Vulnerability Profile

Djibouti

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Overview

Djibouti met the income-only criterion alone for the first time during the 2021 CDP Triennial Review of the LDC Group. Its score for the first criterion, that of Gross National Income (GNI) per capita, was 132% in 2021, with an income per capita of $3,235[1]. For the second criterion, the Human Assets Index (HAI), Djibouti has a score of 61.9, whereas for a graduation 66.0 is required. Hence, its score is 93.8% of the graduation threshold.[2] Highest vulnerabilities to Djibouti's development of human assets are found in the areas of gross secondary school enrolment, low literacy rate, and under-5 mortality. For the Economic and Environmental Vulnerability Index (EVI), Djibouti had a score of 53.9 during the 2021 review, which indicates a long distance to the necessary score for meeting the graduation criteria of 32 (60%).[3] Djibouti's score is also largely above the average score of LDCs (39.1), emphasizing the country's large vulnerability to economic and environmental shocks. The three greatest areas of vulnerability to Djibouti's prosperity and sustainable development are: instabilities in the export of goods and services, the share of the population living in arid areas, and victims of natural disasters.

Over the last two decades, Djibouti has experienced strong economic growth. Between 2010 and 2019, gross domestic product (GDP) growth in constant 2015 prices ranged between 11.7% (2010) and 6.6% (2019). The rise in GDP is the result of massive investments in the field of transport and logistics, placing Djibouti as an important hub in the Horn of Africa. Djibouti has three unique advantages in the region, which are: (i) peace and security; (ii) a geostrategic position; and (iii) a stable macroeconomic framework with a strong currency (the Djibouti Franc) pegged to the US dollar and stable since its creation on 20 March 1949. The economic structure of Djibouti a markedly different from that of the average LDC. The tertiary sector produces 80% of GDP, the secondary sector 17% and the primary sector 3%. Djibouti's commercial services are dominated by the transport sector and income depends heavily on commercial activities related to its port facilities. Ethiopia is the main customer of the port of Djibouti, as more than 85% of its capacity is taken by Ethiopia's trade.

The economic growth that Djibouti has experienced has not been redistributive, which has resulted in increased inequality. There are strong disparities between the capital and the interior regions. In 2017, about 39% of the population lived below the $3.2 per day poverty line and 17% lived in extreme poverty (i.e. below the international poverty line of $1.9 per day). Poverty and growing

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[1] The income-only graduation threshold is set at three times the graduation threshold and is $3,918 for the 2024 review. With an updated GNI per capita of $2,931 in 2022 (estimated at $3,029 for 2023), Djibouti would not meet the income-only criteria anymore.

[2] Based on the 2023 data update, Djibouti would reach an HAI of 63.06, a score of 95.5% of the graduation threshold.

[3] Based on the 2023 data update, Djibouti would reach an EVI of 51.86.

inequalities are central challenges for sustainable development in order to achieve Sustainable Development Goal (SDG) 1 in Djibouti and constitute major vulnerabilities for social cohesion.

As a small country with a population of approximately 1 million inhabitants, Djibouti largely depends on the world and regional economy, and it is highly vulnerable to external shocks. The COVID-19 pandemic caused a slowdown in real GDP growth from 6.6% in 2019 to less than 1.1% in 2020.

a) People

The indicators of human capital performance indicate that Djibouti is highly vulnerable with regards to low literacy rate, low school enrollment and high prevalence of malnutrition. Although the population in rural areas represents only about 15% of the total population, rural areas are made up of 45% of people living in extreme poverty and have particularly limited access to public services such as electricity, water and sanitation.

While progress has been made, prevalence of stunting remains at 20.9 percent in 2019. Model estimates by UNICEF/World Bank suggest a slight decline to 18.7 percent in 2022. This is well below the LDC average of 32.3 percent. According to the Voluntary National Review on the monitoring of the SDGs, 33.6% of children in rural areas suffered from stunted growth, compared with 18.5% for children in urban areas.

In terms of progress on education, gross secondary school enrolment has improved from 39% in 2015 to 45% in 2022, according to UNESCO Institute for Statistics. This is slightly lower than the LDC average (46.5%). Despite improvements, the share of illiterate population remains high. Estimates suggest that the literacy rate for women is currently 39.5%, compared to 60.1% for men. Moreover, women are highly vulnerable as they constitute only 36% of the active population and they are particularly present in the informal sector. Compared to Djibouti's relatively high-income levels, its poor performance especially in health indicators and its weak human capital base is of major concern for its sustainable development towards and beyond graduation. The current national health system is characterized by an insufficient infrastructure of health, primary care and hospital services. Energy shortages and poverty, especially in rural areas, compromise the effectiveness of care, prevent access to adequate health care and put lives at risk. Domestic general government expenditures on health, estimated at only 1% of GDP – compared to an average of 1.4% of lower middle-income countries – must be increased in order to effectively fight malnutrition.

b) Prosperity

The recent external shocks caused by the COVID-19 pandemic, followed by the crisis in Ethiopia and the war in Ukraine exemplified Djibouti's volatile exports. In 2020, imports and exports of goods and services fell by around 30%. While real economic growth (in 2015 constant prices) slowed to 1.1% in 2020, estimates indicate that it rebounded to 5.64% in 2021, thanks to the rebound in exports in the free zones and the recovery in the economy activity, as well as services exports (transport, logistics and telecommunications) to Ethiopia. Still, growth softened to 3.06% in 2022, according to UNCTADstat. Political instability in Ethiopia also affects food exports to Djibouti, which depends on Ethiopia for most of its domestic food consumption. The increase in global oil prices due to the global political context could induce higher freight prices and shipping costs for the transport of goods, which has an upward impact on all imported goods. It must be noted that trade data are not reliable for Djibouti, which prevents in-depth analysis and definitive conclusions on the impact of exogenous shocks on exports and imports.

The prevailing economic model based on port infrastructure and associated services generates few jobs for Djiboutians in the private sector. The most visible consequence of the concentration of economic activity and vulnerability of exports is Djibouti's high national unemployment rate, estimated at 47%. Unemployment affects more women (63.4%) than men (38.7%) throughout the country and is extremely high among young people (15-24 years old), whose unemployment rate in Djibouti-City is 87.5%. The COVID-19 pandemic has heightened vulnerabilities. An estimated 40 thousand people lost their jobs. The tertiary sector, the country's main job creator, was the most affected.

Moreover, due to its limited productive capacities and arable land (less than 0.1% according to FAO estimates), Djibouti is a net food importer: 90% of the food is imported, according to World Food Programme estimates. This makes the country highly dependent on international market prices. The consequences of the war in Ukraine weigh heavily on the Djiboutian economy, which was strongly affected by an additional increase in prices of basic food products that Djibouti imports from Ukraine, such as flour, wheat and oil.

Last but not least, the concentration of economic activity on the capital-intensive transportation and logistics sectors has caused a surge of external debt from 51% of GNI in 2015 to 86.9% of GNI in 2020, and 97.7% in 2021. Interest payments have risen sharply in recent years.

Djibouti's natural resource endowments are clearly limited and so are its possibilities for diversification and structural transformation based on current productive capacities. Nevertheless, potential areas for diversification include information and communication technology (ICT) and some business services, as well as low-skilled manufacturing. However, Djibouti's private sector currently plays a marginal role and faces several challenges: limited access to water, electricity and skilled labour are the three major factors, due to their high cost and scarcity, which constitute obstacles to economic development and the growth of the private sector. Closing the gender literacy gap and improving the quality of education would unlock untapped potential in the economy. Moreover, the economic sectors are insufficiently open to competition and are still dominated by monopolies and state enterprises, which poses the risk of the accumulation and concentration of wealth among a restricted group.

c) Planet

The consequences of climate change are critically felt in Djibouti. According to the Global Climate Risk Index, Djibouti is one of the 50 countries in the world most vulnerable to extreme climate risks. The increase in the incidence of droughts between 1990 and 2022 poses an extreme risk to the population living in arid zones. Over the period 2010 to 2022, a total cumulated number of 392 thousand people were affected by severe droughts and 360 thousand people by floods, illustrating the heightening future risk of climate change. The consequences of Djibouti's vulnerability to extreme climate risks are felt more than ever. The recent ongoing drought in East Africa is one of its worst in history and not only led to the death of millions of livestock but also impact natural vegetation. The high price volatility of food items which has been exacerbated by the war in Ukraine are affecting the food security and nutrition situation in Djibouti. The national consumer price index for food rose sharply, more than any other consumed product group. Consumer prices in Djibouti for fresh fruit or root vegetables rose by 87% and tubers and plantain by 127% between June 2021 and 2022.

The multidimensional and interrelated vulnerabilities of the Djiboutian economy to exogenous supply shocks hit the poorest parts of population, mostly living in rural areas, the most. Apart from investment in climate change adaptation, private sector development and diversification, a strengthening of the social protection system is key to reap high benefits of Djibouti's economic growth and advantageous geopolitical position.

d) Peace

Despite this unique relative stability in the region, Djibouti is not immune to the upheavals that affect the region, particularly neighboring Ethiopia. The border states of Djibouti present factors of chronic instability, both internal and external. Also, the risks that the effects of regional instability are introduced into the economy are very real and are linked to movements in the flow of investments from abroad but also trade in goods and services.

e) Partnerships

Because of its small size, Djibouti depends on partnerships, especially with regard to development and investment financing. On the one hand, the ratio of public and publicly guaranteed debt to GNI has doubled between 2015 and 2020. On the other hand, worker remittances make a modest and decreasing contribution to GNI and official development assistance received has fallen from 15 percent of GNI in 2011 to 5 percent in 2020. To increase fiscal space for necessary social sector spending, Djibouti needs to prioritize concessional borrowing, strengthen debt management, improve public enterprise management, and broaden its tax base.

Economic dependence on key partners China and Ethiopia represents vulnerability in the event of heightened conflict in Ethiopia or slower economic growth in China. Chinese overseas development funding has been slowing for years and is unlikely to resume any time soon as the Chinese government will prioritize domestic economic revitalization. In addition, due to the strong dependence, any disruption of bilateral relations with its main partners may also have repercussions on the economic or financial situation of Djibouti.

1. Introduction

Geographically and demographically, Djibouti is the smallest state in the Horn of Africa in terms of size, with 23,200 km2, and population, with less than one million inhabitants. It shares borders with three countries: Ethiopia, Somalia and Eritrea. Djibouti has also a maritime border with Yemen. The neighboring countries are better endowed with resources and much more populated. In contrast, Djibouti has few natural or mineral resources. It is a dual economy, divided between a globalized sector (port activity, logistics, and a performing banking and financial system) and a traditional domestic economy, still largely informal. It is an economy with little or no agriculture, no extractive activities and an embryonic manufacturing sector. The state maintains a leading role, thanks to the fees it collects from port activities and from military bases installed on national soil. All of these characteristics, which Djibouti does not share with any other country, are reflected in a particularly high unemployment rate. Despite these constraints, Djibouti offers its citizens a much higher level of income than any of its neighbors. Hence, it is the distribution of this wealth that poses a problem, as the level of poverty remains high. GDP per capita (at constant 2015 prices) is estimated at $3,121 in 2022, compared to $815 in Ethiopia (according to UNCTAD stat database), its large neighbor and main economic partner. Whatever the nature of the crisis (political, economic or financial) that affects its regional or international environment, Djibouti’s economy shows a certain resilience.

Djibouti's resilience and relative prosperity are based on three factors which constitute its major assets:

- Peace and security, sources of lasting political stability in a region plagued by permanent conflicts;
- A unique geostrategic position at the origin of its constitution, a source of military and commercial revenue;
- A strong currency indexed to the dollar and stable since its creation on 20 March 1949, the Djibouti Franc (DJF), which positions it as the region's financial center.

These factors form the basis for economic growth and make Djibouti an important player in the region. Thanks to these three unique advantages in the region, Djibouti has served as a refuge for all those fleeing wars, ethnic conflicts and misery in neighboring countries (Eritreans, Ethiopians, Somalis, Yemenis). These assets are the foundation of its relative prosperity in relation to these same countries.

In terms of public policy, in 2022, the country launched the second five-year plan of its strategy 'Vision 2035', the National Development Plan (NDP) 2020-2024. This development plan, strongly influenced by the global pandemic of COVID-19 and its impact on macroeconomic and social variables, proposes a more inclusive economy, based on strong institutions and open to the outside world. It rests on the three pillars *inclusion*, *connectivity* and *institutions*, hence its name, 'Djibouti ICI' (UNECA, 2021).

This vulnerability profile aims to provide an analytical assessment of Djibouti's readiness for its reclassification in the category of least developed countries (LDC). In addition, the document can assist in the implementation of the NDP. However, it should be noted that the lack of data, particularly regarding structural transformation and trade, is a major constraint in analyzing vulnerabilities and developing evidence-based policies in Djibouti.

Section 2 presents background information on the country and provides a situation analysis of the path to graduation of Djibouti. It highlights recent issues and areas of intervention, including an analysis of the COVID-19 situation and the economic crisis. Section 3 then assesses the main areas of vulnerability, based on the five “Ps” of the 2030 Agenda for Sustainable Development: people, prosperity, planet, peace and partnerships. Section 4 identifies the structures and characteristics of the economy that are essential for sustainable upgrading and for reducing existing vulnerabilities. An annex will identify the building blocks and potential areas for a dynamic reclassification strategy.

2. Situation analysis: Policy and economic performance

2.1. Acceleration in growth and inclusive growth performance

Acceleration in economic growth

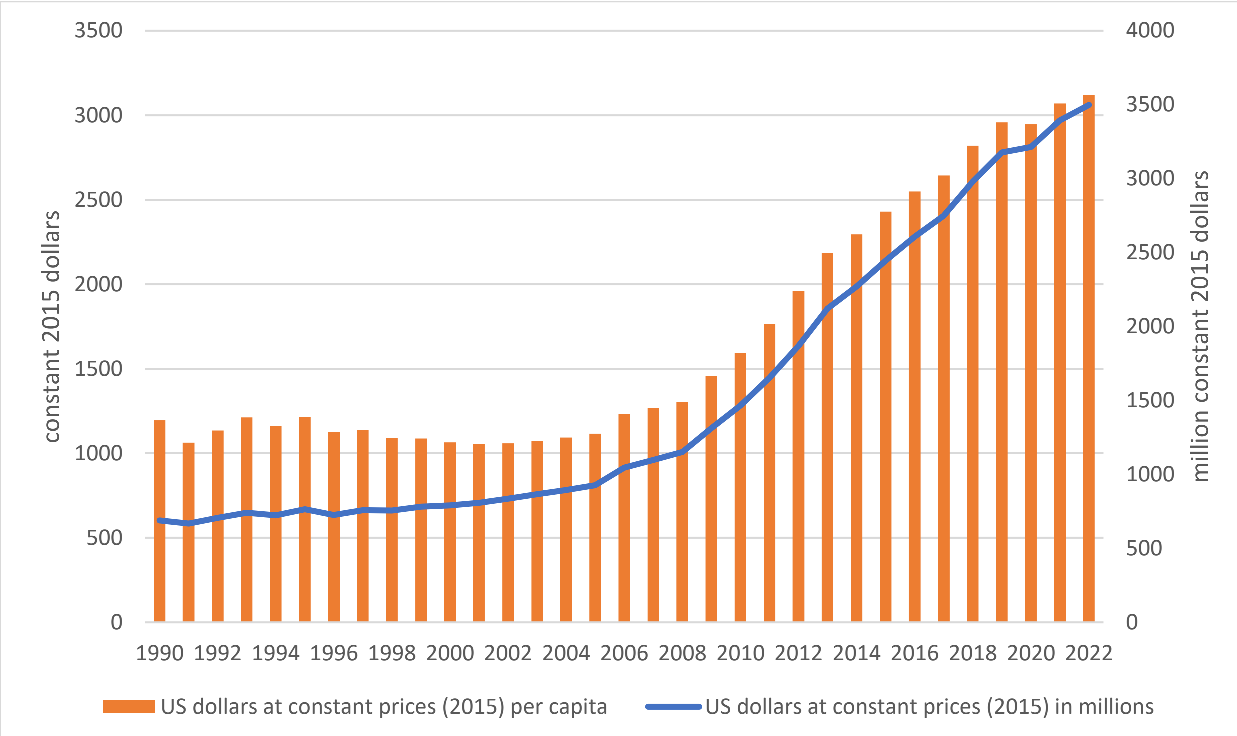
After the country became an independent nation in 1977, Djibouti's economy initially performed poorly before experiencing strong economic growth. As shown in Figure 1, since 2000, Djibouti has experienced a period of accelerating economic growth. Since 2010, economic growth (in constant 2015 prices) has averaged 8.5 percent per year, ranging from 11.7 percent (2010) to 6.6 percent (2019) (Figure 1). In total, between 1971 and 2019, Djibouti has witnessed 10 years of acceleration and 9 years of deceleration in its growth.

The national economy is resolutely outward-oriented, with the main growth sectors being livestock trade (up to 4 million heads of cattle exported per year), the commercial and industrial free zone around the port, tourism, the construction sector and the banking industry. Noting also that Djibouti heavily relies on international trade for its economic prosperity, the ratio between imports and exports of goods and services and GDP averages 151 percent between 2013 and 2021[4].

