cost of exporting for commodity-exporting LDCs, 2005-14**



Source: Based on the World Bank.

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Since commodities are by nature bulky products no matter what countries export, there may not be any specific reason for mineral exports costing more than costs of exporting other commodities. One explanation, however, for the higher trade cost faced by mineral exporters compared to oil exporters is that among the exporters of oil, all but Chad happen to be coastal countries, which incur lower export costs. This seems to suggest that the higher trade costs for mineral exporting countries are due to their being landlocked rather than anything else. However, further research is required to establish that this is actually the case.

### Fragile situation

LDCs are also amongst the most fragile countries, either facing ongoing political unrest, armed revolt and/or the threat of terrorism, which can impose trade costs that are not trivial. These can be due to damage caused to vital infrastructure, such as roads, bridges, telecommunications or ports, additional security checks that are required to contain potential damages, threats of strikes and shutdown of trade routes and higher insurance premiums due to the above mentioned threats. For example, the 2006 Sierra Leone DTIS takes account of the damage caused by civil conflict to much of the country's infrastructure and trade related services.

Although the impact of conflict on trade costs is a relatively under-researched area, Blomberg and Hess (2006), who conducted an empirical investigation with the annual observation of a panel dataset of 177 countries between 1968 and 1999, found that for a given year, the presence of terrorism coupled with internal and external conflict is equivalent to a nearly 30% tariff on trade. This is much larger than many other trade costs discussed so far.

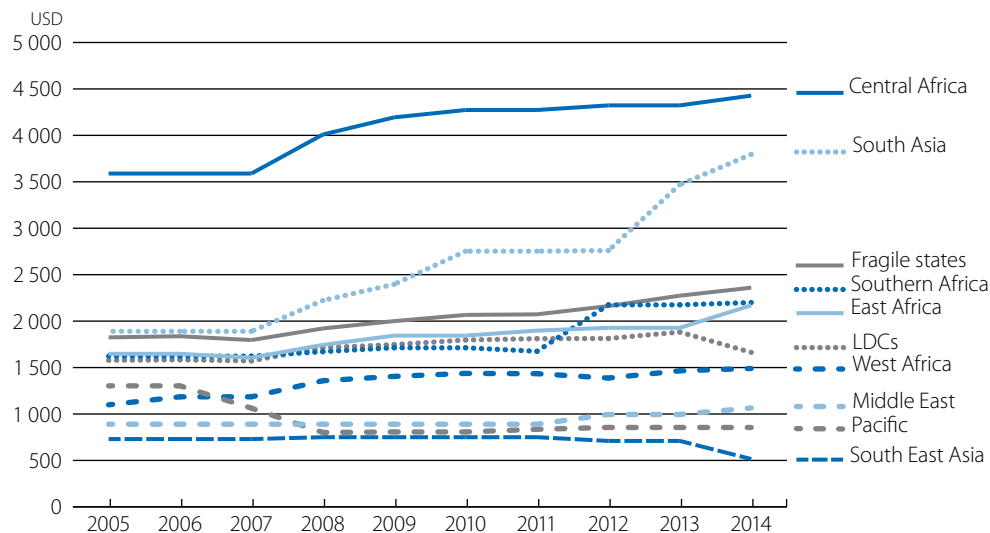
No less than 23 out of 48 LDCs are on the World Bank 2014 Harmonized List of Fragile Situations. Some are still reeling under civil strife, while others are in the post-conflict stage. Three countries on the World Bank list (Somalia, South Sudan and Tuvalu) were not included in the Doing Business Report, consequently, they could not be included for comparative analysis. The final list of countries was grouped into the six sub-regions as presented in Table 5.2.

**TABLE 5.2 List of fragile states and their sub-regions, 2014**

Sub-region	Country
<b>Asia</b>	Afghanistan, Myanmar, Nepal, Timor-Leste and Yemen
<b>Pacific</b>	Kiribati and Solomon Islands
<b>East Africa</b>	Burundi, Comoros, Eritrea and Sudan
<b>West Africa</b>	Liberia, Mali, Sierra Leone and Togo
<b>Central Africa</b>	Central African Republic and Democratic Republic of the Congo
<b>Southern Africa</b>	Malawi

Source: World Bank (2014).

Based on the costs for exporting obtained from the Doing Business Report, we take the costs per sub-region as well as overall costs incurred for exports by fragile LDCs. We also include the LDC average figure for comparison. As it turns out, the fragile states tend to pay anywhere between 29% and 34% more than what is paid by all the LDCs for exporting their goods, and the costs have been generally rising over the past few years, except for the Pacific sub-region (Figure 5.6). According to the figure, Central Africa, South Asia, East Africa and the Southern Africa sub-region pay more costs to export than the overall LDC average, as well as the average for all the fragile states. However, fragile states in the South East Asia sub-region, followed by the Pacific, the Middle East and West Africa, face lower trade costs as compared to the averages for the LDCs and the fragile states.

**Figure 5.6 Costs of exports in fragile states, their sub-regions and LDCs, 2005-14**

Source: World Bank.

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Although the above findings tend to suggest trade costs are higher in fragile states, lending credence to the findings of Blomberg and Hess (2006), more analysis is required to see if the cost differences are actually not driven by the countries being landlocked. This is because if we take out landlocked countries from all the sub-regions, export costs are actually lower than the overall LDC average for all sub-regions, except for Central Africa, which is an outlier in any case.

### The changing structure of trade costs in the last decade

There has been some reduction in trade costs over the past ten years, although they are far limited compared to other countries, as pointed out by Arvis et al. (2013). Based on the review of a dozen of case stories submitted by the LDCs to the Third Global Review of Aid for Trade and an analysis of data published in the Doing Business Indicators (between 2007 and 2013) and the LPI (between 2007 and 2012), ITC (2013a) infers that LDCs, to their credit, have taken initiatives to address policy-induced barriers to reduce trade costs. It further shows that between these periods, the number of days needed for exports fell from 40 to 33 and the logistics performance indicators for the LDCs as a whole improved from 2.2 to close to 2.4. However, there were variations between the Asian and Pacific Islands LDCs and African LDCs and Haiti (ibid.).

Individual country performance on these fronts indicates that some LDCs are making considerably more progress as compared to others. The evolution of the indices (rather than the ranking, which is also affected by the number of countries chosen for the indicator) for the top ten LDC performers in 2014 shows that there has been some progress, although they have a long way to go in terms of improving their LPI (Table 5.3). The fact that the best performing LDC, Malawi, features only 73 in a list of 160 countries included in 2014, shows that LDCs will have to undertake significant and far reaching reforms to catch up with the rest of the world. It is also worth noting that out of the bottom ten countries, seven are LDCs.

It appears from the table that Rwanda, which achieved a change of 0.98 points in the Index, although starting from a low base, is a shining example worth highlighting. Also starting with a relatively low base, LDCs such as Malawi, Burkina Faso and Nepal, despite being landlocked, have also made significant progress in improving their LPIs. Such a jump in score is not possible in the case of developed countries, which already have a relatively higher score and are close to perfection. For example, Germany, the best performer in 2014, made a marginal improvement from 4.10 to 4.12 in the corresponding period.

