Country-driven strategies and best practices on economic diversification and transformation

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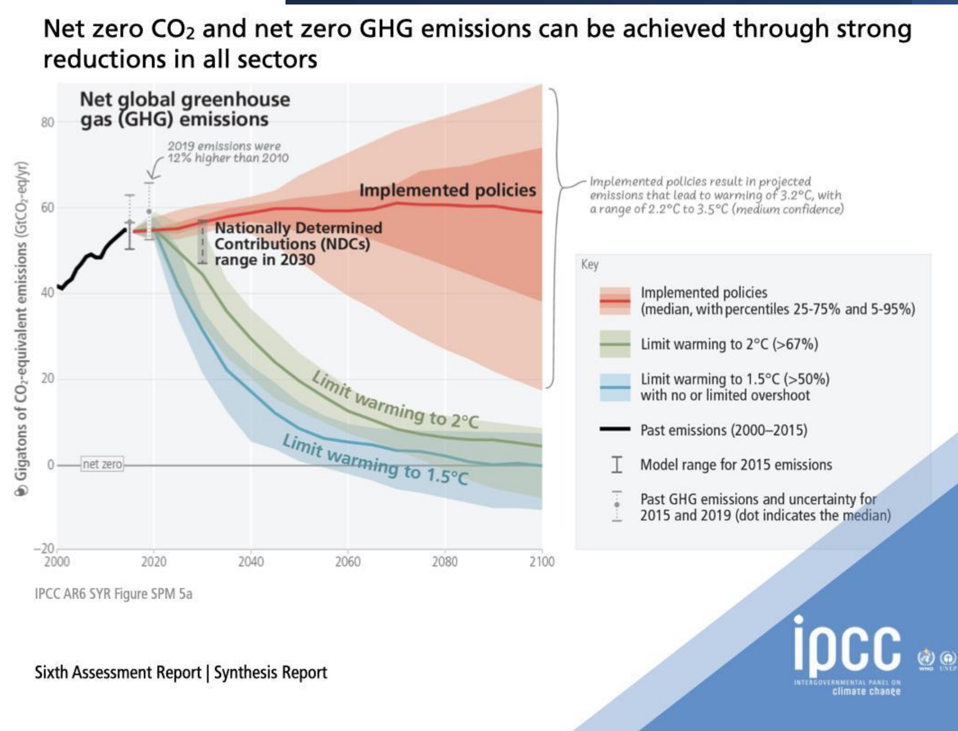
1.2 Objectives

- Present concrete examples of country-led strategies and best practices for economic diversification and transformation adopted by countries in response to climate change.
- Highlight key challenges and opportunities for resource-dependent economies seeking to transition to diversified economic structures while implementing low greenhouse gas emission policies.
- Provides policy recommendations for possible actions by the subsidiary bodies

Report structure

1.3 Economic diversification in the context of response measures

- Limiting global warming to 1.5°C and 2 °C requires rapid, deep reductions in GHG emissions compared to pre-industrial levels, a decline of 43% by 2030 and reach net zero around mid-century.
- However, the adoption of climate change policies in one country or region can have transboundary impacts.
- In essence, economies dependent on resources such as fossil fuels, agriculture and minerals are the most vulnerable to the effects of response measures.



1.4. Approaches for economic diversification

- **Economic diversification** is a strategy used to expand the profile of economic activities across a wide range of sectors and industries, hence reducing overreliance on a single industry or a narrow set of economic activities, to enhance economic growth and build resilience against cross-border economic vulnerability, including the negative effects that may arise from climate response measures.
  - i) *Horizontal diversification:* involves expanding into new products and industries to reduce dependence on a limited set of commodities. It often starts by leveraging existing strengths in different resource-based sectors, such as minerals, forestry or agriculture, where there is already a comparative advantage. This approach involves broadening the production base and shifting to export-led policies to move away from over-reliance on a single sector, often based on natural resources. To enable such diversification, countries could focus on creating a business-friendly climate to attract investment and foreign capital and strive for a more complex and higher quality national economic output.
  - ii) *Vertical diversification*: focuses on adding value to raw materials by moving up the value chain, thereby increasing their economic value. For many countries, especially those heavily dependent on commodities, this approach is an effective first step towards broader economic diversification. This involves not only expanding value creation within the extractive sector, but also strengthening links with other industries and moving into more downstream value-added activities.

2. Economic diversification case studies and learnt lessons

2.1. Oil and gas-based economy

- 2.1.1 United Arab Emirates
- 2.1.2 Saudi Arabia
- 2.1.3 Oman
- 2.1.4 Indonesia
- 2.1.5 Norway

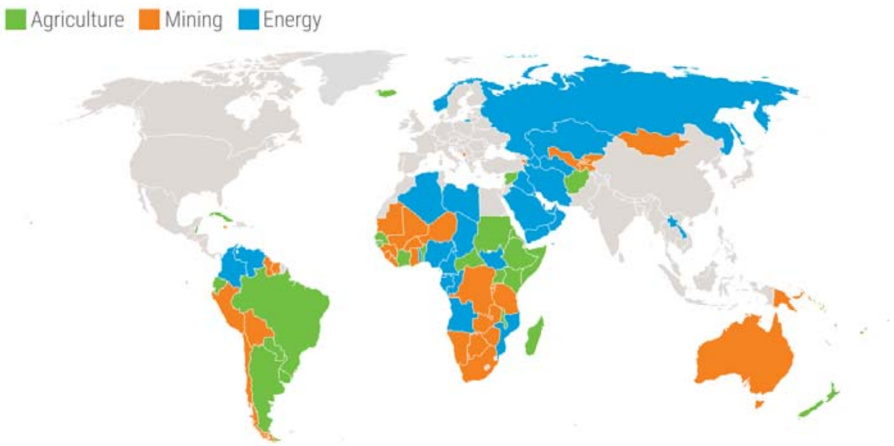
2.2. Agriculture-based economy

- 2.2.1 Mauritius
- 2.2.2 Costa Rica
- 2.2.3 Uganda

2.3. Mineral extraction-based economy

- 2.3.1 Chile
- 2.3.2 Indonesia

Global Commodity dependence



Note: In the case of two countries (Togo and United Arab Emirates), it was not possible to consistently identify the dominant commodity group due to the presence of large volumes of exports of manufactured products that may partially or totally be re-exports. The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