The economic performance of recent years is notably the result of the implementation of the Strategy for Accelerated Growth and Employment Promotion 2015-2019 (SCAPE), the first five-year plan carried out under the Djibouti Vision 2035. SCAPE has led to significant progress, including accelerated economic growth, poverty reduction, improved social indicators, and the construction of modern infrastructures such as the Djibouti-Addis Ababa railroad, ports, and an international free trade zone. The negative consequences of COVID-19 on this socio-economic progress have been mitigated by the implementation of the National Solidarity Pact (NSP) adopted by the Government on 13 April 2020 and aligned with the 2030 Agenda for Sustainable Development (République de Djibouti, 2021).

[4] Annual Report 2021 of the Ministry of Economy and Finance

Figure 1: Real GDP and GDP per capita, 1990-2022



Source : UNCTAD based on the UNCTADstat database [accessed November 2023].

Four positive elements have characterized Djibouti's strong growth performance since 2010 (Banque Mondiale, 2022)[5].

1. Peace and political stability. After a decade of civil conflict (1991-2001), Djibouti has built modern institutions that have matured, although they are still fragile. The country's stability stands out at a time when the region is in turmoil. The large presence of foreign military bases has provided Djibouti with a steady stream of income based on rent for its land, estimated at more than $130 million annually. For NATO countries, a presence in Djibouti provides maritime security and a base to combat regional militant threats.

2. Accelerated public investment. The Government has implemented the 2015-2019 strategy of accelerated growth and employment promotion, supported by large-scale investment in transport and logistics infrastructure, largely financed by China.

[5] Banque Mondiale (2022), Diagnostic du secteur privé : créer des marchés à Djibouti (Private Sector Diagnosis : Creating markets in Djibouti)

3. An important role in regional integration. Djibouti is the gateway to the Horn of Africa, a regional hub that connects Asia and Africa, and a gateway that links landlocked Ethiopia to the sea, the region's largest and fastest-growing economy.

4. Increased flows of foreign direct investment (FDI), driven by significant improvements in the business climate. Djibouti has attracted nearly $1 billion in FDI between 2014 and 2019, with the main investors in the services sector coming from China, the Gulf countries, and Ethiopia. However, the dispute between the Government of Djibouti and Dubai Port World over the concession of the port of Doraleh could damage the country's reputation as a prime investment destination.

The increased GDP is the result of massive investments in transport and logistics, making the Republic of Djibouti an important hub in the Horn of Africa. The trade and logistics platform (20.2 percent of the total value added) is skill- and capital-intensive. These massive capital-intensive investments are not labor-intensive, resulting in a persistently high unemployment rate and a correspondingly high level of poverty.

Inclusive growth: poverty and inequalities

Despite two decades of sustained growth, the income poverty rate in Djibouti has hardly declined. In 2017, about 39 percent of the population were living below the lower middle income poverty line ($3.2 per day) and 17 percent in extreme poverty (below the international poverty line of $1.9 per day)[6]. In 2002, 20 percent were living in extreme poverty. In Djibouti, vulnerability is multifaceted and particularly age and gender specific (affecting mainly children, the elderly and women) (Lazhar, 2020).

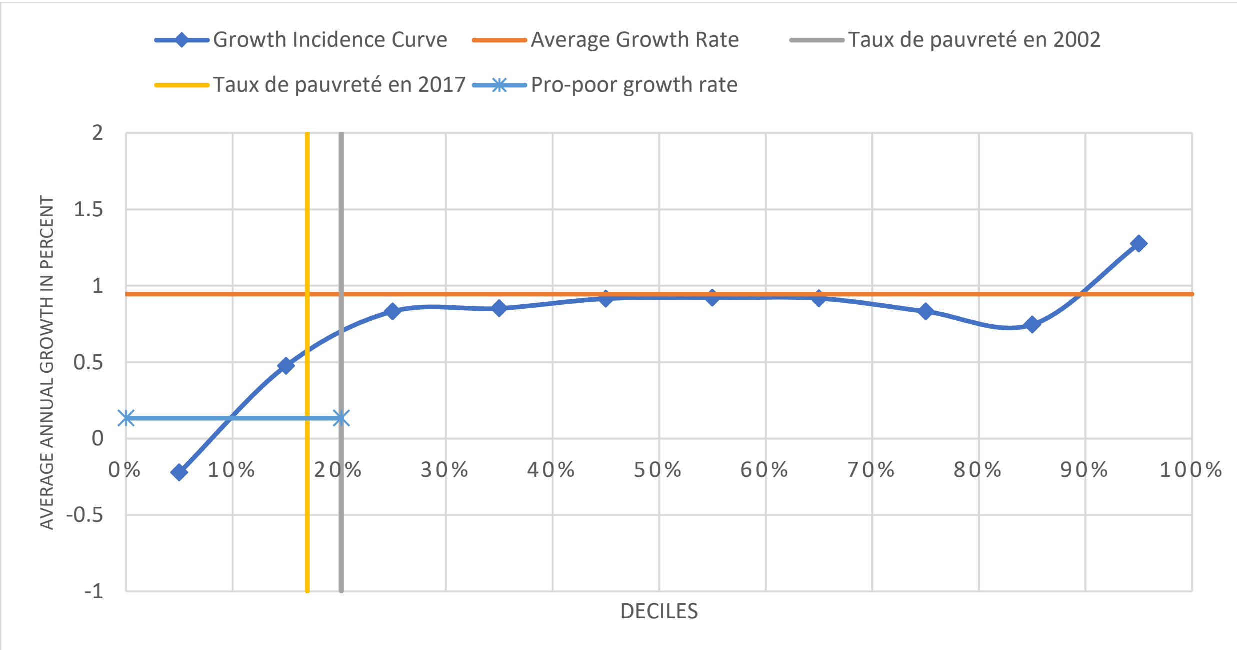
In addition, Djibouti's economic growth has not been distributive, which has resulted in increased inequality. The Gini index is estimated at 41.6. This is in line with the average for Africa, which ranges from 27.6 (Algeria) to 63.3 (South Africa) (UNCTAD, 2021)[7]. There are significant disparities between the capital and the interior regions. In 2021, extreme poverty reached 62.6 percent in the interior regions and 11.4 percent in the capital, a difference of 51.2 percentage points, compared to 45 percentage points in 2017. Poverty and growing inequality are central challenges for sustainable development in order to achieve SDG1 in Djibouti. They constitute vulnerabilities for social cohesion in a region riddled with socio-political tensions that accentuate and exploit these socio-economic differences[8].

Figure 2 shows the growth incidence curve for Djibouti. When the curve is upward-sloping, the growth of the first decile of the income distribution is lower than the growth of the last decile. The consumption of the poorest 5 percent declined between 2002 and 2017. Although the consumption

[6] Based on the adjusted global poverty lines, 43.8 percent of the population were living below the adjusted poverty line of $3.65 per day, and 19.1 percent below the poverty line of $2.15 per day in 2017 (World Bank World Development Indicators).
[7] A Gini index of 0 represents perfect equality, while an index of 100 implies perfect inequality.
[8] Unpublished internal study

of the poorest 10 percent increased, growth was very low (less than 1 percent) and the curve progressively increases with each decile.

Figure 2: Djibouti Growth Incidence Curve, 2002-2017



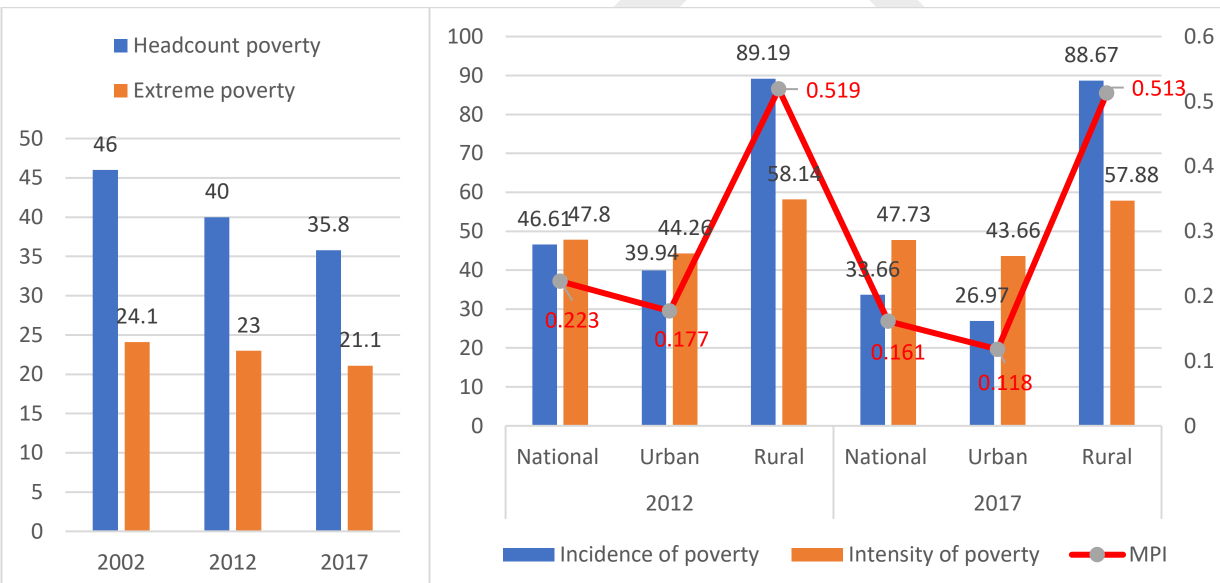
Source: UNCTAD, based on the World Bank's PovcalNet database.

Djibouti is one of the most urbanized countries in Africa with 85 percent of the population living in cities. The national population is concentrated in Djibouti City, which is home to 76 percent of the country's population. Outside the city of Djibouti, 63 percent of the population is rural; none of the country's five regional capitals has a population exceeding 30,000 inhabitants. Although the population in rural areas is only about 15 percent of the total population, rural areas are home to 45 percent of the people living in extreme poverty and with very limited access to public services such as electricity, water and sanitation (Republic of Djibouti, 2021a).

Overall, 80 percent of the rural population faces multidimensional poverty, compared to less than 20 percent in urban areas. Rural employment is particularly low, with only 16.8 percent of the working-age population, compared to 24.4 percent in Djibouti City and 27.8 percent in other cities. Unemployment affects more women (63.4 percent) than men (38.7 percent) throughout the country and is extremely high among youth (15-24 years) at 87.5 percent in Djibouti City (Republique de Djibouti, 2021a) (see also Section 3.1.3). According to the "Djibouti ICI" plan, one-fifth of the population, particularly in rural areas, lived in extreme poverty.

Another indicator of poverty incidence is the Multidimensional Poverty Index (MPI), which includes questions regarding standard of living, health and education[9]. With an incidence of 33.66 percent and an intensity of 47.73 percent, the MPI was 0.161 in 2017. As Figure 3 shows, the national incidence of multidimensional poverty has decreased from 46.61 percent in 2012 to 33.66 percent in 2017, which means that fewer citizens are in multidimensional poverty: this leads to a decrease in the MPI from 0.223 to 0.161 (UNDP, 2010). Moreover, multidimensional poverty, like income poverty, is mostly a rural phenomenon. Poverty is significantly higher in rural areas compared to urban areas. The incidence of multidimensional poverty in rural areas is four times higher than in urban areas (51.3 percent versus 11.8 percent) in 2017, as shown in Figure 3.

Figure 3: Income poverty indicators and multidimensional poverty indicators in percentage



Source: République de Djibouti (2022), Examen National Volontaire (National Voluntary Exam).

In Djibouti City, poverty and inequality are unevenly distributed across the city. The Balbala district is home to 60 percent of the capital's population and 76 percent of those living in extreme poverty. Labor market participation is lower and unemployment is higher (Republic of Djibouti, 2021) (Section 3.1.3). In order to put an end to this situation, which leads families into both monetary and multidimensional poverty, the Government of Djibouti has undertaken several actions to support households. These build on the existing social protection infrastructure, which has gradually expanded since the National Social Protection Strategy 2018-2022, and brought several social protection schemes under one unified platform for the management and coordination of social assistance for the first time (Republic of Djibouti, 2021a). In addition, to better address poverty, the Ministry of Social Affairs has created a Register of Poor Households: as of August

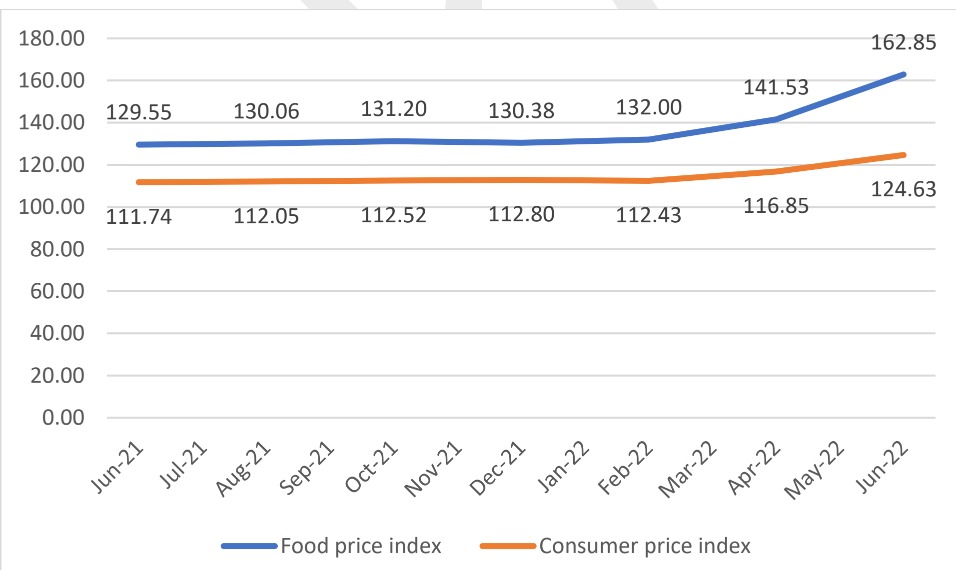
[9] The Multidimensional Poverty Index (MPI) is a statistical indicator developed in 2010 by the Oxford Poverty and Human Development Initiative (OPHI)

2021, the register lists information on 42,000 households, exceeding the target of 20,000 households. The collection of biometric data about these households has recently been launched (World Bank, 2021).

Price volatility

The post-crisis inflationary surge in 2008 to 8.7 percent was a disaster for Djiboutian consumers accustomed to stable prices and an inflation barely exceeding 3 percent. After a stagnation of consumer prices between 2013 and 2018, prices have increased again with an inflation of 3.3 percent in 2019 and 2.9 percent in 2020. In 2021 and 2022 Djibouti experienced very high levels of inflation. The Consumer Price Index (CPI) rose sharply from 112 in June 2021 to 125 in June 2022 (base 100 in 2013). Especially the food price index increased from 130 to 163 (Figure 4). For example, the price of flour increased by 12 percent between June 2021 and 2022, oils by 21.5 percent, fresh vegetables, fruit and roots by 87.5 percent, and tubercles and plantain by 126.7 percent (INSTAD, 2022). This sharp increase is mainly due to the decline in the supply of fruits and vegetables to the Djibouti market from Ethiopia (INSTAD, 2022). Such disruptions in supplies of fruit and vegetables, coupled with reduced income, low access to public services and limited savings, have severe implications for households. As a result, up to 69 percent of the households covered by the World Bank/INSD survey reported not having the resources to support themselves for another month. Female-headed households struggle more than male-headed households (Republique de Djibouti, 2022). Between June 2022 and June 2023, the CPI and the food price index slightly fell to 118 and 144, respectively (INSTAD, 2023).

Figure 4: Evolution of the Consumer Price Index (CPI) Index Base 100 in 2013



Source: INSTAD, 2022, http://www.instad.dj/IPCJUI2022.pdf

Note: the global index includes all products

The Republic of Djibouti, thanks to the currency board system and the absence of any monetary creation, is essentially subject to imported inflation, depending on the dollar, the currency to which the Djibouti Franc (DJF) is pegged, and this since 20 March 1949. The exchange rate between the Djibouti franc and the US dollar has not changed since October 1973, and amounts to 177.721 DJF for one dollar[10].

2.2. Structural transformation and trade

Structural transformation

At first glance, the distribution of the GDP by major sectors looks more like that of a developed country than that of an LDC. The tertiary sector accounts for 80 percent of the GDP, the secondary sector for 17 percent and the primary sector for 3 percent. Djibouti's economy is based on international maritime trade (handling nearly 90 percent of Ethiopia's exports, which accounts for nearly 80 percent of Djibouti's port activity). Ports and free trade zones account for about 35.5 percent of Djibouti's GDP. Although container shipping dropped significantly during the lock-down period, trade has since returned to a positive trend in the third quarter of 2020.

Djibouti's economic growth is driven primarily by foreign investment, port and transport activities, telecommunications, and construction. In recent years, the government has implemented large-scale investments to develop infrastructures for transport and logistics. Combined with business climate reforms, this development strategy has fueled strong growth and positioned Djibouti to become a regional trade and logistics hub. However, with investment concentrated in capital-intensive activities that rely heavily on highly skilled foreign labor, job creation and the benefits from structural transformation have been limited. The most transformative factors have been accomplished in the field of state-of-the-art infrastructures such as the Djibouti-Addis Ababa railroad, ports, and the creation of a 240-hectare free trade zone (inaugurated in 2018) that is on its way to becoming the largest on the African continent once it reaches a capacity of 4,800 hectares (Republique de Djibouti, 2021a).