**TABLE 5.3 Changes in the Logistics Performance Index for the top ten performing LDCs, 2007-14**

Country	2007	2010	2012	2014	Change
Malawi	2.42	-	2.81	2.81	0.39
Rwanda	1.77	2.04	2.27	2.76	0.98
Cambodia	2.50	2.37	2.56	2.74	0.24
São Tomé and Príncipe	-	-	-	2.73	-
Burkina Faso	2.24	2.23	2.32	2.64	0.40
Senegal	2.37	2.86	2.49	2.62	0.26
Liberia	2.31	2.38	2.45	2.62	0.31
Ethiopia	2.33	2.41	2.24	2.59	0.27
Nepal	2.14	2.20	2.04	2.59	0.45
Solomon Island	2.08	2.31	2.41	2.59	0.51

Source: World Bank.

Based on the four categories of LDCs discussed in Section 2 above, if we look at the evolution of cost structure over the period of the last decade, it is clear that costs have been rising rapidly in the Central Africa region, followed by South Asia. As discussed, higher costs in these regions over the past decade can be ascribed to the presence of a large number of landlocked countries, including outliers like Chad and Afghanistan, which face higher initial costs that further increased in the past decade. That being landlocked adds to the trading costs is also proven by the fact it is this factor that contributes predominantly, if not exclusively, to the high initial as well as increased costs in mineral exporting LDCs (Figure 5.5) and fragile states (Figure 5.6).

Trade cost information gathered from 20 DTIS and DTISUs from across different sub-regions, shows that trade costs are not only changing in magnitude but also in nature. Table 5.4 provides the details of major elements of trade costs in the earlier versions of DTISs completed between 2002 and 2008 and the latest versions, including DTISUs completed between 2012 and 2014. However, problems such as transit, which are outside the control of the landlocked countries, are highlighted as challenges in both versions of DTISs in some countries. Another set of problems, which seems to persist despite its diagnosis in the previous versions of DTISs, is corruption, lack of competition in the transportation sector and complicated, non-transparent and lengthy procedures at the border.

### LDCs' PRIORITIES IN ADDRESSING TRADE COSTS: THEN AND NOW

As indicated in the different LDCs' DTISs, the nature of trade costs in LDCs over the past decade has varied to some extent, but there has been no drastic change in their orientation. In Table 5.5, on the basis of DTISs and DTISUs of 11 countries reviewed for the purpose of this chapter, we compile the priorities of the LDCs in relation to lowering trade costs for an earlier period (2002-08) and compare them to the recent period (2013-14).

This review shows that at the generic level a reduction in transportation costs, an improvement in logistics performance and enhanced border management were recurring themes during both periods. However, the major priority areas in transportation and logistics in the earlier versions of DTISs prepared between 2002 and 2008 include the issues of quality of road construction, allocating more resources for transport infrastructure, promoting competition in the transportation sector, controlling bribery and corruption and better handling and management of regional trade and transit traffic. Similarly, the major priorities identified in this period in border management include putting into place improved systems through enhanced transparency of various processes, implementing appropriate mechanisms for customs valuation, facilitating digital exchanges and enhancing the capacity of the border management agencies. Moreover, reducing duplications and achieving the harmonisation and simplification of tariffs and non-tariff barriers and increasing transparency were also priorities.

**TABLE 5.4 Evolution of trade costs in LDCs based on DTIs, 2002-14**

Country	Major elements of trade costs (2002-08)	Major elements of trade costs (2012-14)
<b>Bhutan</b>	N/A	Transit problems; fragmented administrative processes; absence of telecommunications and data connection between clearance and inspection locations; and limited sharing of information between agencies
<b>Burkina Faso</b>	Transit; corruption; informal nature of trucking business; demand for dispensable fees imposed on trucking; and duplication of forms	Transit challenges; informal checkpoints and roadblocks; inadequate transport infrastructure; inefficient customs practices; corruption; trucking firm monopolies; and poor quality service in three transit corridors
<b>Burundi</b>	Absence of clear rules; limited capacity, corruption and inefficiencies in customs administration; poor condition and unreliable physical infrastructure; high transportation costs; and incompatibility of customs clearance procedures from intervening institutions	Poor infrastructure, including road network; inadequate computerization; underdeveloped logistics services sector; long customs delays; corruption; and high transportation costs
<b>Cambodia</b>	Opaqueness and limited capacity of customs administration; and high transportation costs.	Poor implementation of cross border procedures; checkpoints and informal payments at main trade corridors; monopolies of trucking firm; and insufficient logistics to support agricultural exports
<b>Haiti</b>	N/A	Reduced capacity of the international port due to the earthquake; absence of a single window to facilitate the issuance of registrations, permits, and certifications; and lack of a co-ordinated mechanism between government agencies at the border
<b>Lao PDR</b>	Underdeveloped and limited logistics industry, mostly operated by small, family run companies; time spent dealing with regulatory procedures; multiple steps involved in complying with trade regulations; weak and fragmented customs system; lack of infrastructure and capacity at border crossings; and administrative practices requiring applicants to stand in long queues or apply for formal appointments with the right officials	Complex trade procedures at the border requiring excessive documentation; lack of equipment and facilities to ensure the smooth and efficient administration of trade and customs procedures; informal fees at the border; small size of the local freight forwarding industry; poorly developed container transport network; underdeveloped river port facilities not suited to handle containerised cargos; and some cross-border points lacking basic facilities, such as working weighbridges and permanent paving
<b>Malawi</b>	Outmoded customs procedures and management practices, including lack of data on processing times and on volume of declarations processed at various entry points; inefficient and inadequate transport system; lack of liberalised trucking routes and restrictions on competition from international haulers; outdated customs legislation inconsistent with international and regional agreements; ineffective transit computerised system; poor communications infrastructure; corruption; lack of technical expertise; and poor condition of road networks	Limited transparency in the preparation of trade policy and its implementation; outdated technical regulations and their application at the borders; complicated border and transit procedures; limited competition in the transport sector; traditional fragmented markets of customs brokers; and cabotage restrictions for domestic road transport

**TABLE 5.4 Evolution of trade costs in LDCs based on DTIs, 2002-14**

Country	Major elements of trade costs (2002-08)	Major elements of trade costs (2012-14)
<b>Senegal</b>	Complicated and lengthy import procedures; corruption; irregularities and lack of data on release procedures by customs officers; inadequate customs information system; customs officers inexperienced in modern valuation techniques; and inadequate administrative capacity to implement trade policy	Poor road network and infrastructure leading to high transportation costs; multiplicity of customs related platforms and procedures; and customs fraud
<b>Sierra Leone</b>	Underdeveloped logistics and transport sectors; inexperienced customs officials and managers; lack of transparency and inconsistent application of the customs valuation system; lack of infrastructure to implement the WTO Agreement on Customs Valuation; misuse of the customs role; lack of knowledge and skill in tariff classification; time consuming, costly and corrupt border clearance systems; limited clearing and forwarding companies and restricting legislation in place for clearing and freight forwarding activities to be carried out by national companies or individuals; and poor infrastructure coverage and quality (telecommunications and electrical power) due to the civil war	Poor infrastructure due to civil conflict; underdeveloped logistics services; increased transit time, particularly during the rainy season; lack of transparency in border post operations; arbitrary roadblocks/checkpoints and unlawful collections on transport routes; ineffective cross border trucking services and truck congestion and extensive delays at border posts due to a high level of bureaucracy; and high transportation costs
<b>Sudan</b>	Fragmented transport infrastructure due to internal conflict and geography; absence of logistics service providers; relatively disorganised clearing and forwarding industry; limited number of container handling facilities; inefficient rail services and infrastructure; lack of road maintenance; frequent delays in the port; customs bonds for transit goods required by the East African countries; and lack of a formal articulated plan for the modernisation of the customs general administration	Inefficient border agencies, including requirement to submit same information to multiple agencies; high transportation costs; poor co-ordination with neighbour countries to form regional corridors; and poor registration system for trucks
<b>Zambia</b>	Long clearance times; inadequate information sharing between all the border control agencies; unnecessary complicated procedures requiring redundant information, checking and physical inspection; inadequate use of risk assessment to reduce the proportion of goods being inspected; corruption; onerous transit trade procedures; and bad road network, as well as the failure to prevent systematic overloading of trucks	Non-transparent and unpredictable non tariff regulatory measures; excessive documentation requirements; lengthy administrative procedures; and rent seeking tendency amongst border agencies