Source: UNCTAD calculations

2. Economic diversification case studies and learnt lessons

2.1. Oil and gas-based economy

2.1.1 United Arab Emirates (strategic investments in various non-oil sectors -food, beverage, agriculture, pharmaceuticals, electrical equipment, electronics, petrochemicals, chemical products, rubber, plastics, machinery, equipment, hydrogen, medical technology, and space technology and tourism, and fostering a competitive knowledge economy)

2.1.2 Saudi Arabia (enhancing the value chain of its oil industry and strengthening or establishing new non-oil sectors, including significant investments in clean energy sources, creation of 'economic cities', tourism, entertainment, expansion of its mining and mineral processing industry)

2.1.3 Oman (enhancing the value chain of its oil and gas industry; and investments in non-oil sectors such as energy, mining, manufacturing, transport, sustainable tourism, ICT)

2.1.4 Indonesia (shift to export-oriented policies and attracting foreign investment, relocation of factories and creation of export processingzones; opening the market to private investment such as telecommunications, banking, cement, television and gas)

2.1.5 Norway (decoupling oil and gas industry from readily diversified economy based on industries such as fishing, shipping, forestry, ag riculture and hydropower)

2.2. Agriculture-based economy

2.2.1 Mauritius (dominated by sugar exports until the mid-1980s; to a diversified, service-oriented economy: such as information technology, financial services and business services, and tourism. maritime security, export processing zones, leveraging international trade)

2.2.2 Costa Rica (transition from a predominantly agricultural economy (coffee and banana export) to a diversified economy focused on high-value industries and sustainable tourism; shift to attracting foreign direct investment (FDI) focused on exporting domestically produced goods)

2.2.3 Uganda (transition from a predominantly agricultural economy (coffee, cotton and tea) to moving into the production of food, beverag es, tobacco and light construction materials such as steel and cement, and tourism; revising the investment code to encourage foreign direct investment, industrial polici es and trade policies)

2.3. Mineral extraction-based economy

2.3.1 Chile (strategic use of its vast copper reserves- implementation of a structural budget surplus rule- improving the quality of copper production and has expanded into the export of processed copper products; expanded into industries such as salmon, fresh fruit, forest products and wine-the development of human capital to raise level of skills in these industries)

2.3.2 Indonesia (moving up the value chain with its nickel industrial strategy; from stainless steel to use its nickel resources for domestic EV battery production)

Learnt lessons

- There is no consensus on the starting point or best practice for economic diversification
- Countries have taken different approaches to economic diversification
- Most used a combination of both vertical and horizontal diversification policies:
- *Vertical:* **strategic natural resources management**
    - develop a comprehensive strategy
    - law requiring companies to add value within the country
    - joint ventures (Indonesia)
    - Expanding industrial base (Norway, Indonesia)
    - Advancement of technologies (Norway)
    - diversifying export profile (Indonesia)
- *Horizontal:* **developing new, high-value industries/sectors**
    - attract private and foreign investment (Chile, Indonesia)
    - financial incentives
    - market access (costa rica from coffee/banana to medical products)
    - the development of human capital (training programmes, technical centres, collaborative initiatives) (Chile, Saudi Arabia)
    - Use of commodity sale profits to invest in other sectors (Indonesia, Saudi Arabia, Oman, UAE)
    - Research and development (Norway and UAE)
    - Low carbon energy sources (Indonesia, Oman, Saudi Arabia, UAE, Norway)

3. Challenges and opportunities for economic diversification

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- Political and macroeconomic stability
- Building Human Capital
- Accumulating skills and productive knowledge
- Investing in research for export sophistication
- Primary commodity or new products and new markets (Geographic location and connectivity to markets)
- Vertical Policies and Effective Public Spending

4.1 Possible actions by the subsidiary bodies

- Maintain macroeconomic stability
- Adopt export-oriented policies
- Ensuring a just and inclusive transition away from commodity dependence
- Use of industrial policies
- Investing in transport and communications infrastructure
- Involving the private sector
- Addressing climate risks and opportunities

Thank you

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Learnt lessons

- There is no consensus on the starting point or best practice for economic diversification,
- Countries have taken different approaches to economic diversification
- Most used a combination of both vertical and horizontal diversification policies:
- *Vertical:* strategic natural resources management (Indonesia shift in nickel use from traditional stainless-steel production to domestic EV battery production; Chile-improving the quality of copper production and has expanded into the export of processed copper products)
    - develop a comprehensive strategy
    - law requiring companies to add value within the country
    - joint ventures
    - Expanding industrial base
    - Advancement of technologies
    - diversifying export profile
- *Horizontal:* Chile has successfully expanded into industries such as salmon, fresh fruit, forest products and wine; Costa Rica's transition from a predominantly agricultural economy to a diversified economy focused on high-value industries and sustainable tourism:
    - attract private and foreign investment (Chile, Indonesia)
    - financial incentives
    - market access (costa rica from coffee/banana to medical products)
    - the development of human capital (training programmes, technical centres, collaborative initiatives) (Chile, Saudi Arabia)
    - Use of commodity sale profits to invest in other sectors (Indonesia, Saudi Arabia, Oman, UAE)
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