However, at the end of the SCAPE implementation period, economic growth, which had reached 6.6 percent in 2019, did not create enough jobs to sufficiently reduce unemployment and poverty as expected. The economic boom could not materialize in the face of high levels of poverty and unemployment. The unemployment rate was 48 percent, and it affected 70 percent of those under 30. Despite significant progress in terms of access to public services (electricity, water, education) and a reduction in extreme poverty, one-fifth of the population still lives in extreme poverty, with significant inequalities between urban and rural areas (IMF, 2019).

According to an estimate by the International Labor Organization (ILO), about 25 percent of the total workforce, including informal employment, works in the agricultural sector, 13 percent in the

[10] https://banque-centrale.dj/index.php/bref-historique/

industrial sector, and 62 percent in the tertiary sector. The services (tertiary) sector has always been the main sector, but it has been gaining more importance since 1991 (42 percent of jobs in the services sector in 1991). Public sector jobs constitute about half of total formal employment, indicating that the economic model based on the port infrastructure and associated services generates few jobs for Djiboutians in the private sector.

There are two labor markets, the formal and the informal. Informal work is important and represents about 43 percent of all employment, 80 percent of which is concentrated in low-skilled activities in the service sector. It is estimated that the informal sector accounts for 15 percent of the national GDP. Djibouti City is home to 75.1 percent of all informal production units, compared with 14.4 percent in other urban areas and 10.5 percent in rural areas. The majority of production units in the informal sector are subsistence businesses (Republique de Djibouti, 2021a).

Productive Capacities Index

Productive capacity development operates both within firms/sectors, as the profit-investment nexus promotes capital deepening and productivity gains, and across sectors, as capacity acquisition, itself dependent on the existing pattern of production, paves the way for the emergence of new products and higher value-added activities (UNCTAD, 2020a). UNCTAD has developed a composite index to capture this articulated process of expanding a country's productive capacities (box 1).

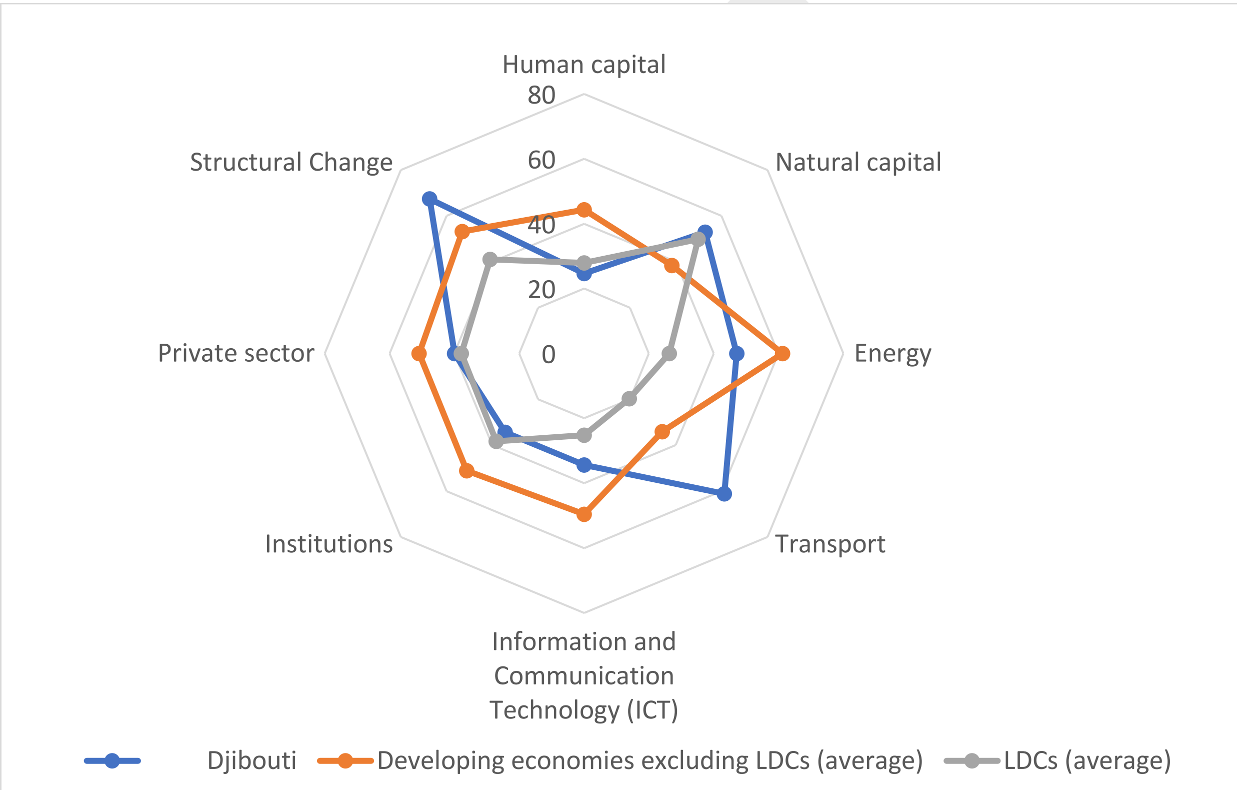
Box 1. UNCTAD Productive Capacities Index

The UNCTAD Productive Capacities Index (PCI) is the first comprehensive attempt to measure productive capacities in all economies, LDCs and non-LDCs, developed and developing. The index builds on the conceptualization of productive capacities defined as "the productive resources, entrepreneurial capabilities and production linkages which together determine the capacity of a country to produce goods and services and enable it to grow and develop" (UNCTAD, 2006).

As such, the PCI is a composite index of 46 indicators under eight components, namely, natural capital, human capital, energy, transport, ICT, institutions, structural change and the private sector. A detailed description of the methodology of the construction of the PCI is provided in (UNCTAD, 2020b). For the purpose of this report, it suffices to note that – after imputation and/or forecasting of missing data as required – principal component analysis is applied to reduce the dimensionality of the data. The resulting factor weights are then used in the weighting of the individual indicators to construct each PCI component, which is subsequently standardized using the maximum and minimum normalization. The overall PCI score is finally obtained as a geometric mean of the eight components, whereby the geometric mean is chosen to reduce the level of substitutability across components. The PCI scale, both for the aggregate index and its components, ranges from 0 to 100, with 100 being the best score.

An analysis of the sub-components of the composite index gives a first perspective on the strengths and weaknesses of productive capacities of Djibouti and its sustainable development. Figure 5 shows that the productive capacities of Djibouti are superior to those of LDCs and developing economies without LDCs (average) in terms of transport and structural change thanks to the contribution of services to GDP. On the contrary, it performs weaker than developing economies in terms of energy and information and communication technologies. Another impediment to development is the country's poor record in the dimension of private sector, human capital and institutions. The human capital and institutions index is lower than the LDC average.

Figure 5: Components of the Productive capacity index for Djibouti and related benchmarks



Source: UNCTAD secretariat calculations, based on data from UNCTADStat [accessed July 2023]

Trade

Djibouti is heavily dependent on imports. Between 2010 and 2022, imports of goods grew from $374 million to $5.4 billion (UNCTADStat). There is no official data available on Djibouti's exports. The last official notification to UN COMTRADE was in 2009 and indicates an export value of $364 million and re-exports for a value of $206 million[11]. Despite uncertainties due to lack of data, mirror trade data reported by the ITC Trade Map for the year 2021 (based on UN COMTRADE) suggest that the main exports are animal or vegetable fats (about $185 million), inorganic chemicals ($56 million) (i.e., chlorides), livestock ($22 million), and editable vegetables ($11 million). The top five markets are Ethiopia (25 percent), China (22 percent), the United States (19 percent), India (8 percent), and Saudi Arabia (8 percent).

On the other hand, the country is heavily dependent on commercial activities related to its port facilities that serve the countries of the region. Commercial services exports ($552 million in 2021) are completely concentrated in the transport sector ($552 million). In 2020, transport services accounted for 95 percent of commercial services, followed by travel services (5 percent). However, Djibouti also records a large share of its exports of public administration goods and services, n.i.e.. [12] ($307 million) (Figure 6), heavily dependent on foreign military bases in Djibouti. Among other things, exports of telecommunication, computer, and information services increased between 2010 ($7.4 million) and 2019 ($113 million), which signifies some diversification of services (UNCTADStat). For example, the Djibouti Data Center, established in 2013 by a group of local and international investors, is the leading operator in East Africa with access to all major international fiber optic systems connecting Europe, the Middle East, and Asia-Pacific. In total, Djibouti exported services worth $1.15 billion in 2019 and $0.9 billion in 2020.

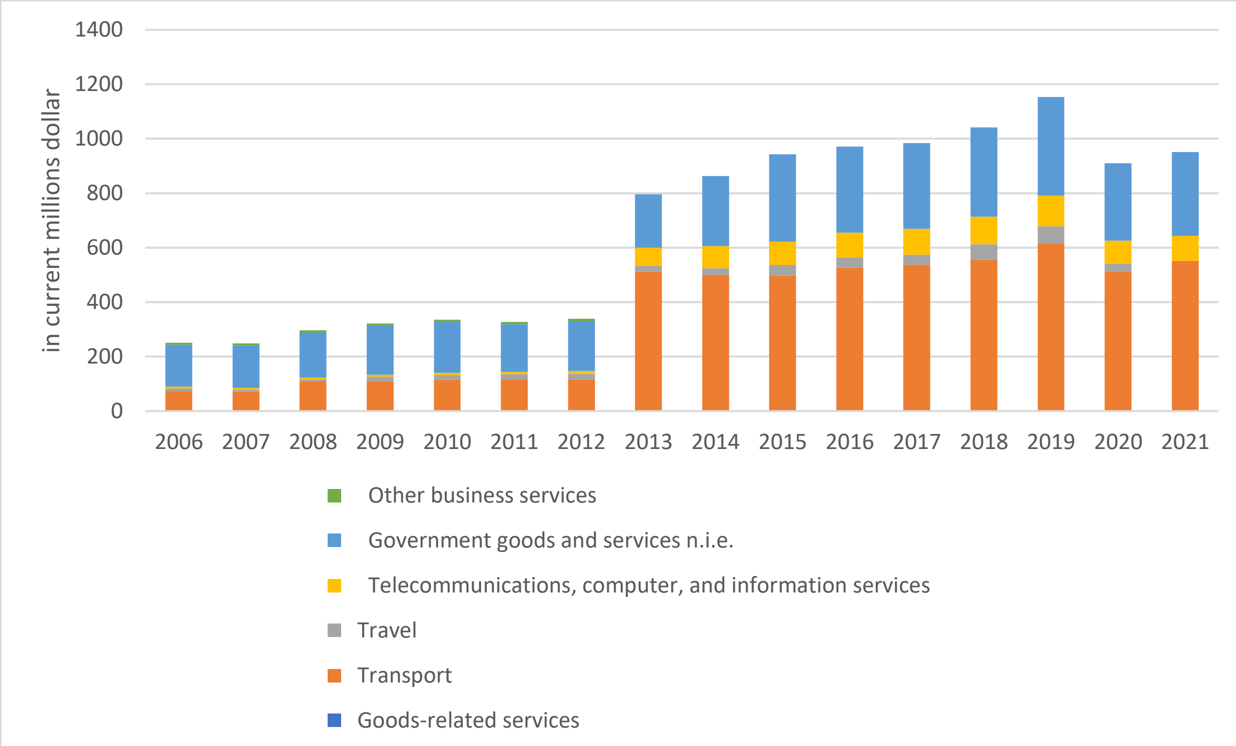
Djibouti does not officially have a customs tariff. However, in terms of its operation, the domestic consumption tax is very similar to a customs tariff because the tax is levied on all goods imported and consumed in the country. The simple average of these rates was 18.2 percent in 2022, as opposed to 21 percent in 2013. The tariff on non-agricultural goods is higher (simple average of 19 percent) than on agricultural goods (simple average of 11.6 percent) (WTO, 2022).

Indeed, Djibouti's 80 percent service-based economy is dependent on cross-border trade and exports of goods from Ethiopia, all of which transit through the Port of Djibouti. Thus, a decline in Ethiopian exports could lead to a decrease in transit, a slowdown in activity along the cross-border corridor, a drop in port activities, and indirectly a lower level of foreign exchange earnings, government revenues, and household income (see Section 3 for a detailed discussion on vulnerabilities).

[11] The largest value of re-exports in 2009 was reported in the trade categories: rubber ($45 million), dairy products ($29 million), vehicles ($23 million), electric machinery ($13 million) and animal or vegetable fats ($13 million).

[12] Government goods and services n.i.e. consist of: (a) goods and services provided or received by enclaves such as embassies, military bases and international organizations, (b) goods and services purchased from the host economy by diplomats, consular staff and military personnel posted abroad, as well as their dependents, (c) services provided or received by government agencies and not included in other categories of services (UNCTADStat)

Figure 6: Djibouti, export of services



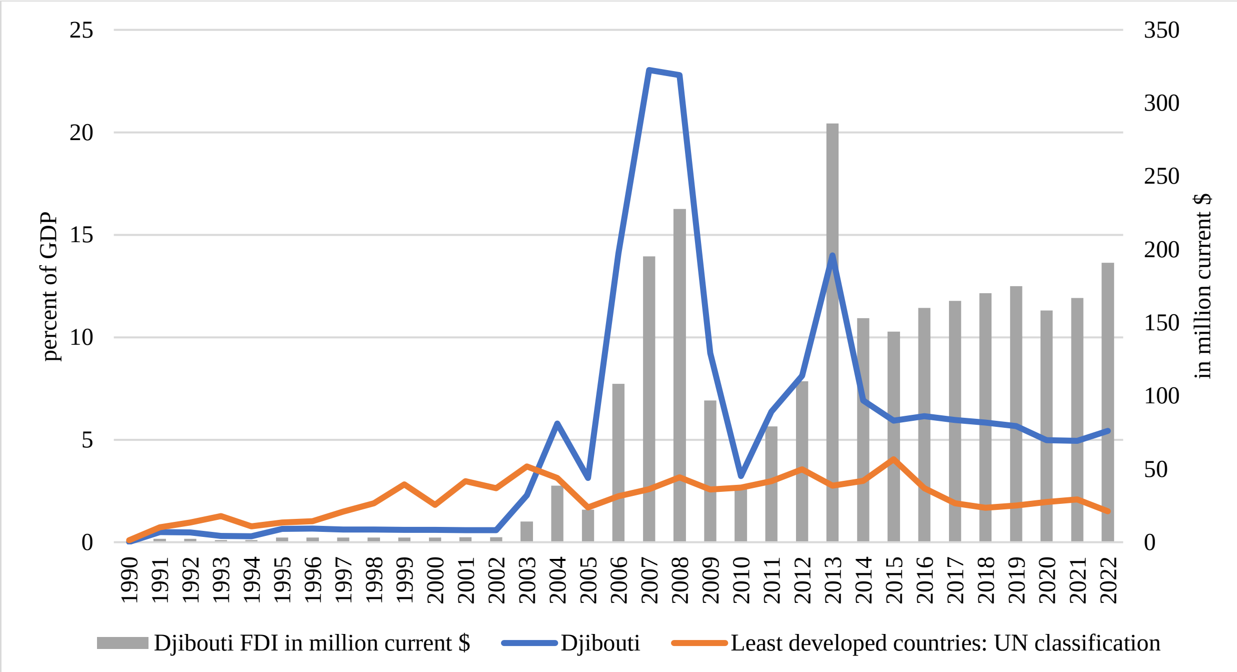
Source : UNCTAD based on the UNCTADstat database [accessed November 2023].

Investment

Thanks to a its climate of peace, its political stability, and its geopolitical position, Djibouti attracted nearly $1 billion in foreign direct investment (FDI) over the 2015-2020 period, with the main investors in the services sector coming from China, the Gulf countries, and Ethiopia.

Because of the COVID-19 pandemic, foreign direct investment flows declined from $175 million in 2019 to $158 million in 2020, but they recovered and amounted to $191 million in 2022 Figure 7 shows that flows were highly volatile since 2005 with a peak of 23 percent of GDP in 2007 and 2008, 14 percent in 2013, and an extreme low point of 3.2 percent in 2010 and 5 percent in 2020. However, as a percentage of GDP, FDI in Djibouti is higher than the LDC average.

Figure 7: Foreign direct investment (FDI) in $ millions and as a percentage of GDP, Djibouti and LDC average, 1990-2022



Source: Prepared by the UNCTAD secretariat on the basis of data from the World Bank's World Development Indicators database [accessed November 2023].

The United Arab Emirates, Kuwait, and Qatar, as well as the United States are the top countries of origin, accounting for 40 percent, 21 percent, 21 percent, and 7 percent, respectively, of greenfield investments between 2003 and 2015.[13] Djibouti is part of nine bilateral investment treaties (with Egypt, Malaysia, Switzerland, India, China, France, Kuwait, the Islamic Republic of Iran, and Turkey) (WTO, 2022).