Source: Author's compilation based on DTIS and DTISUs.

The relatively newer versions of the DTIS (those finalised in 2013 and 2014, with most of them being updates) also identify similar priorities at the general level. However, within the transport and logistics domains, issues such as the management of transit corridors, the implementation of cross border transport arrangements for regional and transit traffic and improvement in port infrastructure feature prominently. In terms of improved border management, major priorities include a better management of infrastructure, the use of information technology – including the introduction of electronic clearance systems – the professionalisation of customs administration, the reduction of duplication, the increase in transparency of procedures and the fight against corruption. Some of the new priorities that emerge from the latest version of DTISs for the reduction in trade costs are addressing cross cutting barriers for infrastructure development, designing transport policies and regulations to strengthen market structures in the transport as well as the logistics sectors, modernising the regulatory frameworks and improving the collaboration among border agencies and with the private sector. This is more in line with the tendency among many developing countries towards focusing on the “software” of trade cost dynamics alongside the “hardware”.

### Reforms undertaken

A closer look at reform measures undertaken by LDCs over the past decade in the indicators of trading across borders of the Doing Business Report shows that LDCs are undertaking far reaching and often sweeping reforms to improve their indicators as well as reduce costs. Our count shows that 21 LDCs undertook some reform measures to improve their ranking in cost of trading across border between 2006 and 2014. Some LDCs have undertaken many more reform measures than the global average number of reforms in this area, which is close to two. These LDCs are Benin (5), Madagascar (4), Rwanda (6) and Uganda (4) (World Bank, 2015a). A review of DTISs and other published documents reveals that reforms have indeed been far reaching. Select examples are as discussed below.

Burkina Faso has considerably improved the effectiveness of transport and logistics on the Tema Ouagadougou Corridor in the period from 2008 to 2012, and due to an increased transparency, informal payments dropped by more than 50%. In Cambodia, the simplification of licensing procedures, the elimination of unnecessary steps and documents and the introduction of time limits for the issuance of licences reduced trade costs for processed agricultural products by 30% by December 2014. Following the simplification of export procedures, the cost to obtain export licenses for milled rice was reduced by 28% – generating about USD 700 000 annually in savings for rice exporters (World Bank, 2015a). Similarly, the number of days required for the clearance of containers at the border was halved through the computerisation of customs operations using the Automated System for Customs Data (ASYCUDA) and bringing the customs system into compliance with WTO obligations. As a result, the time to export decreased from 37 days in 2007 to 22 days in 2012, and the time to import from 45 days in 2007 to 26 days in 2012. Awareness programmes on trade facilitation for customs officials, Camcontrol, port officials and the private sector have further contributed to increased productivity at Sihanoukville Port from 10 containers/hour to 30 containers/hour (EIF, 2014).

In Lao PDR, opening Lao transit trade to all Thai truckers on the Vientiane-Bangkok Corridor reduced logistics costs by 30% (UNOHRLLS 2014). The launching of a trade portal in 2012 contributed to increased transparency and helped reduce trade costs. As a result, the clearance times for goods by non customs agencies have reduced by 42%, from five days in 2009 to 2.9 days in 2012. More importantly, this idea is being replicated by the Malawi DTISU (2014). At the same time, Myanmar and Lesotho are trying to replicate this model. For Sudan and Cambodia, the national trade portal is part of the recommendations going forward.

The introduction of ASYCUDA in Haiti in 2008 helped to significantly improve the logistics performance of the country, which resulted in Haiti moving from 123 in 2007 to 98 in 2010 in the LPI. In Liberia, the automation of the national business registry by the Ministry of Trade with the support of the EIF drastically reduced the time it takes to register a company, allowing Liberia to move up the in World Bank’s Doing Business ranking from 167 in 2008 to 144 in 2014.



Malawi for its part decided in March 2013 to reduce the number of border agencies from 14 to 5, thereby significantly curtailing duplications and improving efficiency (Malawi DTISU, 2014). In Rwanda, TradeMark East Africa (TMEA) introduced, among other things, a one-stop electronic customs clearing system, thus cutting the time required to clear goods by 40%, or one full day, which brings Rwanda almost a day closer to the ports of Mombasa or Dar es Salaam. This has resulted in direct savings for businesses of around USD 8-17 million a year.

Sierra Leone rehabilitated 85 km of roads (76 km in Sierra Leone and 9 km in Guinea) along the Freetown-Conakry Highway and constructed a joint border post between 2009 and 2012 with funding from the European Union's in a bid to connect its closest neighbours along the Atlantic coastline. As a result of this infrastructure upgrade, transport costs and travelling time have been reduced by 30%, with trade volumes between Sierra Leone and Guinea expected to have increased significantly. Another major road project was the rehabilitation of 165 km of roads along the Masiaka-Bo Highway, which took place over five years from 2006. As a component of the Conakry-Freetown-Monrovia road, it also contributes to the regional connectivity of Sierra Leone (Sierra Leone DTISU, 2013).

The establishment of a one-stop border post at Chirundu on the border between Zambia and Zimbabwe, which uses a non invasive inspection scanner for pre-clearance, has led to a reduction in the average time spent by a truck at the border from seven to nine days to about three to four hours and an increase in the number of trucks passing through the border from an average of 1 800 to 2 000 per month in 2009 to 12 000 to 14 000 in 2012. These reforms resulted in average savings of about USD 20 million a month for the private sector. This is due to faster transit times since mid-2012 and an increase in trade tax collection at the Zambian side of Chirundu by more than 100% from an average of USD 10 million a month in 2009 to USD 20.3 million a month in 2012. Time saved at border, which is valued at USD 600 000 a day, further trickles down to transporters, brokers, traders, producers and consumers (TradeMark Southern Africa).

## DRIVERS OF CHANGE

Reducing trade costs is an agenda being pursued by all the countries regardless of their economic status; it is only that the focus has now shifted more towards host country barriers, border formalities and transport and logistics. The agenda for lowering trade costs is driven by the interplay of several factors. In the context of LDCs, based on the factual descriptions as well as the analysis presented above, the following can be considered as the major driver of change:

### Evolving dynamics in global trade

Pressures emanating from international trends, such as GRVCs, have also contributed to a change in perception as the countries now realise that they need to focus on the seamless movement of goods – both for exports as well as imports. Although limited in number, this issue came out clearly from the LDCs' responses to the questionnaire administered by the WTO for the Fifth Global Review of Aid for Trade. Countries as varied as Afghanistan, Bangladesh, Bhutan, Cambodia, the Democratic Republic of the Congo, Mali, Sierra Leone and Uganda thought that trade costs were important to access imported inputs. Some of these countries did emphasise the fact that increased trade costs on imported inputs eventually tax their exports.