In 2016 alone, Djibouti made four capacity building investments worth $235 million. In the same year, combined financing flows in trade and financial services totaled $3 billion (African Development Bank, 2022a). In 2017, Djibouti opened three ports in the course of two months. The multipurpose Port of Doraleh was completed in May 2017 and has the capacity to handle 8 million tonnes of bulk and containerized cargo. The $64 million Ghoubet Port was developed to facilitate salt exports. The port has an operational capacity of 5 million tonnes per year. The railroad to the Port of Mekele Tadjoura, in the north of the country, is still in the planning stage. The railroad will facilitate the export of potash from Ethiopia via the new Port of Tadjourah. The $90 million Port of Tadjourah has an annual capacity of 4 million tonnes.[14]

In terms of destination sectors greenfield investment data indicate that between 2016 and 2020, the tertiary sector attracted almost 100 percent of investment. The transportation and storage sector

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[13] https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/fragility-resilience/promoting-private-investment-in-transition-countries/the-horn-of-africa-opportunity/country-profiles/djibouti

[14] https://www.presidence.dj/article/la-ceremonie-dinauguration-du-port-de-tadjourah-placee-sous-le-haut-patronage-du-president-de-la-republique-372; https://oxfordbusinessgroup.com/news/djibouti-ouvre-trois-ports-en-deux-mois

received 51 percent ($371 million) of total investment (Table 1). Next, the power sector (electricity, gas, steam and air conditioning supply) attracted 23 percent and the information and communication sector accounted for 14 percent of greenfield investments. On the one hand, Djibouti's economy is highly dependent on foreign investment. Between 2005 and 2020, FDI contributed an average of 9 percent to GDP. The LDC equivalent was 2.6 percent on average. On the other hand, investment is highly concentrated from a few countries and in few sectors, which makes Djibouti vulnerable to exogenous shocks (see Sections 3.4 and 3.5).

Table 1: Greenfield investments

	2016	2017	2018	2019	2020	Total 2016-2020
Total (in millions)	**236.9**	**9.5**	**185.8**	**181.3**	**111.4**	**724.9**
Primary	-	-	-	-	-	**0 percent**
Manufacturing	1.4	0.0	0.0	0.0	0.0	**1 percent**
Manufacture of chemicals and chemical products	1.4	0.0	0.0	0.0	0.0	**0 percent**
Tertiary	98.6	100.0	100.0	100.0	100.0	**99 percent**
Transportation and storage	78.4	0.0	100.0	0.0	0.0	**51 percent**
Accommodation and food service activities	10.3	0.0	0.0	0.0	0.0	**3 percent**
Administrative and support service activities	0.0	0.0	0.0	1.0	0.0	**0 percent**
Education	0.0	0.0	0.0	0.0	6.2	**1 percent**
Electricity, gas, steam and air conditioning supply	0.0	0.0	0.0	93.7	0.0	**23 percent**
Financial and insurance activities	0.0	100.0	0.0	5.2	0.0	**3 percent**
Information and communication	0.0	0.0	0.0	0.0	93.8	**14 percent**
Professional, scientific and technical activities	9.8	0.0	0.0	0.0	0.0	**3 percent**

Source: UNCTAD based on the fdimarkets.com database

2.3. Regional dynamics

The Republic of Djibouti is one of the smallest countries in Africa, but its geographic position in a region of political instability and insecurity has earned it a significant amount of interest from major foreign powers. As the main gateway to and from Ethiopia's trade, Djibouti is of inestimable importance to its neighboring country, which represents the powerhouse of the Horn of Africa - both in terms of its demographic size and its natural resources. Since the 19th century, Djibouti and the coast of the Horn of Africa have been of great interest to European countries seeking access to the resources of Africa. After the opening of the Suez Canal, the geostrategic importance of the Red Sea is undeniable and the securing of one of the most important maritime routes in the world, which passes through the Bab el-Mandeb Strait, located between Yemen and Djibouti, has become the geopolitical objective of world powers. A pole of stability in a turbulent region, the former French Territory of the Afars and the Issas (FTAI) was one of the last countries to gain its independence on the African continent in June 1977, after a 115-year French presence on its territory. Today, its strategic position at the entrance to the Bab el-Mandeb is evidenced by the presence of five foreign military bases (France, United States, Italy, China and Japan). The country is also home to the European Union's *Atalanta* forces, which Djibouti has hosted as part of the fight against piracy and the securing of maritime routes, but also to ensure its own security through the defense agreement that exists between France and the Republic of Djibouti. The Gulf countries have also recognized the strategic relevance of the country. The increased international presence shows that Djibouti has succeeded in consolidating the principle of a security pole by actively pursuing its diplomacy for peace and stability, both politically and militarily, for example through its reconciliation, in September 2018, with Eritrea. Djibouti actively participates in the African Union peacekeeping mission in Somalia as well as in the UN missions in the Central African Republic and the Democratic of the Congo[15].

Djibouti benefits greatly from regional integration with an open economy focused on activities such as port services, logistics, and related services to neighboring countries. As a member of the Common Market for Eastern and Southern Africa (COMESA) and the Intergovernmental Authority on Development (IGAD), the country has made harmonization efforts, including the introduction of value added tax (VAT) in 2009, the implementation of regional motor vehicle insurance, the COMESA customs guarantee, and of course, the African Continental Free Trade Area (AfCFTA) agreement (République de Djibouti, 2021a).

The launch of the AfCFTA therefore offers a unique opportunity to promote inclusive growth and accelerate the achievement of the 2030 Agenda for Sustainable Development and the African Union's Agenda 2063. According to an UNCTAD estimate (2021), the AfCFTA could unlock the continent's untapped export potential of $21.9 billion. It indicates that an additional $9.2 billion in export potential can be realized through partial tariff liberalization under the AfCFTA over the next five years. To realize this potential, various intra-African non-tariff barriers, including costly non-tariff measures, deficiencies in infrastructure and business information gaps, must be removed and addressed. This requires joint efforts under the AfCFTA. Long-term cooperation in terms of investment and competition policies will be essential to overcome market dominance by a few players and to reduce structural and regulatory barriers to market access.

Djibouti validated its National Strategy for the AfCFTA in May 2022. The strategy emphasizes the importance of trade and free trade, which were already central to the "Djibouti ICI" National Development Plan 2020-2024. The five sectors prioritized in the strategy are: tourism, transportation, communication, telecommunications, and the financial sector (UNECA, 2022).

2.4. Economic challenges related to the pandemic and other external shocks

In 2020, Djibouti's macroeconomic situation was seriously affected by the COVID-19 pandemic and the Ethiopian crisis. Djibouti's economy is based on international maritime trade, which handles nearly 90 percent of Ethiopia's foreign trade and accounts for nearly 80 percent of Djibouti's port activity. Ports and free trade zones account for about 35 percent of Djibouti's GDP.

[15] Djibouti is the third largest troop contributor to the African Union Mission in Somalia (AMISOM). 35 Djibouti military/UPFs serve in the United Nations Organization Stabilization Mission in the Democratic Republic of the Congo (MONUSCO) and the United Nations Multidimensional Integrated Stabilization Mission in the Central African Republic (MINUSCA)

As a result of COVID-19, the decline in production due to supply and demand shocks and the resulting drop in tax revenues have led to budgetary pressures and forced a shift in expenditure and official development assistance. Although the sanitary impact of the COVID-19 pandemic was relatively limited, its economic and social consequences were significant, due to the country's social and economic structure, the poverty profile and incidence, as well as its strong integration into the global economy. The tertiary sector, the country's main job generator, has been the most affected: the activities most severely hit by the closure of the borders and the lockdown measures are mainly air and road transport, tourism and retail trade. For instance, the tourism sub-sector has seen a reduction of more than 50 percent in the number of travelers hosted: from 167,474 in 2019 to 83,737 in 2020 (République de Djibouti, 2021a).

According to the United Nations Djibouti (Nations Unies Djibouti, 2021), the impact of the COVID-19 pandemic on the economy has been limited due to the continued satisfactory level of activity in the free trade zone, trade with Ethiopia, and the telecommunications sector in the last quarter of 2020. In the medium term, Djibouti is expected to return to pre-pandemic levels of growth driven by the recovery in general activity and global demand. However, the country could face the adverse effects of the Ethiopian crisis, which would entail a drop in demand from this trading partner. After exceeding an annual average of 6 percent for the past two decades, the GDP growth rate has declined significantly in 2020 as a consequence of the pandemic. First, the decline in port activities during 2020 due to the pandemic led to a drop in economic growth from 7.5 percent in 2019 to 1.2 percent in 2020, with a considerable impact on tax revenues and public debt (the latter estimated at 72.9 percent of GDP at the end of 2020) (Nations Unies Djibouti, 2021).

Second, the COVID-19 pandemic has exacerbated the structural weaknesses of the health system and the vulnerability of certain segments of the population, who are unemployed or work in the informal sector without health insurance coverage.

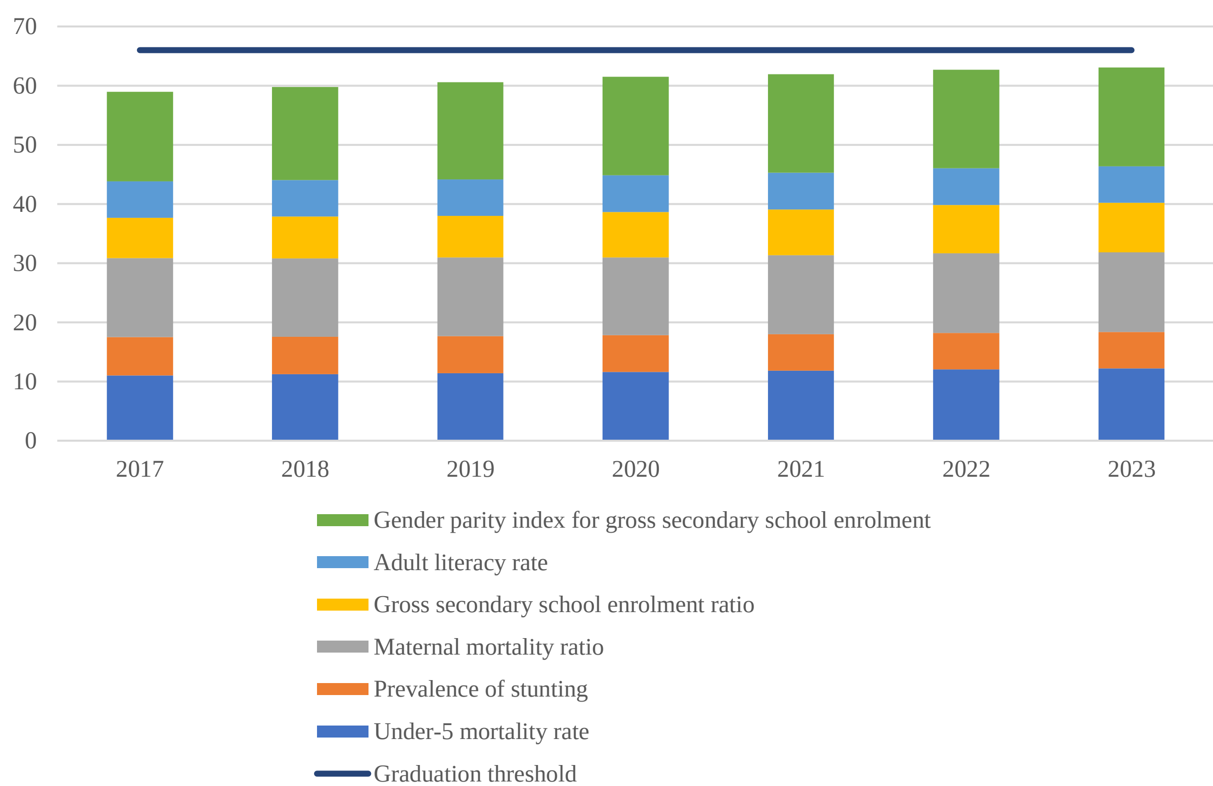
The pandemic has also had a negative impact on the country's public finances. While budget revenues fell by 0.8 percent of GDP, current expenditures increased by 0.3 percent of GDP, resulting in a deterioration of public finances in 2020. The increase in public spending is mainly the consequence of fiscal measures related to actions for increased social protection combined with the additional costs as a result of the COVID-19 pandemic. COVID-19-related spending amounted to 2.7 percent of GDP, concentrated on: i) increased health spending (FDJ 5 billion or +0.8percent of GDP); ii) emergency spending for companies (FDJ 3.5 billion) and households (FDJ 4 billion); iii) an allocation for strategic food security reserves (FDJ 2 billion) and an envelope to update poverty mapping (FDJ 0.2 billion). The fiscal balance thus deteriorated from -0.6 percent to -2.2 percent (Republique de Djibouti, 2021a). According to the World Bank (Banque Mondiale, 2021), even though only 20 percent of Djiboutian families work less than before the pandemic, Djiboutian workers, on average work more but for less pay. In addition, soaring food prices, largely caused by the conflict in Ukraine (as discussed in Section 2.1 of this document) are putting pressure on households that spend the largest share of their income on food. In addition, higher freight rates due to airspace restrictions, for example, can also accelerate price increases.

3. Areas of Vulnerability

3.1. People

Weaknesses in human capital are manifest in areas such as education, health, employment and social protection, and gender equality. According to the latest 2023 update on the Human Assets Index (HAI), Djibouti has a score of 63.06, whereas 66 is needed to reach the reclassification target. Thus, the score is at 95.5 percent of the LDC reclassification threshold. The human capital indicators reveal that Djibouti is most vulnerable when it comes to low literacy rates, low school enrollment and high prevalence of malnutrition (Figure 8).

Figure 8: Human Assets Index (HAI)



Source : UNCTAD based on the LDC indicators developed by the CDP Secretariat [accessed November 2023].

Similarly, the Human Development Index (HDI), calculated according to the life expectancy rate, the average duration of schooling and the GDP per capita, shows a certain gradual evolution for

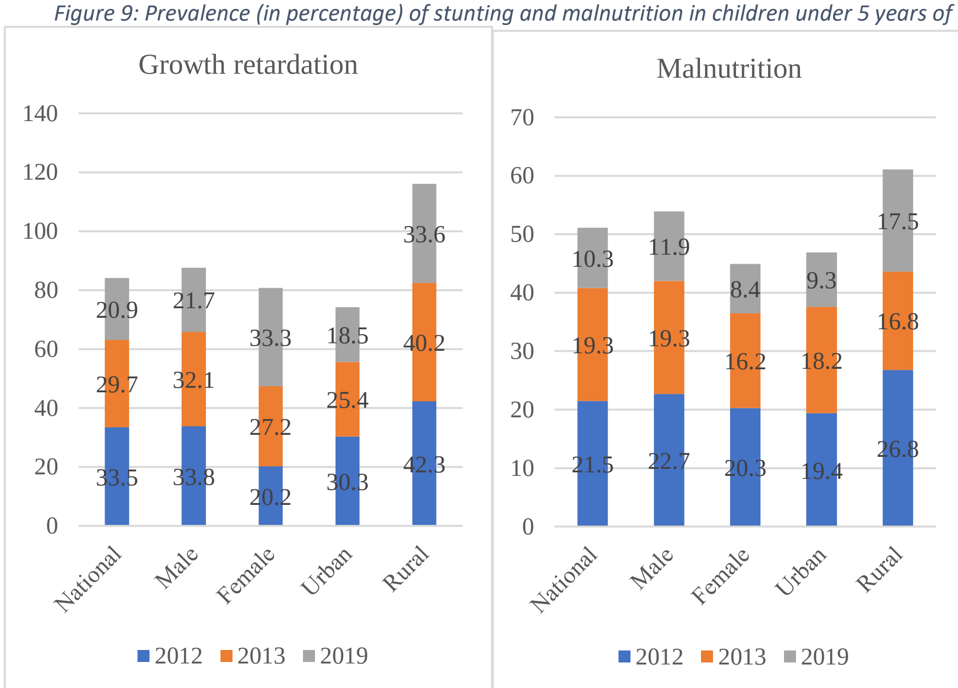
Djibouti: it went from 0.36 in 2000 to 0.509 in 2021, but lags behind the average of Arab countries (0.705). In 2021, the country is ranked 171st out of 189 countries in the HDI (UNDP, 2020), just ahead of Sudan and Ethiopia, which are 172nd and 175th respectively.

3.1.1. Health

In terms of health and well-being, despite the remarkable progress made since 2010, inequalities persist with regard to access to health care. The prevalence of malnutrition and high mortality rates are one of Djibouti's greatest vulnerabilities when it comes to its human capital. In terms of food security and nutrition, the prevalence of malnutrition has been declining since the beginning of the 21th century, but it remains very high. According to SMART (Standardized Monitoring and Assessment of Relief and Transition) survey data of March 2019, the prevalence of malnutrition reaches 19 percent in children under 5 years old, against 10.3 percent suffering from severe malnutrition. According to the 2021 Integrated Food Security Phase Classification (IPC) figures, approximately 17 percent of the population is acutely food insecure (IPC, 2021).