Another path-breaking development that could have a significant impact is the WTO Trade Facilitation Agreement (TFA) agreed during the Bali Ministerial Conference of the WTO, which was eventually adopted in November 2014. A number of initiatives such as the needs assessment exercise and the creation of national level co-ordination mechanisms have sprung up in LDCs, with some of them opting to utilise the EIF National Steering Committee (NSC) as the National Trade Facilitation Committee. Although LDCs can select themselves what they would like to notify as Category C measures, the TFA presents a landmark opportunity for the LDCs to initiate beneficial reform measures, which they would have undertaken anyway (see Chapter 4 for further detail). Moreover, availability of various financing facilities for the implementation of the Agreement means that LDCs are more likely to make use of such opportunities for this purpose.

**TABLE 5.5. Evolution of LDCs' priorities in relation to reducing trade costs, 2002-14**

Country	Major priorities identified (2002-08)	Major priorities identified (2013-14)
<b>Bhutan</b>	N/A	Better management of border infrastructure at the major border points; increasingly using information technology for customs procedures; and building transit corridors
<b>Burkina Faso</b>	Instituting mechanisms for containing frequent road-side demands for bribes and unnecessary though legal fees imposed on trucking; modernising sealed container transport; and introducing competition in the transport sector	Reducing transport costs; creating a dynamic, equitable and professionalised customs administration; developing a common government and private sector vision to fight corruption; simplification and computerisation of customs procedures and operations; and increasing the availability of documents and international customs manuals
<b>Burundi</b>	Preparing an action plan on regional transit issues; designing a programme of action on customs tariffs and valuation; implementing a customs reform programme; finalising an accord on trade facilitation; and facilitating the digital exchange of data between agencies involved in trade facilitation	Improving logistics, customs modernisation and corridor management; reducing connectivity gaps in lagging regions; upgrading storage facilities; and creating a charter for cross-border traders to remove constraints faced by small traders and facilitate regional trade
<b>Cambodia</b>	Reducing the degree of unofficial interventions and increasing transparency to enhance customs efficiency; reducing institutional duplication; strengthening capacity in customs administration; and reducing the cost of transport by improving quality and reducing unofficial fees and charges	Simplifying and automating trade procedures and processes to decrease clearance costs and time; implementing customs practices conforming to WTO Customs Valuation requirements; increasing the transparency of customs tariffs and trade regulations; improving cross border procedures to support a full integration into the ASEAN; and eliminating checkpoints (and informal payments) along the main trade corridors
<b>Haiti</b>	N/A	Reconstructing the Port-au-Prince port and improving and maintaining the infrastructure
<b>Lao PDR</b>	Developing regulations to implement the new customs law; reforming the national customs administration; simplifying, modernising and automating border clearance procedures and data processing; strengthening and expanding anti smuggling programmes; licensing of customs brokers; piloting the gold card programme to expedite clearance procedures for approved traders; improving the single window operations in provinces; trade logistics development; developing standards/technical regulations; facilitating cross border trade; and simplifying or eliminating export/import licensing and indicative plans	Strengthening the capabilities of the National Trade Facilitation Secretariat and Trade Facilitation Division; mainstreaming trade facilitation across relevant line ministries and departments; continuing to develop additional functionality of the Lao Trade Portal to reduce transaction costs related to import and export; designing and implementing the national single window; exploring opportunities to reduce transport costs; developing private sector capacity to trade efficiently in compliance with rules and regulations; adopting and implementing the revised customs law to be consistent with WTO principles; and automating customs clearance procedures at major checkpoints
<b>Malawi</b>	Enforcing compliance mechanisms for harmonised transit fees; streamlining customs procedures and documentation; promoting infrastructure development; professionalising immigration personnel; establishing a standardised customs payment system; harmonising the national customs administration with regional systems and procedures; and more effectively implementing the WTO Customs Valuation Agreement	Reducing the processing fee for use of the Simplified Trade Regime (STR); implementing the Charter for Cross-Border Trade and identifying specific constraints impacting women traders; amending legislation to empower the core border agencies to perform cross border functions; introducing a national trade portal that contains all legally binding information on trade procedures; and identifying selected internal routes and reducing restrictions on foreign truckers delivering/collecting goods in Malawi

**TABLE 5.5. Evolution of LDCs' priorities in relation to reducing trade costs, 2002-14**

Country	Major priorities identified (2002-08)	Major priorities identified (2013-14)
<b>Senegal</b>	Enhancing efficient management of import procedures; improving customs valuation procedures; and improving management of duty-free imports for exporter schemes	Improving and maintaining the road network and infrastructure; reducing multiplicity of customs related platforms and procedures; and addressing customs fraud
<b>Sierra Leone</b>	Reducing clearance costs; increasing transparency; sensitising traders about applicable customs tariff rates and customs procedures; improving valuation procedures; building capacity of customs services; reducing cross border smuggling; upgrading transport infrastructure; encouraging private participation in building and operating ports and terminals and handling and storage facilities; improving coordination between various ministries and related agencies; training private sector transport actors; strengthening public-private dialogue in transport and trade facilitation, transit and border crossings; and developing cheap transport alternatives	Eliminating infrastructure bottlenecks and improving intermodal connectivity; improving the quality and operating environment of core logistics services to build efficient supply chains; building on progress made in customs and border management to boost revenue collection and efficiency in cargo clearing and transit; and introducing measures to better monitor cross-border trade and address challenges of informal traders to help bring them in to the formal sector
<b>Sudan</b>	Improving trade logistics services; reducing bottlenecks at Port Sudan; streamlining national customs procedures and harmonising them with WTO rules; simplifying and harmonising taxes, fees, and charges; eliminating measures that restrict exports; and introducing more uniformity and predictability into trade policies	Adopting improved mechanisms to ensure integrated border management; improving the existing one-stop service and continuing implementing the national single window; introducing a national trade portal for all legally binding information on trade procedures; revising requirements for obtaining a clearing agent licence; allowing self-clearing by importers; revising regulations for trucking and forwarding business; expediting the implementation of the agreed upon business plan for the rail network on the Port Sudan-Khartoum Corridor; building a bypass to Soba Dry Port or developing a new dry port north of Khartoum; and developing a comprehensive logistics strategy to implement the national transport master plan
<b>Zambia</b>	Upgrading equipment and infrastructure of the Zambia Revenue Authority; integrating border agencies; reducing border clearance times while ensuring integrity and increased compliance; implementing trade facilitation agreements; improving regulatory framework for transport/transit logistics/efficiency/costs; reducing transit costs; accelerating investment in new transport infrastructure; and augmenting capacity in the transport industry	Developing a coherent logistics approach with the definition of a core strategic logistics network; linking a strategy to trade facilitation needs assessment as part of the WTO Trade Facilitation Agreement; designating an agency with overall responsibility for border co-ordination and management; prioritising the quality of service to major shippers and offering incentives for co-operation between local and cross-border railways; developing a clear logistics plans to integrate into potential regional supply chains; and implementing the charter for cross border traders

Source: Authors' compilation based on DTISs and DTISUs.

## Rise of regional integration

Regional integration is burgeoning, and the pace is likely to increase regardless of the development taking place within the multilateral trading system. All LDCs are now party to regional trade agreements, and some of them have realised that regional integration can be a cushion against vulnerability associated with excessive dependence on countries outside of the region for their trade relations. At the same time, landlocked countries find it more convenient and cost effective to trade with their immediate neighbours where transit issues are not a problem.

Moreover, some of the reduction in trade costs can be more conveniently and economically achieved at the regional level rather than at the international level. Considerable evidence shows that trade could be expanded within existing regional integration schemes by relatively less costly and straightforward reforms, such as simplifying and reducing documentation requirements across borders, enhancing transparency, expediting the release of goods from customs, standardising trade-related regulations and improving border agency co-ordination within and among members of a common regional trading arrangement (Milner, Morrissey and Zgou, 2008). This issue features prominently in some of the new versions of DTISs. Two noteworthy examples of regional endeavours to reduce costs are Sierra Leone and Zambia, which show that regionally-induced reform measures can have a multiplier effect on lowering trade costs.

## Analytical work

The past decade has witnessed a vast amount of analytical work that underpins the DTIS process, national trade policies and national export strategies, as well as various reports produced by multilateral institutions, regional economic commissions and not for profit foundations. Trade facilitation, which is a major constituent part of the trade cost universe, is included as a dedicated chapter or as a cross cutting issue in the new generation of DTISUs (e.g. Burkina Faso DTISU 2014, Burundi DTISU 2012, Cambodia DTISU 2014, Haiti DTIS 2013, etc.) or national export strategies (for example, the national export strategies of Gambia and of Malawi include trade facilitation as an important agenda).

These works have also contributed to the publication of the global ranking of trade costs as reflected in the World Bank's Doing Business Report and the LPI and the World Economic Forum's Global Competitiveness Report and Enabling Trade Report. These rankings have become powerful tools not only because of the carrot they offer to reformers but also the stick they provide to countries that maintain the status quo or regress. Despite their methodological limitations, as accepted measurements these rankings exert considerable pressures on the countries to reform, because as the organisation theorist Mason Haire once suggested, "What gets measured, gets done". Moreover, potential traders, lead firms in GVCs and foreign investors who wish to engage in business transactions with the countries included in these global rankings use this type of information to make their business decisions (see Kelley and Simmons [2015], for example), which provides a further impetus for reforms.

## Changing priorities and policies of governments

Trade is being increasingly perceived as a key instrument for achieving development objectives, including inclusive economic growth and poverty reduction in the LDCs. Given relatively strong government adherence to this agenda within the LDCs, countries are keen to take the necessary measures to expand and diversify trade, which offers a significant developmental spin off. It must be noted that one of the major objectives of the EIF is to ensure trade mainstreaming into the national development strategies as well as sectoral programmes and policies. For example, based on the EIF Annual Progress Report 2014, 82% of EIF countries have reached a "satisfactory" level of trade mainstreaming into their national development plans compared with 32 per cent in 2010, and 93% of EIF countries implementing "productive capacity building" projects have at least one productive sector that prioritises trade in its strategy (EIF, forthcoming).

Based on the limited response received from the LDCs on the WTO's Fifth Global Review of Aid for Trade questionnaire, one can observe the inclusion of this agenda in various policy documents, such as the DTISs of the governments in Bangladesh, Cambodia, Chad, the Democratic Republic of the Congo, Mali, Sierra Leone and Uganda.

### **Role of the private sector**

The private sector in many LDCs is becoming increasingly aware of the significance of their involvement in issues such as private sector development, improving the business climate, trade policy and aid for trade. In some countries, various bilateral donors as well as multilateral agencies have been supporting private sector development and business climate projects, of which trade policy is a major constituent part. The private sector is represented in all the working groups that have been constituted and the public private dialogue fora that have been organised, which have helped enhance the private sector's capacities as well as expertise. Similarly, representation of the private sector in the National Steering Committee– the apex policy making body within the National Implementation Arrangements of the EIF – has been ensured in all the LDCs. This has contributed to building an active involvement of the private sector in the key decision making processes. Because private sector entities pay the price of higher trade costs, they tend to exert pressure on their governments to identify bottlenecks and undertake reforms aimed at reducing trade costs, as well as contribute to the reform process.

The success rate of programmes with the involvement of the private sector tends to be high. For example, in Bangladesh, the Dhaka Custom House Automation Project is a joint initiative of the Dhaka Chamber of Commerce and Industry and of DataSoft Management Services, which has brought together several public and private sector entities dealing with various trade-related services. It is anticipated that the implementation of the project may ensure doubling revenue within two years, reducing the cost of doing business by at least 70% and lowering customs processing time by 80%. It is also envisaged that the project will help to ensure the precise monitoring of international and domestic prices, enhance transparency, provide a level playing field for business and achieve better risk management (see Datasoft website for further details).

Similarly, the success of the one-stop border post established at Chirundu on the border of Zambia and Zimbabwe, as discussed above, is attributed to the involvement of the private sector right from the beginning of the initiative on both sides of the border. Likewise, in Bhutan, joint efforts by the public and the private sectors, including better cross-border co-ordination, is recommended by its DTIS in order to remove regulatory and other constraints and to facilitate trade and the movement of cargo along the Phuentsholing–Kolkata road Corridor (Bhutan DTIS, 2012).

### **Global development discourse and initiatives**

Recent development discourse, particularly after the Millennium Development Goals (MDGs), has recognised the role of trade in promoting sustainable and inclusive economic growth and development. This is reflected in the LDCs' specific action plans, such as the Brussels Programme of Action, as well as the Istanbul Programme of Action (IPOA). These are further supported by the inclusion of trade as a priority issue in the post-2015 Sustainable Development Goals (SDGs). Increased focus on trade at the political level has not only influenced the priority setting of the governments as noted in 4.2.4 above, but also led to the creation of various initiatives aimed at addressing the challenges facing developing countries and LDCs in their pursuit of leveraging trade for economic development and poverty reduction.

This has led to the launch of various global initiatives and programmes aimed at building the trade capacity of developing countries in general and of LDCs in particular in the past decade. These include the aid-for-trade initiative of the WTO, the Standards and Trade Development Facility, the Trade Facilitation Facility and the EIF. The reduction in trade costs is one of the objectives of these initiatives, although they are not always explicitly mentioned.

Various regional initiatives, such as the TMEA (a multi-donor initiative which aims for an enhanced trade environment and has specific and measurable targets) and the Trade Hub Projects (A USAID-funded initiative that targets customs reforms and modernisation and trade facilitation, WTO compliance and trade costs reduction) have supplemented these global efforts aimed at reducing trade costs. Moreover, there are several other initiatives at the bilateral level – both traditional and with South-South donors. The existence of these initiatives has provided an incentive for the governments to undertake reforms to lower trade costs.