The structural problem of food security is mainly due to the low level of agricultural production, which covers only 10 percent of the needs, and the country is therefore dependent on food imports. The prevalence of stunted growth among children under 5 years of age has dropped by 12.6 percentage points over an eight-year period. The Ministry of Health with support from development partners has initiated nutrition programs. As shown in Figure 9, progress has been made and the prevalence of stunting decreased from 33.5 percent in 2012 to 20.9 percent in 2019 with a slightly higher level among boys (21.7 percent) than for girls (20.2 percent). In addition, it is important to note that the situation in rural areas is very alarming when compared to urban areas. Indeed, in 2019, 33.6 percent of children in rural areas were suffering from stunting compared to 18.5 percent of those in urban areas. As for the prevalence of malnutrition (measured by the weight for height) among children under 5, it was reduced by 11.2 percentage points from 21.5 percent in 2012 to 10.3 percent in 2019. Malnutrition is slightly higher for boys (11.9 percent) than for girls (8.4 percent) and affects more children living in rural areas (17.5 percent) than in urban areas (9.3 percent) (République de Djibouti, 2022).

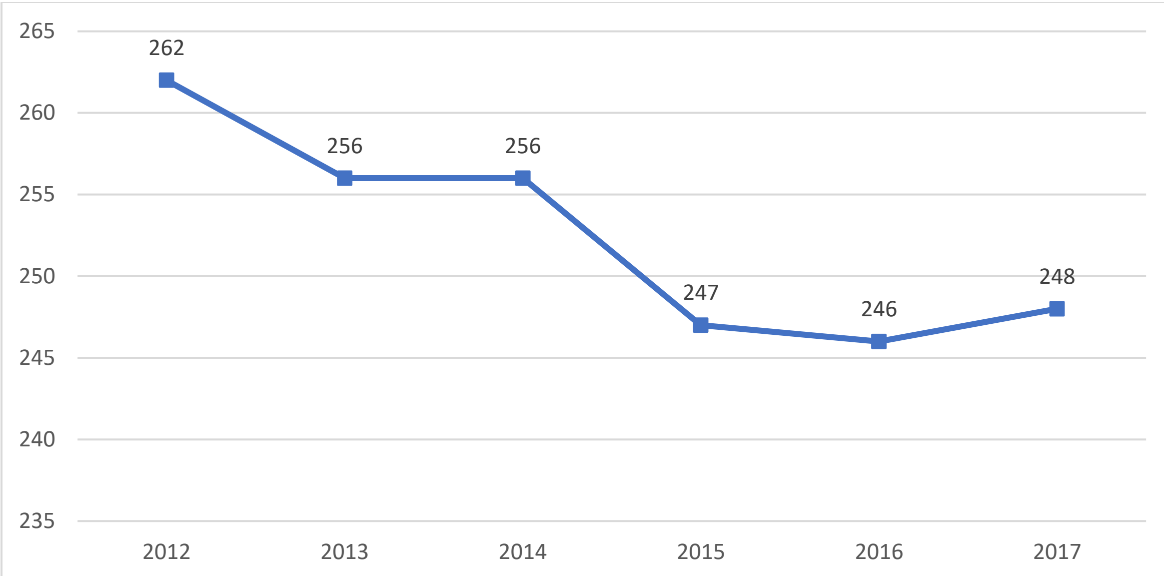
Figure 9: Prevalence (in percentage) of stunting and malnutrition in children under 5 years of age



Source : République de Djibouti (2022).

As a result, the under-5 mortality rate remains high at 54.1 per 1,000 live births despite strong progress since 2015 (65.6). Further, although a majority of women have access to basic health care, there are still unmet needs such as the demand for family planning. Maternal mortality remains high as shown in Figure 10 from the Voluntary National Review document presented in New York in July 2022.

Figure 10: Maternal mortality rate per 100,000 live births



Source : République de Djibouti (2022).

In addition, the battle against infectious diseases is far from won. HIV/AIDS affects the country as a generalized epidemic. Several hundreds of people die each year from tuberculosis and malaria cases are continually increasing. Achieving universal health coverage requires an efficient health system in all its components (République de Djibouti and Nations Unies Djibouti, 2018).

The current national health system is characterized by inadequate health infrastructure, poor primary care and hospital services. The fight against COVID-19, with an implementation cost of more than FDJ 4 billion, has led to the weakening of the health systems in Djibouti, as elsewhere in the world. The Ministry of Health's strategy seeks to address communicable and non-communicable diseases, including the three priority diseases (malaria, tuberculosis, and HIV). Djibouti benefits in this area from the support of the WHO through a cooperation strategy that contributes, among other things, to support mother/child health and to strengthen the health system according to the 2020-2021 response plan and the National Health Development Plan (République de Djibouti and Nations Unies Djibouti, 2018).

Finally, an important vulnerability factor to highlight on the economic front, but above all on the health front, is the consumption of khat. In spite of the fact that this substance reduces employability and negatively reflects on consumer productivity and despite low incomes, 20-30 percent of the family budget is reportedly used to buy khat just after food items. On average, between 3 and 7 hours are spent on the consumption of khat. It has a negative impact on the pace of work, concentration and financial resources of households (Banque Mondiale, 2011)

3.1.2. Education

Education has been compulsory for Djiboutian children aged 6 to 16 since 2000 with the law on the education system. The gross school enrollment rate is 76.4 percent in general middle school and 46 percent in general, technical, and vocational secondary school (ages 11-17) in 2020-2021 (Republique de Djibouti, 2021b). Estimates from the UNESCO Institute for Statistics also point to progress on education and suggest the gross secondary school enrollment rate increased from 39 percent in 2015 to 45 percent in 2022 although girls are slightly disadvantaged with 41.6 percent (2022), compared to 48.4 percent for boys.. Despite the progress recognized by the Committee on Economic, Social and Cultural Rights in terms of access to basic education, there is a social divide between urban and rural, sedentary and nomadic populations. Thus, access to education remains more difficult for children from families living in isolated rural areas and for nomads (Republique de Djibouti, 2022). Also, the challenge is less about accessibility than about quality. Djibouti also suffers from a striking delay in female literacy: the female literacy rate is currently 39.5 percent, compared to 60.1 percent for men. In terms of quality, learning outcomes are modest, and there is evidence that basic competencies are not achieved in the early years. The Common Country Analysis (Nations Unies Djibouti, 2021) estimates that the education and vocational training system is not yet sufficiently adapted to provide the competencies required for the growing development of the economy, especially to provide career opportunities for young Djiboutian professionals. Regions outside Djibouti are poorly integrated and interconnected to take advantage of the economic engine of the port and its associated services. Economic sectors are insufficiently open to competition and still dominated by monopolies and state-owned enterprises, which presents the risk of wealth accumulation and distribution among a small group. The efforts made in recent years to strengthen social protection for the most vulnerable and to open up the regions are encouraging (Nations Unies Djibouti, 2021).

The small size of the country in terms of its surface (23 000 km^2) and number of inhabitants (less than one million) and the high urban concentration of its population (around 75 percent) do not prevent the country from having outlying areas that are difficult to access and sparsely populated: the average population density on the territory of the Republic of Djibouti is only around 49 inhabitants per km^2 which is significantly lower than that of Ethiopia, for instance (126.5)[16]. However, rurality and low population density are serious obstacles to the development of education and, contrary to first appearances, Djibouti is not spared from them[17].

Language makes Djibouti a very special place. The republic has two official languages, French and Arabic, and two national languages, Afar and Somali. Other languages are spoken in Djibouti, such as Amharic. French is also the language of instruction, although it is not spoken by the majority of the population. As far as French is concerned, Djibouti is a linguistic isolate, since the closest French-speaking countries are Chad and the Central African Republic, more than 2,000

[16] https://atlasocio.com/classements/demographie/densite/classement-etats-par-densite-population-afrique.php
[17] Educational Master Plan 2021-2035

kilometers away. The education system is thus in a difficult linguistic position and is, so to speak, condemned to multilingualism or, at least, to an in-depth learning of several languages.

Djibouti is also an isolate of stability and security in a space marked by violence and conflict in Yemen, Somalia and Ethiopia, which has resulted in the arrival of refugees. This reality demands that school authorities be very careful with respect to their language policies, and that any incident that occurs in the school environment must be dealt with without delay[18].

An analysis of the United Nations in Djibouti (Nations Unies Djibouti, 2021) estimates that the most pressing cross-cutting challenges are the following:

1. Access to quality education and its relevance to the labor market
2. Job creation, especially for youth
3. Adaptation to climate change and management of the increased risks for the agro-pastoral population
4. Territorial inequalities, especially those of a socio-economic nature
5. Institutional capacity to ensure transparency, accountability and protection of vulnerable people
6. Access to quality health services

These challenges are closely interconnected and interdependent, and sustainable development policies and strategies therefore require intersectoral and concerted approaches. This joint analysis of the United Nations System will form the basis of the Cooperation Framework with the Republic of Djibouti.

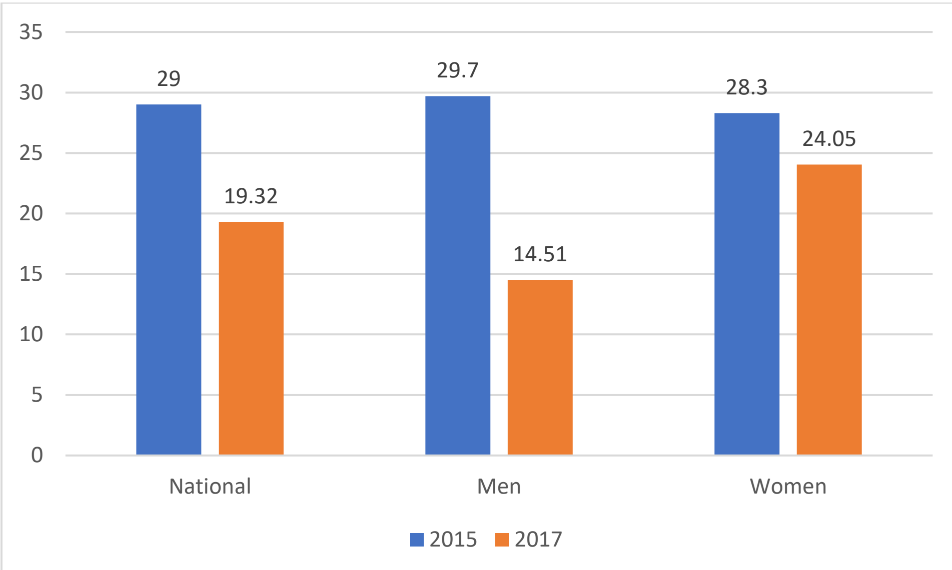
3.1.3. Employment and social protection

As already discussed, social disparities are strong. Unemployment at the national level, estimated at 47 percent, is the main source of poverty. More than 70 percent of the active population are young people, who are the main victims of unemployment. According to the Voluntary National Assessment (Republique de Djibouti, 2022), the proportion of young people (men and women aged 15-24) out of school and without employment or training decreased from 29 percent in 2015 to 19.32 percent in 2017. However, this decline is less significant for women: the proportion of young women not attending school, without a job or any training was 28.30 percent in 2015 and 24.05 percent in 2017 (Figure 10). This small improvement in opportunities for young people constitutes a social time bomb. Regarding access to employment and entrepreneurship, a widespread informal economy and very high level of unemployment demonstrate that a segment of the population is at risk of remaining excluded from progress. For a large part of the population that has already left the education system or that has never been enrolled in school, training and entrepreneurship opportunities seem limited and employment is not necessarily a way out of poverty. Informality and low productivity are prevalent. Highly skilled workers are concentrated

[18] Educational Master Plan 2021-2035

in the public sector, and low-skilled workers are overrepresented in the formal private sector, while the informal private sector is a major employer of people with limited education.

Figure 11: Proportion of youth (aged 15-24) not in enrolled in school and not employed or in training



Source: République de Djibouti (2022).

The Djibouti National Development Plan 2020-2024 (Republique de Djibouti, 2021a) notes that it is important to put in place a strategy that promotes labor-intensive jobs to ensure the employability of individuals lacking advanced skills (unskilled labor) and that undertakes investments in basic social infrastructure such as the rehabilitation of roads, highways, schools and health facilities.

Creating more decent jobs requires a more integrated and diversified economy that allows the private sector to play a leading role in the country's economic growth (see Section 4). On the other hand, it requires the development of human capital in terms of quality education for all and the acquisition of the necessary skills for the ambitions of a regional economic hub. To meet these requirements, the vocational training sector should have the capacity to train the majority of young people after their basic education. This will require equipping the relevant departments with the necessary institutional, technical and logistical capacities. As for the existing labor market information system, it is essential that it will be upgraded from its current embryonic level to a level that allows for the regular execution of surveys and the dissemination of data for both employers and job seekers (Nations Unies Djibouti, 2021).

3.1.4. Gender equality

In 2002, the Ministry in charge of the Promotion of Women, Family Welfare and Social Affairs (created in 1999) developed the National Strategy for Women's Integration and Development (SNIFD). This strategy focused on four priority areas, namely decision-making, health, education and the economy. This strategy was replaced in 2011 by the National Gender Policy 2011-2021

(NGP). Analysis of the gender situation in Djibouti shows an unequal status of women and men in households and in society that restricts women's educational opportunities, limits their ability to make decisions and participate in community life with equal opportunities (World Bank, 2021).

There is a general lack of reliable data and statistics in Djibouti, and sex-disaggregated data is even less available. Data is sometimes created as part of development programs and projects. These data are limited in terms of coverage and time, as they are project specific and not necessarily replicated in another project or in general. As a result, the overall picture of the situation of women is unclear, the monitoring of actions is complex and the impact is difficult to measure. This does not allow for a systematic analysis of gender issues. For example, Djibouti is one of three countries not included in the Africa Gender Index due to lack of data (World Bank, 2021).

Approximately 47 percent of the population are women. The population is also characterized by extreme youth. Young people under the age of 25 make up 55.4 percent of the population, and the proportion of women of childbearing age (12-49 years old) is estimated at nearly 53 percent (World Bank, 2021).[19] In terms of employment, women constitute only 37 percent of the labor force. According to the EDAM-IS (Djibouti Household Survey for Social Indicators) 2017, the unemployment rate is 38.2 percent for women, compared to 23.1 percent for men (Table 2). Gender differences are also significant for youth (57.4 percent of men are unemployed, compared to 75.5 percent of women for that age group). In addition, women are only employed in unstable and vulnerable jobs; they are particularly present in the informal sector. Poverty levels are estimated at 79.4 percent for women; the unemployment level is 48 percent (République de Djibouti, 2021a).

Table 2: Employment indicators between men and women

	Men	Women
Percentage of the active population in relation to the working-age population	58,5	31,6
Percentage of working age the population being employed	36,4	11,6
Unemployment rate - International Labour Organization definition (ILO) (ages 15-59)	23,1	38,2
Unemployment rate for youth (ages 15-34)	57,4	75,5
Percentage of employees (formal jobs) working in the public sector	56,4	37,0

Source: UNCTAD based on the Djibouti Household Survey for Social Indicators (EDAM-IS) 2017 (République de Djibouti, 2022)

[19] Delegation of the European Union, Analysis of the Gender Situation in Djibouti, 2021

The Ministry of Women and Family (Ministère de la Femme et de la Famille) conducted a study on the evolution of the situation of women in the Republic of Djibouti over the last fifteen years (2000-2015). The study was multidimensional and multisectoral and aimed to provide the Government and its partners with an updated overview of the evolution of women and a dashboard of gender indicators and data. Despite its ambition, the scope of the study remains limited due to the lack of (recent) data, particularly for the economic sectors, for which statistics are not broken down by gender[20].

Girls' school enrollment has improved significantly over the past ten years, and the proportion of girls as well as the parity between girls and boys has been evolving positively and steadily. However, gender-based inequalities in access persist, particularly in rural areas. According to the Statistical Yearbook for the 2019-2020 school year, girls accounted for 47 percent of students at the primary level in urban areas and 43 percent in rural areas. These figures do not include school-age children, who are not enrolled in school. The government has established services to facilitate school attendance in rural areas, such as a canteen and free textbooks available in all localities. These services are not widely known by parents, and the explanation may lie in the relationship of many parents with the teaching staff of their school. Parents who are not involved in school life are unlikely to be aware of school attendance facilitation services[21].

Finally, the gender issue has been at the heart of the Government's actions for more than two decades. Women have entered Parliament and several are ministers in the current administration (2022). The progression of women in public service is shown in Table 3. Between 2000 and 2018 the number of women increased from 1,090 to 5,064, corresponding to 28 percent in 2000 and 32 percent of the total in 2018.

Table 3: Survey on the representation of women in public service

Total gender headcount for the period 2000-2018	2000		2018	
	Total	In percentage (percent)	Total	In percentage (percent)
Men	2,856	72.4	10,708	67.9
Women	1,090	27.6	5,064	32.1

Source : République de Djibouti and Fonds des Nations Unies pour la Population (2019)

For senior government jobs, the law sets the quota at 20 percent[22]. However, there was still a persistent underrepresentation of women in the senior civil service, for example at the level of Secretary General (Table 4). Djibouti currently lacks laws that promote gender equity regarding property ownership, due to unequal inheritance rights between men and women, and regarding employment, due to legal restrictions on women's access to employment in certain professions.

[20] Gender analysis 2021 – Delegation of the European Union
[21] Gender analysis 2021 – Delegation of the European Union
[22] Decree n°2008-0270/PR/MPF on the modalities of application of Law n°192/AN/02/4th L of 13 November 2002 instituting the quota system in elective offices and in the State administration.

These issues will need to be addressed to provide a level playing field for women-owned businesses to grow and create jobs (World Bank, 2021).