### **AID-FOR-TRADE PROGRAMMES TO REDUCE TRADE COSTS**

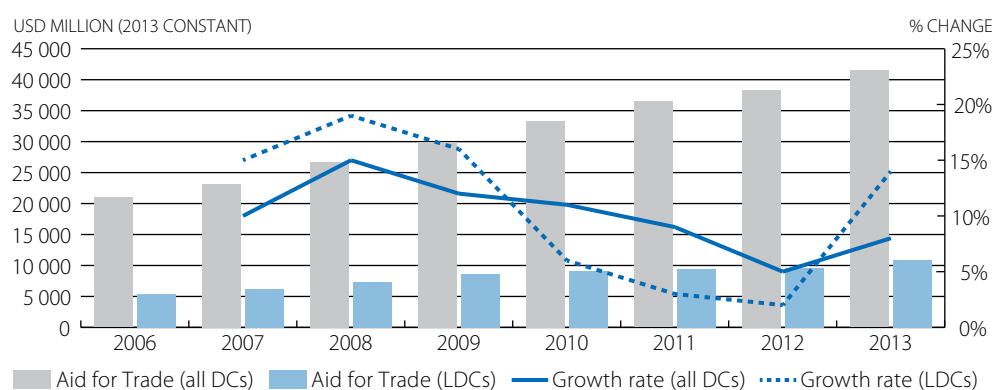
As discussed above, various trade capacity building initiatives have contributed to reducing trade costs in a number of LDCs, of which the aid-for-trade initiative is a prominent one. A rich body of literature has emerged in the areas of aid for trade in general and the role of these initiatives in reducing trade costs in particular. Although the literature is inconclusive, there is a general acknowledgement that support provided for trade policy and reform have been effective in reducing trade costs in developing countries because of its focus on “soft” infrastructure and investment in enhancing institutional quality (see, for example, Cali and te Velde [2009], Portugal-Pérez and Wilson [2010], Helble et al. [2012] and Massa [2013]). This finding is, however, not ubiquitously unambiguous, particularly when it comes to low income countries and LDCs. The reason for this is because the support towards strengthening institutional quality does not seem to produce the desired impact without addressing infrastructural or supply-side bottlenecks for which more and targeted aid for trade is necessary (see, for example, Busse, Hoekstra and Königer [2011], Vijil and Wagner [2012], Hühne, Meyer and Nunnenkamp [2013]).

### **Aid for trade in numbers**

Ever since the launch of the aid-for-trade initiative in 2005, aid for trade has not only been increasing but has also proven resilient to the shock emanating from the global financial crisis. This is not only true for commitment but also for disbursement. Going by the data provided by the OECD CRS, it appears that aid-for-trade commitment as well as disbursement nearly doubled between 2006 and 2013, posting growth rates of approximately 100% and 98% respectively (see OECD CRS database and Chapter 1).

Although the annual growth rate varied considerably, overall, there had been a fairly steady growth except for 2011, when a slight dip of 5% was experienced on aid-for-trade commitment compared to 2010. This may be explained by the austerity measures pursued due to low growth in most member countries of the Development Assistance Committee (DAC) in the aftermath of the global financial crisis. In 2012, the growth rate of commitment rebounded, although there was again a fall in 2013. However, what really matters is that the disbursement rate has remained consistently positive (ibid).

Aid-for-trade disbursement to LDCs has also been increasing in the past eight years; in fact, it has surpassed the growth achieved for total aid for trade. Compared to the 98% growth between 2006 and 2013 for overall aid-for-trade disbursement as indicated above, disbursements to LDCs increased by 104% during the corresponding period. The annual growth rate has been erratic not only for the LDCs but for the entire group of developing countries. Although the growth rate in LDCs declined in the aftermath of the global financial crisis and plummeted to 2% in 2012, it rebounded in 2013 (Figure 5.7). According to CRS figures, LDCs received the second highest share (27%) among various groupings, followed by lower middle income countries (34%).

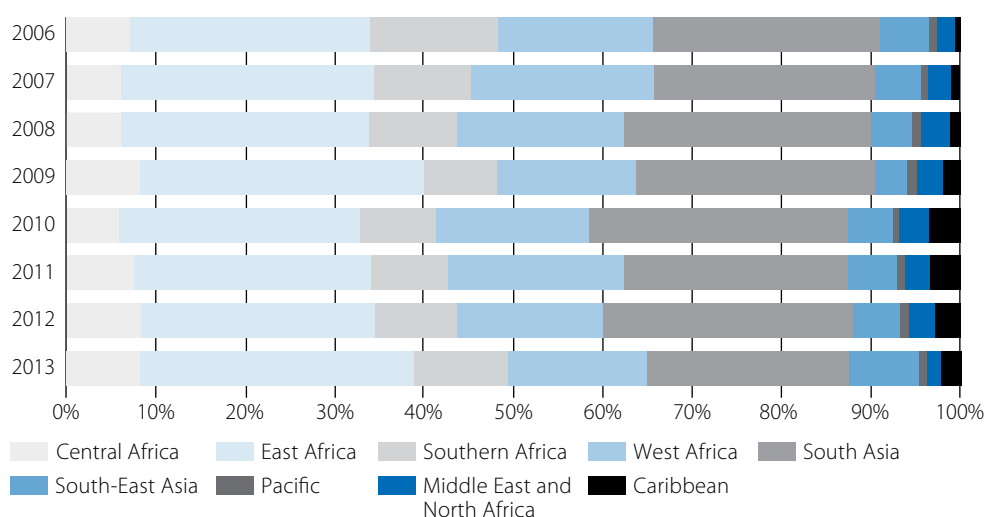
**Figure 5.7 Disbursements, developing countries - LDCs, 2006-13**

Source: Authors' calculation based on the OECD-DAC aid activity database (CRS).

StatLink <http://dx.doi.org/10.1787/888933241270>

However, what may be a matter of concern from a development perspective is the concentration of aid for trade, with the top ten countries receiving 63% of aid-for-trade resources and the bottom ten receiving only 2%. Although this might not be a major problem, because those countries at the bottom of the list are the Small Island Developing States (SIDS) with a limited population, the amount of resources LDCs are receiving comparable to their needs as well as absorptive capacity needs to be considered.

In order to observe the regional variation in aid-for-trade disbursement, we present the share of various groups of LDCs in the aid-for-trade disbursement over the past eight years for LDCs divided into nine sub-regions in Figure 5.8.

**Figure 5.8 Shares of aid for trade disbursement for nine LDC sub-groups, 2006-13**

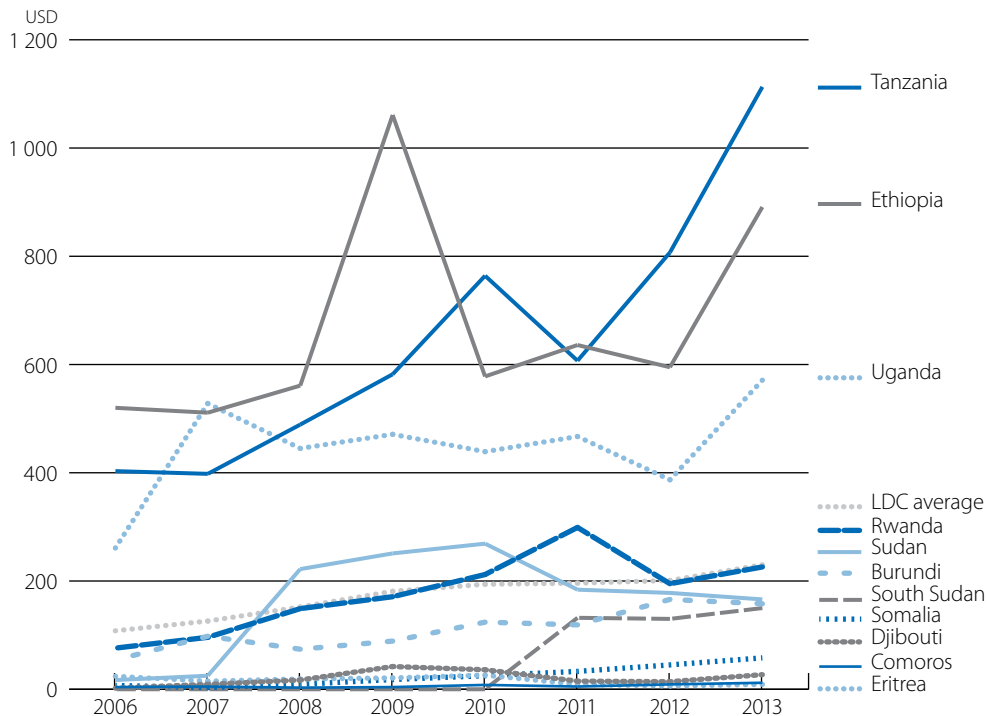
Source: Authors' calculation based on the OECD aid activity database (CRS).

StatLink <http://dx.doi.org/10.1787/888933241288>

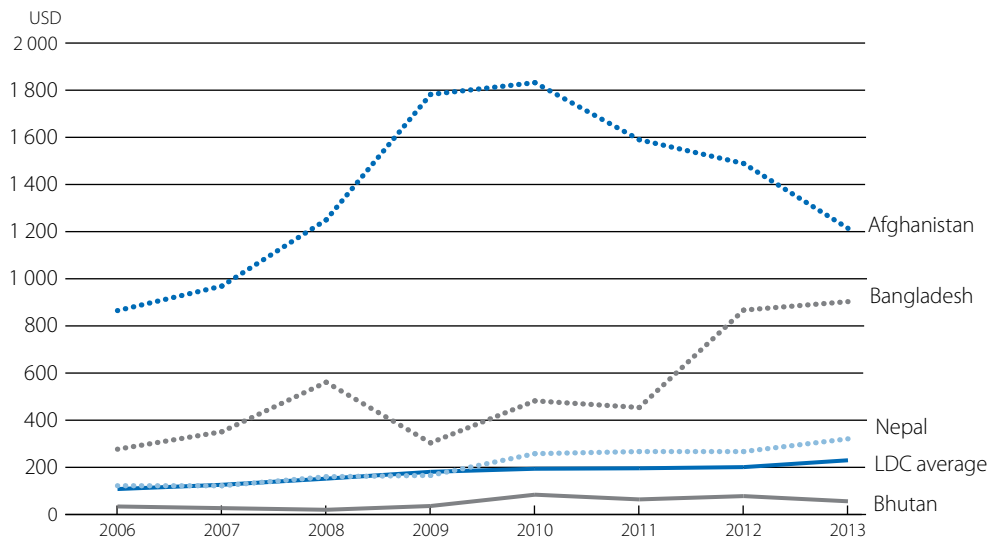
According to Figure 5.8, two sub-regions – East Africa and South Asia – have accounted for a lion's share of aid-for-trade disbursement over the past eight years, with their cumulative receipt being 54%, of which 28% went to East Africa and 26% to South Asia. Other sub-regions were left with a total of 46% of aid-for-trade disbursement. Even within these two sub-regions, aid-for-trade support received by the countries varied significantly. What we present here are country specific pictures within these two sub-regions (Figures 5.9).

**Figure 5.9: Aid for Trade to East Africa and South Asia sub-regions (disbursements)**

**East Africa**



**South Asia**



Source: OECD-DAC/CRS aid activity database.

StatLink <http://dx.doi.org/10.1787/888933241291>

As can be seen from the figures above, there are a few countries receiving a higher share than the rest of the LDCs, and a much higher share than the LDC average tends to dominate. For example, in the case of East Africa, Ethiopia, Tanzania and Uganda receive more than the rest of the countries in the region. Similarly, in the case of South Asia, Afghanistan receives a significantly higher amount than the other LDCs, although the aid-for-trade receipt of Bangladesh is also much higher than the other two countries in the region and certainly much higher than the LDC average.



Finally, turning to aid for trade provided by the EIF, which takes the equity principle into account while providing catalytic resources, support is provided mainly under three broad headings. These are: 1) analytical work (pre-DTIS, DTISU and feasibility study); 2) institutional support (creation and strengthening of national institutional structure and trade mainstreaming support); and 3) building productive capacity (sector specific or cross cutting support in areas such as agribusiness, textiles and apparel, tourism, standards and trade facilitation). As of 3 May 2015, the EIF Programme had made a total allocation of USD 193 million, which represents 97% of the resources available in the EIF Trust Fund. Although 48 LDCs and three recently graduated countries have joined the EIF, institutional support (up to USD 1.5 million) has been provided to 37 countries and 36 incidents of productive capacity building support (up to USD 3 million per project) have been so far delivered in 27 countries (see EIF website for further details).

## LESSONS LEARNED

Based on aid-for-trade intervention on the ground, of which the EIF is an integral part, the following lessons can be learned with a view to addressing trade-related challenges facing LDCs in an effective and sustained manner:

**Analytical work:** Before starting any aid-for-trade intervention, it is necessary to conduct robust, evidence-based analytical work to understand the needs and priorities of the country as well as the trade related opportunities and challenges. It is equally important to understand reforms undertaken and the political economy aspect of reforms and aid-for-trade interventions already in place, as well as to identify gaps. The EIF helps countries to prepare DTISs, which also include priority action matrices, and update them at periodic intervals of three to five years. This comes as a handy tool for the respective government, other in-country stakeholders, the EIF, various bilateral, multilateral and regional donors and EIF partner agencies to design and sequence their interventions. This also contributes to ensuring that the aid-for-trade support is targeted to the needs and priorities identified by the EIF country.

**Institutional capacity:** Countries with better institutional capacity not only tend to set their priorities right but also utilise aid for trade effectively. If the institutional capacity is built and the government is committed to ensuring that benefits derived from the project are sustained, it is likely to contribute institutional, human and financial resources to sustain the gains. The EIF creates two types of institutional structures within the country that are vital for the building of trade-related institutional capacity. First, an NSC is created as the apex body to oversee the implementation of the EIF programme in the country. The NSC is normally chaired by a high ranking government official and comprises representatives of trade and other sectoral ministries, the EIF Donor Facilitator (DF), the private sector, civil society and the academic community. Second, a national EIF Focal Point, usually a senior bureaucrat from the Ministry of Trade, guides the functioning of an EIF National Implementation Unit, which is often housed within the ministry itself.