Table 4: Gender distribution of senior public service positions

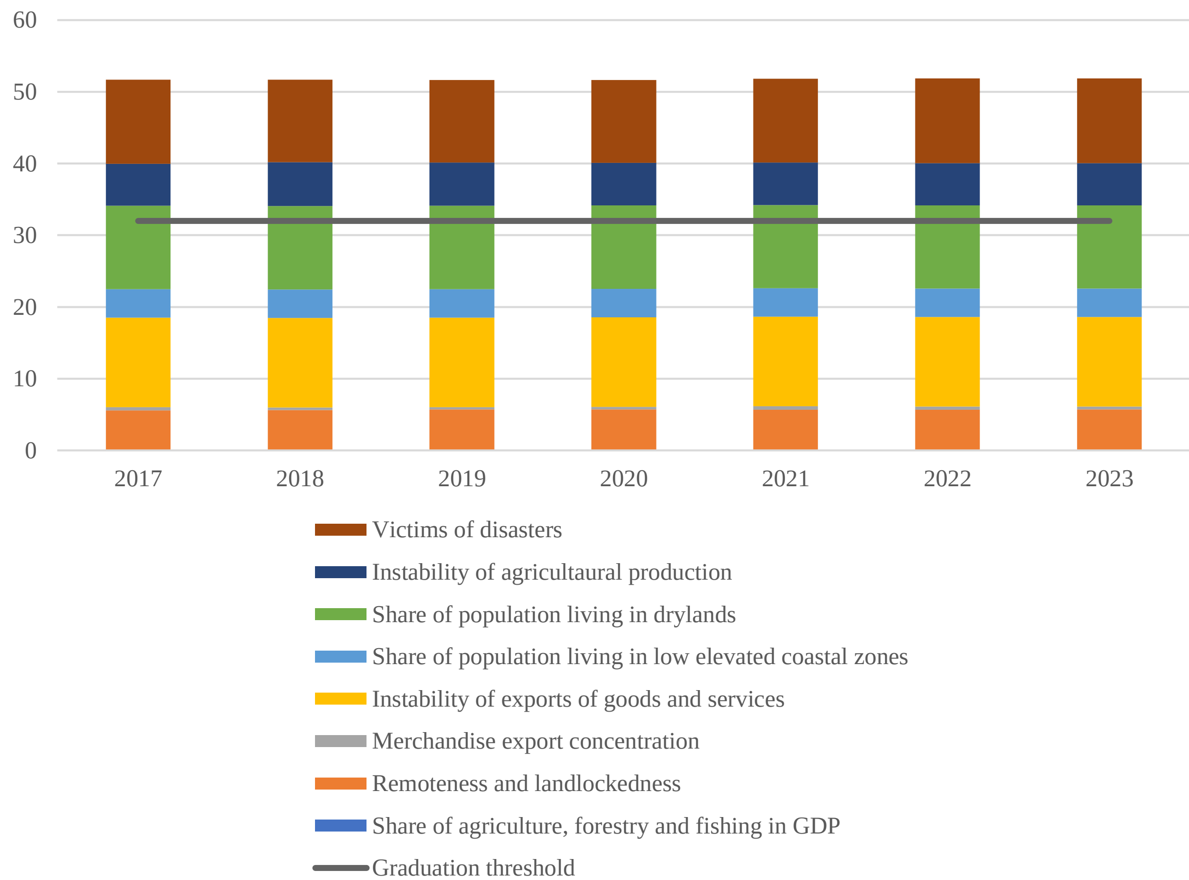
	Men	percent	Women	percent
Head of Office	66	66 percent	33	33 percent
Head of Department	287	65 percent	151	35 percent
Director	123	73 percent	46	27 percent
Technical Advisor	317	87 percent	49	13 percent
Secretary General	18	85 percent	4	14 percent

Source : République de Djibouti et Fonds des Nations Unies pour la Population (2019)

3.2. Prosperity

With an Economic and Environmental Vulnerability Index (EVI) of 51.9, Djibouti is far from the LDC graduation threshold of 32, and also well above the average for all LDCs of 39.1, underscoring the country's high vulnerability to economic and environmental shocks. The three greatest areas of vulnerability to Djibouti's prosperity and sustainable development according to this Index are: instabilities in exports of goods and services, the share of the population living in arid areas and the number of people affected by natural disasters (Figure 12).

Figure 12 : Economic and Environmental Vulnerability Index



Source : UNCTAD based on the LDC indicators developed by the CDP Secretariat [accessed November 2023].

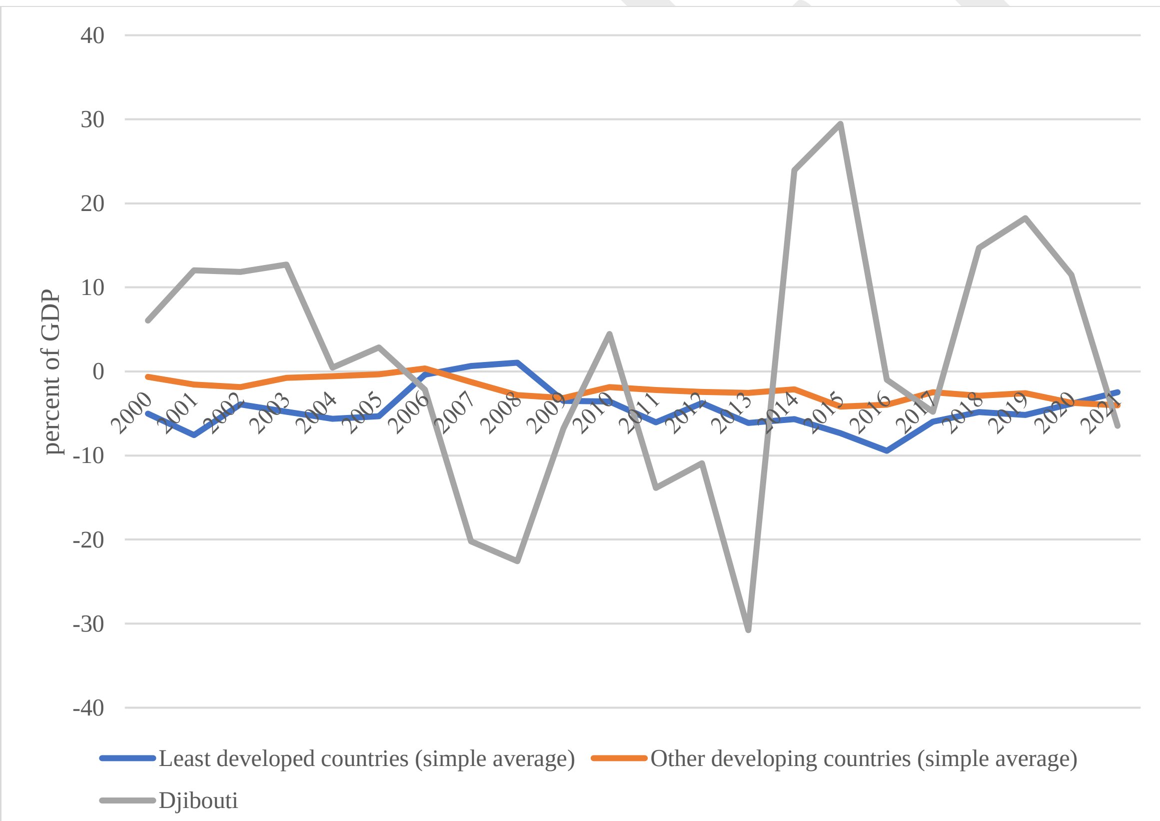
3.2.1. Concentration and instability of economic activity

Djibouti's economy is a small, so-called extroverted economy, which makes it extremely sensitive to any exogenous shocks. The main structural factor responsible for a country's greater exposure to exogenous shocks is its small size. Among the various ways of measuring the size of a country, the most relevant is the number of inhabitants (Guillaumont, 2006).

As already demonstrated in Section 2 of this document, Djibouti's economy relies heavily on international maritime trade. Ethiopian exports account for nearly 85 percent of Djibouti's port activity, which confirms the strong dependence on the Ethiopian economy. Another risk is related to foreign direct investments. Over the past decade, FDI from the oil-producing countries of the Gulf, invested mainly in capital-intensive activities such as the construction of port, road, real estate and hotel infrastructures, have made it possible to accelerate the country's growth. Given the structural changes, some internal/endogenous risks such as political instability and poor governance could potentially affect the country's economic fundamentals.

The concentration and volatility of exports puts pressure on the current account. Figure 13 shows that Djibouti's current account (as a percentage of GDP) is more volatile than the average for other LDCs and other developing countries. While Djibouti's balance was -30 percent of GDP in 2013, it was +30 percent in 2015, 11.5 percent in 2020 and -6.5 percent in 2021. In fact, the fluctuation of the current account balance, as well as the instability of exports, are also due to inventory changes and re-exports (IMF, 2019). Thanks to revenues from military bases, the current account was positive (1.3 percent of GDP) on average between 2002 and 2021 compared to -4.5percent for other LDCs and -2.2 percent for other developing countries (Figure 13). Nevertheless, official reserves have declined from $686 million in 2020 to $588 million in 2021. In 2020, reserve coverage is estimated at only 2.3 months of imports of goods and services due to high import dependence. In comparison, the LDC average was 24 months of reserve coverage and 13 months for the global average.

Figure 13: Current account balance as a percentage of GDP



Source: UNCTAD on the basis of the Additional Reclassification Indicators (https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/SGI-dataset.xlsx, [accessed November 2023]).

Dependence of Djibouti's economy on Ethiopia

The port of Djibouti is the leading contributor to GDP. Combined with related transport and logistics activities, it accounts for more than 35 percent of GDP. In addition, since May 1998, the date of the conflict between Ethiopia and Eritrea, the Port of Djibouti has become the only point of access to the sea for Ethiopia. But the latter is also the main engine of the Djiboutian economy. As a result, Ethiopia contributes 28 percent of Djibouti's GDP. Conversely, Djibouti imports from Ethiopia its consumption of fruits and vegetables and especially of khat, the euphoria-inducing herb that Djiboutians consume on a daily basis. Practically, between 12 and 15 tonnes of khat are imported per day. The annual value of these imports ranges between FDJ 4 and 5 billion, which is between $22.5 and $28.2 million. Just like tobacco and alcohol, khat is heavily taxed. It is a significant source of tax revenue for the government. Khat, which is imported mainly from Ethiopia and must be consumed fresh, employs thousands of women who are active in street vending, an activity estimated to be the largest employer in the informal sector in Djibouti. However, it should be noted here that khat is the second largest household expenditure item and sometimes at the expense of food. A 2011 World Bank survey indicates that the average household's consumption of khat amounts to about 20 percent of its income, and direct taxes on khat account for 15 percent of government tax revenues and a turnover of more than $50 million per year in Djibouti (Banque Mondiale, 2011).

In addition, a significant portion of electricity and water resources are imported from Ethiopia, indicating the country's current energy dependence. Since June 2011, Djibouti has been importing 70 percent of its annual electricity consumption, estimated at 300,000 MWh, from Ethiopia, for a total of 210,000 MWh at a price of 7 cents per KWh. The completion of renewable energy projects, including geothermal and wind power, will reduce this dependence and facilitate compliance with the commitments made in the Nationally Determined Contributions (NDC) to reduce greenhouse gas emissions (République de Djibouti, 2021a).

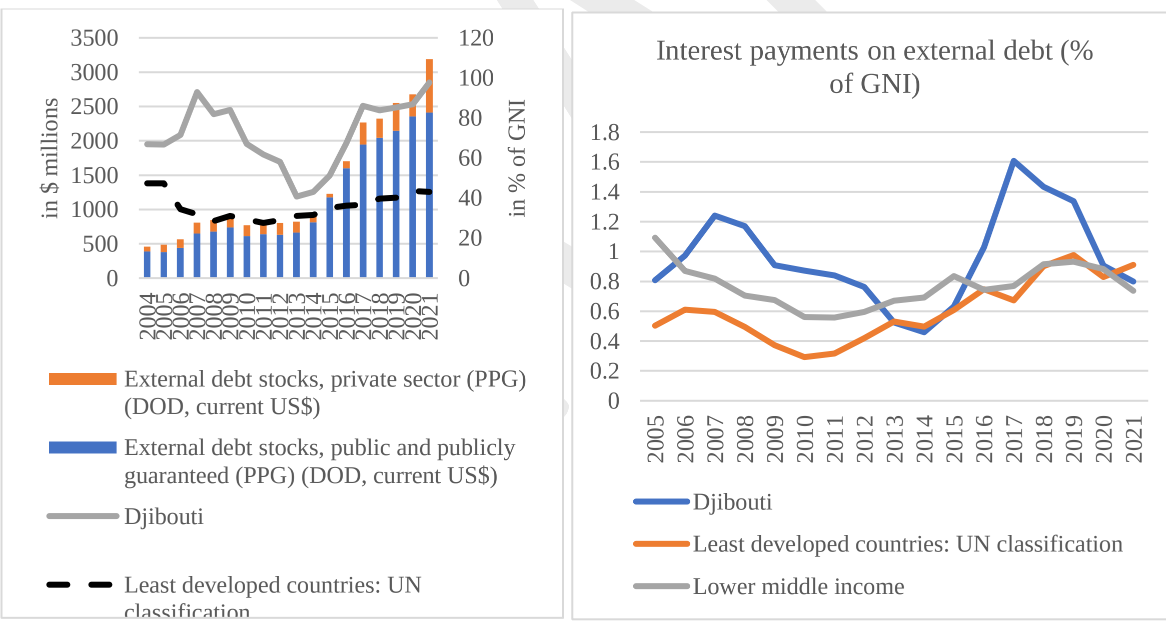
The risks associated with Djibouti's high concentration of exports and economic activity with Ethiopia are mainly: a possible downturn in foreign trade due to the Tigray crisis, which could lead to a drastic decline in customs revenues, and the resurgence of COVID-19. To mitigate these risks, Djibouti is strongly supporting mediation efforts in the Ethiopian conflict, and aims to diversify investment and economic activities.

3.2.2. Vulnerability to debt

Between 2015 and 2021, the external debt stock increased from 51.2 percent of Gross National Income to 97.7 percent due to large investments in the transport sector, including the construction of the Addis Ababa-Djibouti railroad and a cross-border freshwater pipeline. In absolute terms, the debt has increased from $769 million in 2010, to $1.2 billion in 2015, and to almost $3.2 billion in 2021. 84 percent of this debt belongs to the public sector (see figure 14, left). During the 2020 Debt Service Suspension Initiative (DSSI), Djibouti's debt service payments to public creditors were deferred, and the DSSI provided fiscal reserves to Djibouti in both 2020 and 2021 (World Bank, 2022). Interest payments as a percentage of GNI was brought down from 1.6 percent to 0.8 percent in 2021 (see Figure 14, right)

Figure 15 compares the share of concessional debt and the average interest rate on new external debt between Djibouti, the average LDC, and the average of lower middle-income countries. Figure 15 (left) shows that while only 21 percent of the debt is under concessional terms, 10 percentage points lower than the LDC average, the average interest rate is about the same, at 1.7 percent in 2020.

Figure 14: External debt, in $ millions and as a percentage of gross national income (GNI) (left) and interest payments as a percentage of GNI (right)

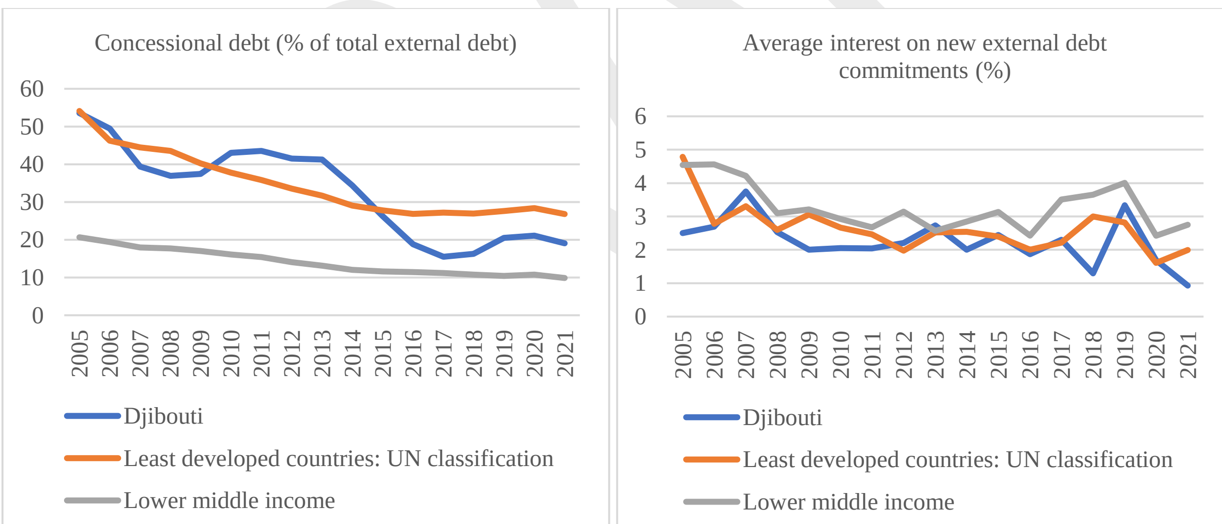


Source: UNCTAD based on the data of the International Debt Statistics [accessed November 2023].

Interest rate risk is real, as 25.6 percent of its portfolio has a floating interest rate (World Bank, 2018). Similarly, most of the credits obtained from China are at variable rates. The second risk and vulnerability is that return on investment made is slow and the rates are low. At the domestic level, inefficiencies in the financial services sector limit the ability of companies to raise capital and take out loans to develop the services sector (République de Djibouti, 2021a). It is also worth noting that in Djibouti, "98.3 percent of informal economic units do not have bank accounts, either because a bank account does not meet their needs (82.8 percent), or because the procedures are complicated (18.4 percent), or because the interest/agios are high (15.4 percent)" (République de Djibouti, 2021a).

However, the strongest risks are related to the concentration of debt and over-indebtedness to China (54 percent of Djibouti's external debt). Debt to China exceeded 43 percent of GNI in 2020[23], which implies that more than 3 percent of Djibouti's GNI would have to be repaid to China in 2022.[24] Whether a greater concentration of debt on a single creditor is good or bad is a question difficult to resolve. On the one hand, having fewer creditors might make it easier to renegotiate debt; on the other hand, a single large creditor like China might have more power to negotiate. It can be argued that the increase in official loans from China may also be linked to the decrease in the share of concessional loans (Jensen, 2021). With respect to debt renegotiation, China has announced interest-free loan relief; the effectiveness, however, remains to be seen.[25]

Figure 15: Concessional debt and average interest rate, 2004-2020



Source: UNCTAD based on the database of the International Debt Statistics [accessed November 2023].

In the event of a shock, be it the COVID-19 pandemic or natural disasters, a highly indebted country has little room for maneuver to react financially in a proper manner. External aid as well

[23] https://fr.statista.com/infographie/27636/pays-les-plus-endettes-envers-la-chine-selon-le-niveau-de-dette-exterieure-rapporte-au-revenu-national-brut/
[24] https://www.lesechos.fr/monde/enjeux-internationaux/dette-la-chine-va-recevoir-14-milliards-de-dollars-des-pays-les-plus-pauvres-en-2022-1395065
[25] https://african.business/2022/09/trade-investment/chinese-banks-want-to-be-repaid-in-full-scepticism-greets-chinas-debt-forgiveness/

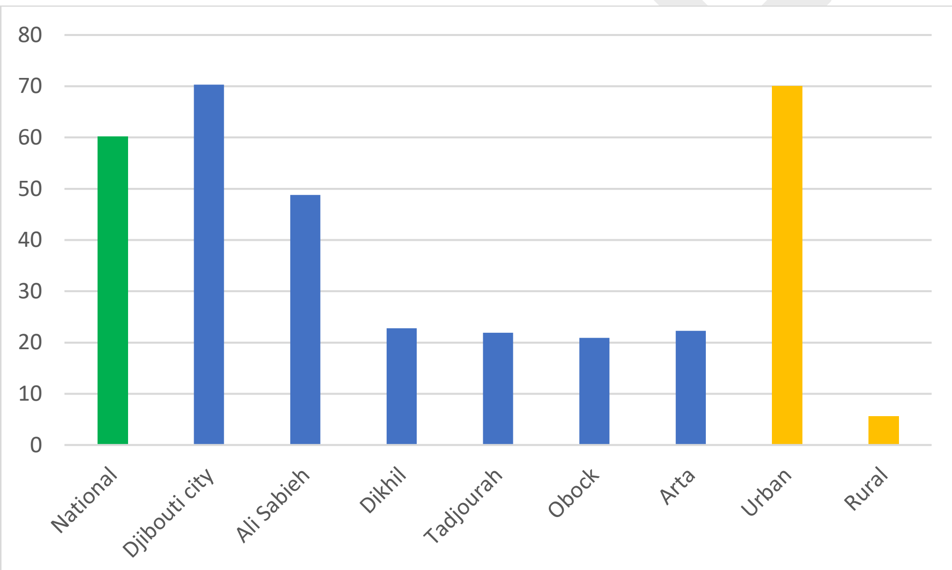
as the programs of the World Bank and the International Monetary Fund (IMF) are often insufficient, given the immense economic damage.

3.2.3. Other vulnerabilities and economic risks

Djibouti's macroeconomic outlook has been severely affected by the COVID-19 pandemic and inflationary pressures on food and energy. Djibouti, like other countries, has faced a large negative external demand shock due to the global recession. Specifically rural areas are suffering from these negative shocks. One-fifth of the population, particularly in rural areas, lived in extreme poverty (République de Djibouti, 2022).

One of the most striking aspects of poverty is that access to electricity is based on the place of residence. Figure 16 shows that while 70 percent of the urban population has access to electricity, only an average of 5.6 percent of the rural population does.

Figure 16: Access to electricity by residence and region in 2017



Source: République de Djibouti (2022).

One of the risks that Djibouti could face is that its basic infrastructure is of high quality and potentially provides jobs, but that its development is partly beyond the control of Djiboutians themselves. In some ways, the quality of the corridor between Djibouti and Addis Ababa illustrates the problem, with a very significant proportion of the jobs created by transport and logistics held by Ethiopian operators and workers. In terms of freight transport, Djibouti is not even able to cover the amount of traffic granted under the Djibouti-Ethiopia Joint Commission agreements. There is a risk that this phenomenon will be repeated with the New Information and Communication Technologies (NICTs) (UNCTAD, 2015). While undersea cables generate public revenue through the payment of access fees from neighboring countries, they do not guarantee that Djibouti will be able to generate the production of the services they created.

Djibouti ranks 158th out of 175 countries in the ICT Development Index published by the International Telecommunication Union (ITU). Mobile financial services are just beginning to emerge. According to the World Bank (2021), however, micro, small, and medium-sized enterprises are not using digital financial services, opting instead for cash transactions.

The banking and financial sector (dominated by the banking sector with 97 percent of assets) (WTO, 2022) also faces the risks to which the banking sector is exposed. These include non-performing loans, weak financial penetration and inclusion, low customer base, and the fight against both money laundering and the financing of terrorism. Private sector credit as a percentage of GDP remains low (18 percent of GDP in 2022) due to a shortage of lending instruments suitable for households or SMEs (only 5 percent of formal companies have access to bank financing). Credits are concentrated mainly in the transport, logistics, construction and real estate sectors.

Non-performing loans measure the quality of the loan portfolio and amounted to 16 percent of the total loans in 2019 and then dropped the following year to 13 percent. Non-performing loans that measure the quality of the loan portfolio represented 16 percent of total loans in 2019 and 13 percent in 2020. This improvement is not directly related to effective and efficient management of the loan portfolio, but rather to a combination of loan expansion and write-offs of non-performing loans older than five years which lowered the ratio. The net effect of nonperforming loans is a draw on the reserve for doubtful and uncollectible loans, which ultimately impacts bank profitability. In the same year, the provisioning rate for nonperforming loans increased by 5.8 percentage points, from 78.2 percent to 84 percent (Banque Centrale de Djibouti, 2021).

A deterioration in global financial conditions could raise interest costs and subsequently worsen external financing prospects. Renewed pressure on central banks could create funding disruptions (IMF, 2019).

Other financial risks emanate from the country's geostrategic location. Djibouti's thriving banking system, which has virtually no foreign exchange shortages, is located near areas of international piracy in the Indian Ocean and nearby terrorist groups that are active in the surroundings. This puts the banking sector at risk of being exposed to the perpetrators of these crimes. The illicit financial flows (IFFs) discussed above serve as a modus operandi for organizations engaged in these clandestine activities (Banque Centrale de Djibouti, 2021).

A crisis in Djibouti's banking sector, which serves the entire region, would have an impact on neighboring countries, especially Ethiopia and Somalia, and could present a risk for the growing trade flows in the area. Due to the less developed state of the banking system in Ethiopia and its frequent shortage of hard currency, traders rely primarily on the Djibouti banking system to open letters of credit. A disruption of financial services would slow or even stop trade flows. In addition, some regional cross-border investments (Somaliland) could suffer from a banking crisis in Djibouti.

3.3. Planet

Importance of the environmental issue

As of 2004, the Djibouti authorities became aware of the environmental issue and issued Decree No. 2004-0092/PR/MHUEAT establishing a National Commission for Sustainable Development (CNDD). This Commission is chaired by the Prime Minister and assisted by a Technical Committee for Sustainable Development (République de Djibouti, 2022).

During the last Administration, a Ministry of Environment and Sustainable Development was created. Its action covers the three environmental components (biodiversity, pollution, climate change) and their five SDGs (SDG7, SDG12, SDG13, SDG14, SDG15). The linkages between the environment and social and economic aspects are well integrated in all of the Ministry's activities, such as poverty eradication and food security (SDG1 and SDG2); gender equality (SDG5); access to safe water and sanitation (SDG6); the promotion of sustained, shared and sustainable economic growth, full and productive employment and decent work for all (SDG8) and finally the strengthening and revitalization of the means to implement the global partnership for sustainable development (SDG17) (République de Djibouti, 2022).

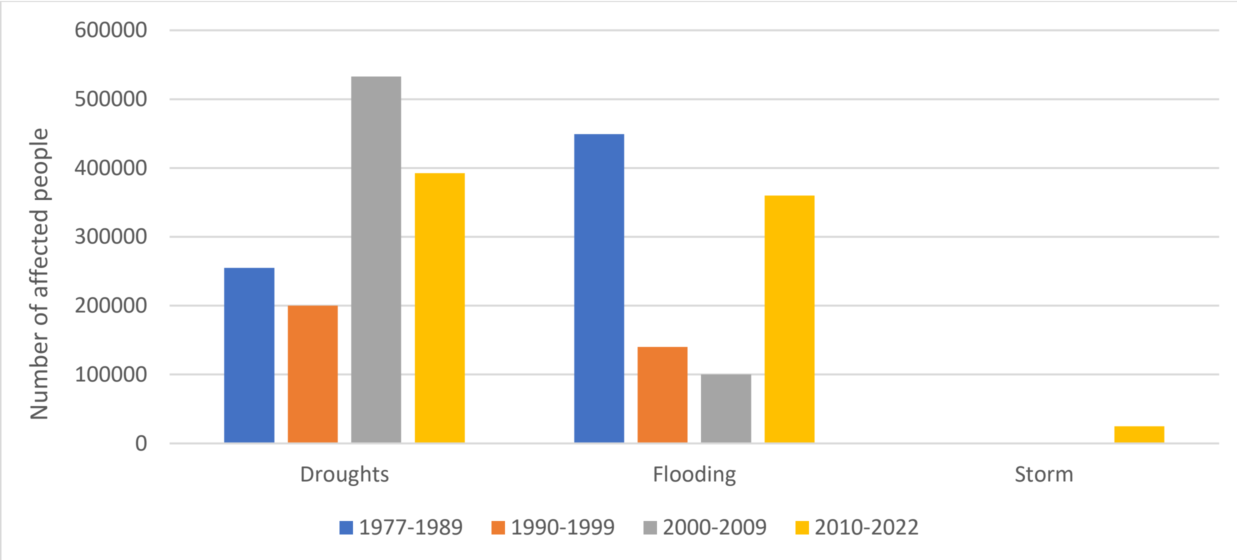
Vulnerability to climate change

Djibouti is extremely vulnerable to climate change and is a high-risk land in terms of the major hazards identified by the UN: earthquake/geological hazards, climactic risks, animal and plant health threats, and the risk of forest fires. According to the Global Climate Risk Index, Djibouti is one of the 50 countries in the world most vulnerable to extreme climate risks. The country is vulnerable to climate change due to an arid climate that makes natural conditions particularly challenging. Djibouti is particularly vulnerable to drought, deforestation and desertification, flooding and inundation, and earthquakes.

Climate change is undoubtedly the most visible risk, as natural disasters such as the droughts and floods that hit Djibouti between 2017-2019 caused huge human losses and material damage, showing the fragility of the way of life of a large part of the population and productive capacities located in the coastal regions.

Between 1990-1999 and 2010-2022, the incidence of natural disasters, measured by the number of people affected, has increased. Between 1990 and 1999, 20,000 people were affected per year (average) by droughts; between 2010 and 2022, this figure was 39,000 per year (Figure 17).

Figure 17: Incidence of natural disasters, between 1977 and 2022



Source: UNCTAD based on the EM-DAT database

The current drought in East Africa has been particularly devastating for small-scale farmers and livestock breeders in the Horn, who are already vulnerable to climate-related shocks. The drought conditions have led to the drying up of wells and the loss of livestock, ultimately impacting particularly the incomes and livelihoods of Djibouti's rural populations.

It is clear that increasing aridification and water shortages are especially affecting rural and (agro)pastoral populations, given the very poor soils, limited vegetation cover and overexploitation of groundwater. The Ministry of Agriculture has estimated an annual loss of 4-5percent of arable land in the main agricultural regions.

According to the IPC (2023), the number of acutely food insecure people increased to 250,000 between March and June 2023, representing 21 percent of the total analyzed population compared to 11 percent in the previous year (March - June 2022). Specifically, in the three zones of Ali Sabieh Rural, Ali Sabieh Ville, and Arta Rural, 20 to 40 percent of their populations face acute food insecurity. Water stress, exacerbated by climate change, is considered very high and is a major concern for the population, especially in rural areas, but also limits economic opportunities. Djibouti has 318 m3 of renewable inland freshwater resources per capita, well below the absolute freshwater scarcity threshold of 500 m3/capita/year. Net population growth increases this pressure on water resources (Nations Unies Djibouti, 2021).

Similarly, the country is experiencing floods more and more frequently. It suffers from soil and water salinization, water erosion and severe flooding with real threats to coastal areas and strategic infrastructure.

In addition, the rise in the sea level and the increasing seawater temperature are other risks that will have an impact on terrestrial and marine biodiversity, in addition to the negative externalities of climate risks on vital sectors of the economy: road and rail transport, water, sanitation and buildings, but also on tourism, a promising sector for growth. The loss of coastal land is due to a rising sea level, flooding, and human actions, including the removal of sand and clay for real estate construction. It is expected that the sea level rise will affect coastal residents (over 80 percent of the population). The risk of saltwater intrusion into the coastal aquifer represents a significant threat to the country's already declining water quality, exacerbating the phenomenon of coastal erosion that affects economic infrastructure and coastal marine ecosystems (World Bank, 2021).

The consequences of climate change for economic and social development can be severe. According to the IMF (2017), a 1°C increase of the average temperature can reduce GNI per capita by 1.5 percent. Also, increasing temperatures have negative impacts on labor productivity, agricultural production, health and peace. Estimates by Kireyev (2018) suggest that a 2°C temperature increase can result in costs as high as 2 percent of GDP in 2040 and 3 percent in 2060. Without adequate adaptation, the costs of the damages caused by climate change are estimated at $5,135 million between 2010 and 2060.

Djibouti is vulnerable to climate change with a rather particular climate, as shown above. Mitigation and environmental protection strategies have been adopted. These will make it possible to take into account environmental considerations and climate change in the various sectors. (République de Djibouti, 2021a) (Section 4 of this document).

3.4. Peace

Djibouti became an independent state on 27 June 1977 and adopted a presidential political system. Initially, for 15 years, between 1977 and 1992, provisional constitutional texts organized the political and institutional life of the country. It was not until September 1992 that a full-fledged constitution was adopted. It was first amended in September 2002 and again in December 2010.

After a decade of civil conflict (1991-2001), Djibouti has established modern institutions that have matured, although they are still fragile. The country stands out for its stability in a troubled region. The strong presence of foreign military bases has provided Djibouti with a steady stream of rent-based income from its land. For NATO countries, a presence in Djibouti provides maritime security and serves as a base to combat regional military threats (Banque Mondiale, 2021). Djibouti's peace and stability are a source of wealth.

Despite this relative stability, which is unique in the region, Djibouti is not immune to the upheavals that affect the region, particularly its neighbor Ethiopia. As early as November 1991, the beginning of an internal conflict arose in the north of the country. On 26 November 1994, a peace agreement without external interference was reached with the rebellion's leaders. The constant adaptation of this balance to the sociological realities of the country are the source of the exceptional political stability that the Republic of Djibouti has enjoyed for over 45 years in a region marked by instability and conflict (Caslin, 2022).

Political instability in Ethiopia has already adversely affected port activities in Djibouti. A prolongation of this conflict could also interrupt or delay major projects underway. A truce reached in November in Ethiopia could allow trade to resume, reverse recent drops in port activity and help attract new foreign investment.

Located in a volatile region, Djibouti has been a host country for refugees from Ethiopia, Somalia, Yemen and Eritrea for decades. In addition, migratory flows from neighboring countries transiting through Djibouti have always benefited from Djibouti's hospitality, resulting in a floating population of an estimated 150,000 irregular and undocumented migrants. In addition, more than 100,000 migrants (mainly Ethiopians) transit through Djibouti each year on their way to or from the Arabian Peninsula. The majority of migrants cross the desert areas of Djibouti to reach the city of Obock, to head to embarkation points along the coast from where they cross the Bab El Mandeb Strait and travel to Yemen. Since 2017, their numbers have surpassed those of migrants crossing the Mediterranean to Europe [26].