**Country ownership:** Commitment and ownership runs right from the highest level of political leadership to the street level bureaucrats. The private sector and civil society are necessary for any aid-for-trade intervention to succeed. If the stakeholders in the country are convinced that they own and lead the process and any outside intervention is only contributing to the agenda that they are pursuing, the chances of success are higher. An indicator of country ownership is the mainstreaming of trade into the national development agenda, as well as sectoral programmes and policies, which are successfully achieved by the EIF as noted above. Moreover, the EIF multi-stakeholder governance structure means that ownership from all the relevant stakeholders tends to be fairly strong.

**Time horizon:** While some reforms can be undertaken with a stroke of a pen, in others it takes time for the benefits to percolate down to the real users. For example, a customs reform programme, such as putting in place a single window system, does not bring immediate results because it is bound to face some teething problems due to the lack of capacity of the actors and operators to deliver and derive benefits, co-ordination failure and opposition by vested interest groups. Once these issues are resolved, which may take considerable time, benefits can be realised. Therefore, perseverance on the part of the stakeholders is extremely important.

**Resource requirement:** Since some of the measures aimed at addressing transportation and logistics problems are resource intensive and the domestic actors – i.e. the government and the private sector – alone cannot meet these costs, donors should contribute sufficient resources to help countries achieve desired results. If a donor is unable to support an initiative in its entirety, it would be advisable either to support the initiative through a consortium approach, with the participation of multiple donors, or to encourage the recipient country right from the beginning to leverage resources. Another alternative approach is to include challenge funds supported by donors that encourage more private sector participation in logistics and transport, as is happening in East Africa. This is an area in which the EIF has achieved mixed results and needs to scale up its work (Capra International Inc., 2104).

**Donor co-ordination:** This is vital to avoid duplication of funding as well as achieve synergy between the support provided by various donors. One of the objectives of the EIF is to ensure a co-ordinated delivery of trade related technical assistance, which is achieved through three different channels. First, the EIF encourages aid-for-trade support to be based on country priorities identified by the DTIS process. The various institutional structures created under the EIF are well informed about these priorities as well as support already provided by other donors. Second, the DF conducts regular consultations with other donors on the ground to co-ordinate the delivery of aid-for-trade support. Third, the DF, who is represented in the NSC, is abreast of the status of aid for trade received by the country in any given period.

**Political economy factors:** In any country, vested interest groups are present, trying to thwart reforms to protect the rent they are used to receiving. Therefore, when undertaking reforms these factors need to be taken into account either by creating an incentive structure such that vested interest groups do not oppose reforms or by convincing them of the long-term benefits of the reform, even if some problems are likely to occur in the short run. This is an area in which the EIF has yet to make inroads.

It needs to be noted that some of these lessons are intimately intertwined. For example, analytical work leads to mainstreaming, mainstreaming relates to ownership, ownership leads to leveraging, particularly through the contribution of domestic resources, and both of these elements contribute to sustainability.

## CONCLUSIONS

The LDCs' participation in global trade, including GRVCs, remains low. Average trade costs are substantially higher in LDCs. Such costs include those related to transport and logistics, onerous border procedures, weak policies and regulatory frameworks and a low capacity in meeting standards. They play a significant role in preventing LDCs from improving their productivity and competitiveness. As a result, LDCs are unable to realise their trade potential as a means to accelerate economic growth and development.

This is compounded by a combination of other inter related structural factors, which are pronounced in LDCs, such as poor levels of human development, high levels of export concentration and prominence of SMEs involved in trade that bear a disproportionate burden of trade costs. There are also other important factors, such as fragility and conflict, and those that are natural, which further disadvantage LDCs, such as being landlocked or being highly vulnerable to the impact of climate change and/or natural disasters.

There has been a shift in the prioritisation of addressing trade costs by LDCs, which reflects the evolving dynamics of global trade and the increasing focus on behind-the-border measures and the growing importance of regional integration. Furthermore, the private sector is more active in shaping country priorities in this area, and there is more access to analyses and data that help better identify such priorities. Finally, there is an improved alignment of aid-for-trade initiatives to address such priorities at the country level.

LDCs have been making progress in undertaking the necessary reforms to reduce their trade costs, of which there are clearly many good examples. However, there are variations among regions, and there is a need for more consistent performance at the country level. There is still much work to be done. Evidence based prioritisation should continue to underpin the reform agenda of LDCs, particularly the EIF's DTIS analytical work.

Aid-for-trade initiatives can play a particularly critical role in terms of financial assistance and technical capacity building and institutional support to help LDCs reduce their trade costs. Support provided for economic infrastructure and trade policy and regulations has been growing over the past eight years, with both of these categories exhibiting robust growth in the past two years. Literature on aid for trade shows that the initiative is contributing to a reduction in trade costs. Given the extensive needs of the LDCs and the significance of high trade costs, commensurate levels of AfT flows to LDCs must continue and also better target those LDCs that are in need the most. As the only global aid-for-trade programme focused on addressing the trade needs of LDCs, the EIF offers a unique opportunity for development partners to support and find ways to advance work in this area.

The impact of aid-for-trade intervention in the context of LDCs tends to be higher when it is underpinned by a robust and credible analytical work; where country ownership is high; when sustainable institutional capacity is built; where support is provided for a sufficiently long period; where diverse resources are tapped into and when a co-ordinated response from donors is achieved. Moreover, such intervention can be successful if political economy challenges are appreciated, mainstreamed and mitigated.

While all of the above are relevant for pursuing the agenda of lowering trade costs in LDCs, this can be bolstered by ensuring an increased participation of the private sector and the enhanced use of regional instruments and mechanisms. Finally, LDCs need to explore how they can leverage global development processes, including the Istanbul Programme of Action for LDCs (IPoA) and the Sustainable Development Goals (SDGs), to support their trade related priorities in general and directly reduce trade costs to realise their overall vision of achieving inclusive and sustainable development.

<b>ANNEX 5A.1 Regional sub-groupings of the LDCs</b>	
<b>Sub-region</b>	<b>Country</b>
<b>South Asia</b>	Afghanistan, Bangladesh, Bhutan and Nepal
<b>South East Asia</b>	Cambodia, Lao PDR, Myanmar and Timor-Leste
<b>Pacific</b>	Kiribati, Solomon Islands, Tuvalu and Vanuatu
<b>Caribbean</b>	Haiti
<b>Middle East and North Africa</b>	Mauritania and Yemen
<b>East Africa</b>	Burundi, Comoros, Djibouti, Eritrea, Ethiopia, Rwanda, Somalia, Sudan, South Sudan, Tanzania and Uganda
<b>West Africa</b>	Benin, Burkina Faso, Cabo Verde, Gambia, Guinea, Guinea-Bissau, Liberia and Mali
<b>Central Africa</b>	Central African Republic, Chad, Democratic Republic of the Congo, Equatorial Guinea and Madagascar
<b>Southern Africa</b>	Angola, Lesotho, Malawi, Mozambique, Sao Tome and Principe and Zambia

Source: African Development Bank <<http://www.afdb.org/en/>>; Asian Development Bank <<http://www.adb.org/>>; and Inter-American Development Bank <<http://www.iadb.org/en>>.

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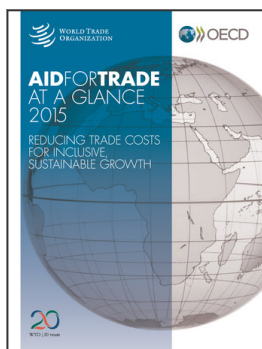
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