Lastly, the states bordering Djibouti are subject to chronic internal and external instability. The risks that the effects of regional instability will be felt in the economy are very real and are linked to the flow of investments from outside the country but also to the exchange of goods and services.

3.5.Partnerships

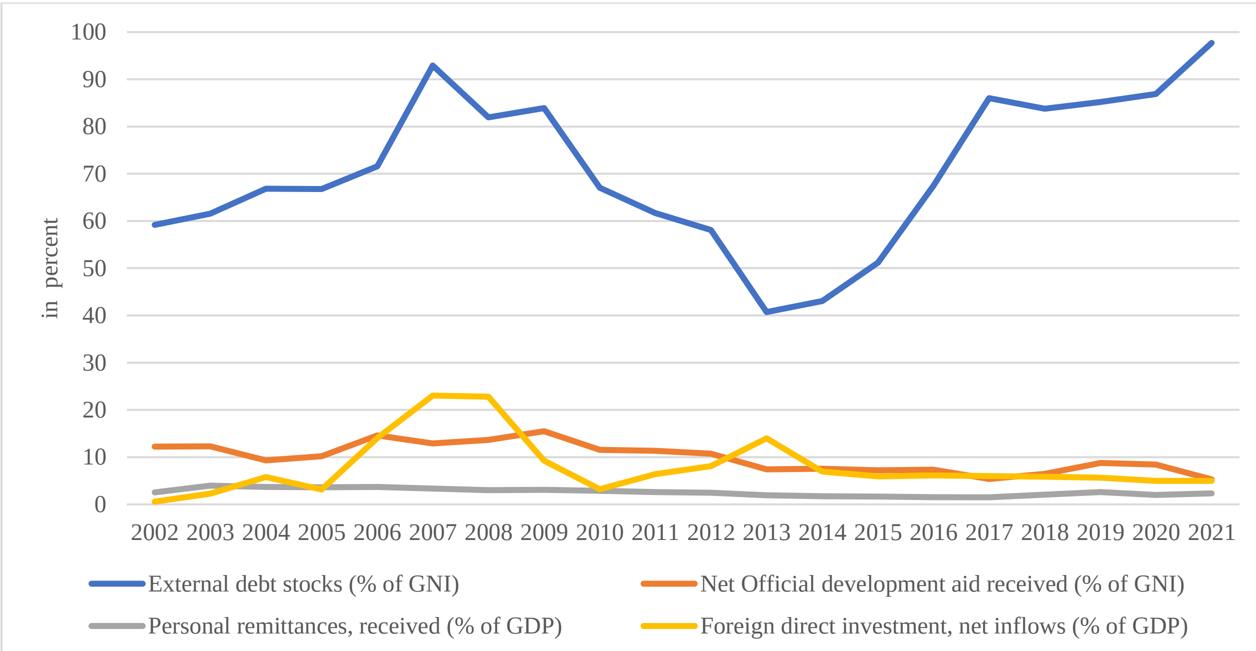
Djibouti's small size makes it dependent on partnerships, especially when it comes to financing development and investments.

China has played a particularly active role in investing in the country's transportation network in line with China's Belt and Road Initiative (BRI). China Merchants Group owns the Doraleh Multipurpose Port, which was completed in May 2017. In 2018, China also opened the Djibouti International Free Zone, the largest free zone in Africa, which is partly owned by Dalian Ports Group, IZP and China Merchants Group. In 2017, China's POLY GCL Petroleum Group announced plans to develop a $4 billion liquefaction plant to process natural gas from Ethiopia. The project will include a pipeline and export terminal[27].
Recently, Djibouti signed a cooperation agreement for one billion dollars with a Chinese company to build a launch site for satellites and rockets.[28]
However, investment has come at the cost of increasing debt vulnerability, and tax revenues have been delayed due to large tax expenditures.

The ratio of public and publicly guaranteed debt to GNI doubled between 2015 and 2020, exceeding private investment. The pandemic has also exacerbated the country's weak external performance and its financial sector's stability[29]. While official development assistance has declined from 15 percent of GNI in 2011 to 5.3 percent in 2021, it still represents an important source of external income (Figure 18). Workers' remittances make a modest and declining contribution to GNI (between 3 percent in 2011 and 2.4 percent in 2021).

[26]According to UNHCR and IOM estimates, 346,000 people crossed the Mediterranean between 2018-2020 compared to 400,000 people for the Bab el Mandeb Strait.
[27] https://oxfordbusinessgroup.com/overview/laying-groundwork-major-logistics-infrastructure-and-new-free-trade-zone-fuel-continued-economic
[28] https://african.business/2023/01/trade-investment/djibouti-signs-1bn-rocket-deal-with-hong-kong-company/
[29] IFC - Private Sector Diagnostic - February 2021

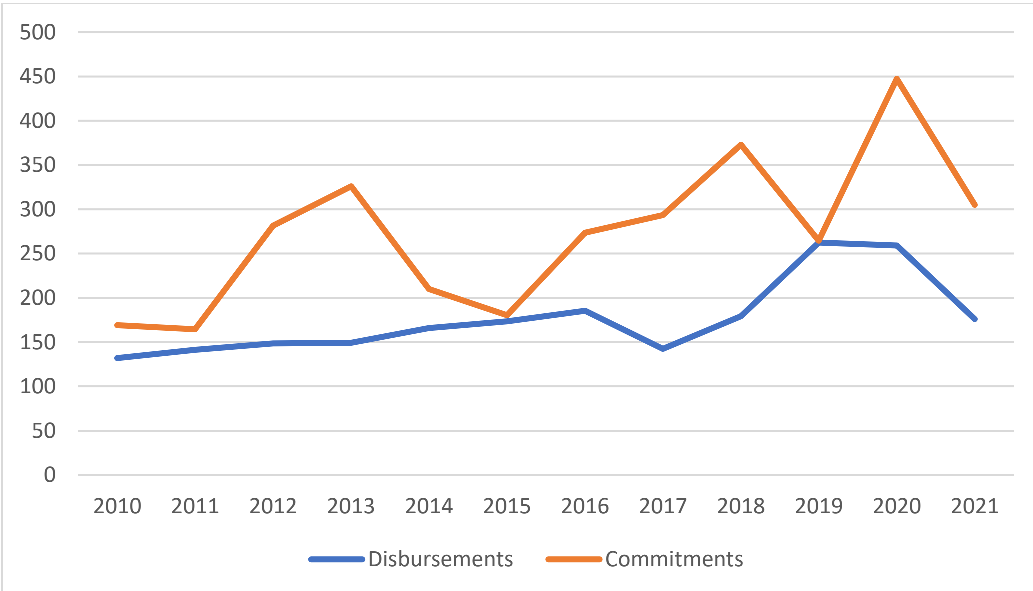
Figure 18: External financing of development



Source: UNCTAD based on the World Development Indicators database [accessed November 2023].

Over the period between 2010-2021, commitments for aid for trade exceeded disbursements. The year 2020 reaches a peak in commitments made to the country with an amount as high as $447 million while disbursements amounted to only $259 million. A similarly high gap of 57 percent between commitments and disbursements in observed for 2021 (Figure 19).

Figure 19: Aid for Trade commitments and disbursements in $ millions, 2010-2021



Source: UNCTAD based on OECD Aid for trade data, https://www.oecd.org/dac/aft/aid-for-tradestatisticalqueries.htm [accessed November 2023].

In addition, economic dependence on the key partners China and Ethiopia poses a vulnerability in the event of intensified conflict in Ethiopia (see Section 3.4) or a slowdown in economic growth in China. Chinese foreign development financing has been slowing down for years and is unlikely to resume soon as the Chinese government prioritizes domestic economic revitalization. Further, due to strong dependences, any disturbances in the bilateral relations with its key partners can also affect Djibouti's economic or financial situation. For example, in June 2000, despite the friendship between Djibouti and Ethiopia and the interdependent economic interests between the two countries, the management of the Port of Doraleh was awarded to Dubai. This choice had upset Ethiopia. In addition, the cancellation of the DP World contract in favor of China Merchants could result in reputational risks (affecting foreign direct investment prospects) as well as budgetary costs. According to the verdict of the London Court of International Arbitration, Djibouti will have to pay over $200 million in damages.[30]

4. Development Challenges: Building resilience to vulnerabilities

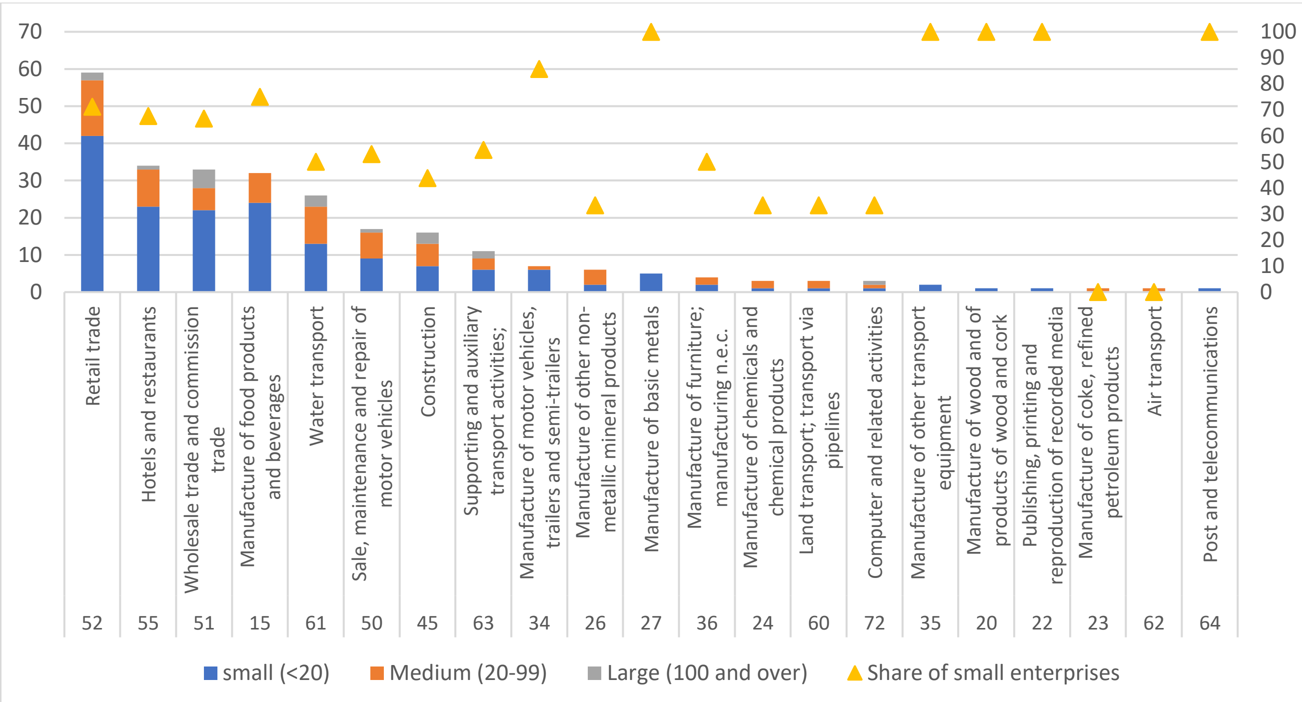
4.1. Competitiveness and development of the private sector

It should be noted that trade activities in export markets and at the national level are constrained by institutional and human weaknesses that raise transaction costs and result in inefficient services. This limits the competitiveness of export products and services (Republique de Djibouti, 2021a).

[30] https://comprendre.media/djibouti-devra-verser-200-millions-de-dommages-interets-pour-son-refus-de-ceder-le-terminal- de-doraleh/

To better identify the main challenges of the private sector, we use the 2013 World Bank enterprise survey. The majority of surveyed firms (22 percent) were in the "Retail trade" sector, followed by "Hotels and restaurants" (13 percent), "Wholesale trade" (12 percent), and "Manufacturing of food products and beverages" (12 percent) (Figure 20). Approximately 63 percent of businesses are small, with less than 20 employees.

Figure 20: Number of enterprises, by sector (ISIC, Rev. 3.1) and by size

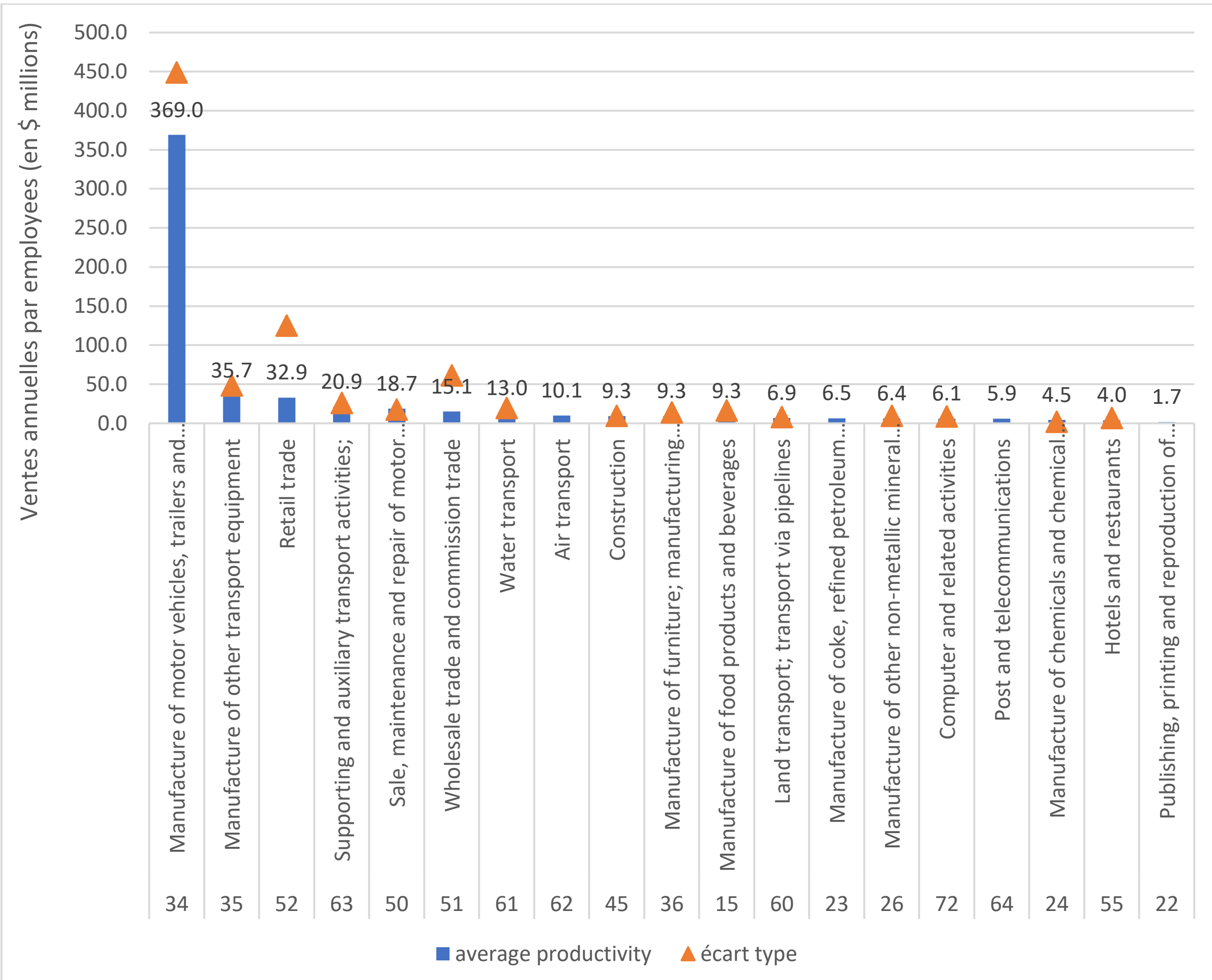


Source: UNCTAD calculations, based on World Bank enterprise survey data in 2013.

The sector with the highest annual sales is "Manufacture of motor vehicles, trailers and semi-trailers" (ISIC 34) with annual sales averaging $583 million, followed by "Sale, maintenance and repair of motor vehicles" (ISIC 50) and "Supporting and auxiliary transport activities" (ISIC 63). A very important indicator for competitiveness as well as inequality among companies is the average labor productivity (Figure 21). The most capital-intensive sectors are also the most productive: "Manufacture of motor vehicles, trailers and semi-trailers" (ISIC 34) and "Manufacture of other transport equipment" (ISIC 35). Next, the service sectors "Retail trade" (ISIC 52) and "Supporting and auxiliary transport activities" (ISIC 63) show the highest productivity with an average of $32.9 million and $20.9 million per employee, respectively. What is striking, however, is the large difference between businesses, shown by the standard deviation, which is highest in the "Retail trade" sector. The concentration of economic activity is the main reason for the high inequality and the very high unemployment rate.

On the one hand, economic sectors are insufficiently open to competition and still dominated by monopolies, which poses the risk of accumulation and distribution of wealth among a small group. However, the efforts made in recent years to strengthen the social protection of the most vulnerable and to open up the regions are encouraging (Nations Unies Djibouti, 2021). The law on competition policy does not cover public enterprises. The exclusion of public enterprises from the scope of competition legislation appears to have contributed to the crowding out of the private sector in Djibouti and to the low quality and high cost of public services, particularly in the electricity and telecommunications sectors (WTO, 2022).

Figure 21: Annual sales per employee

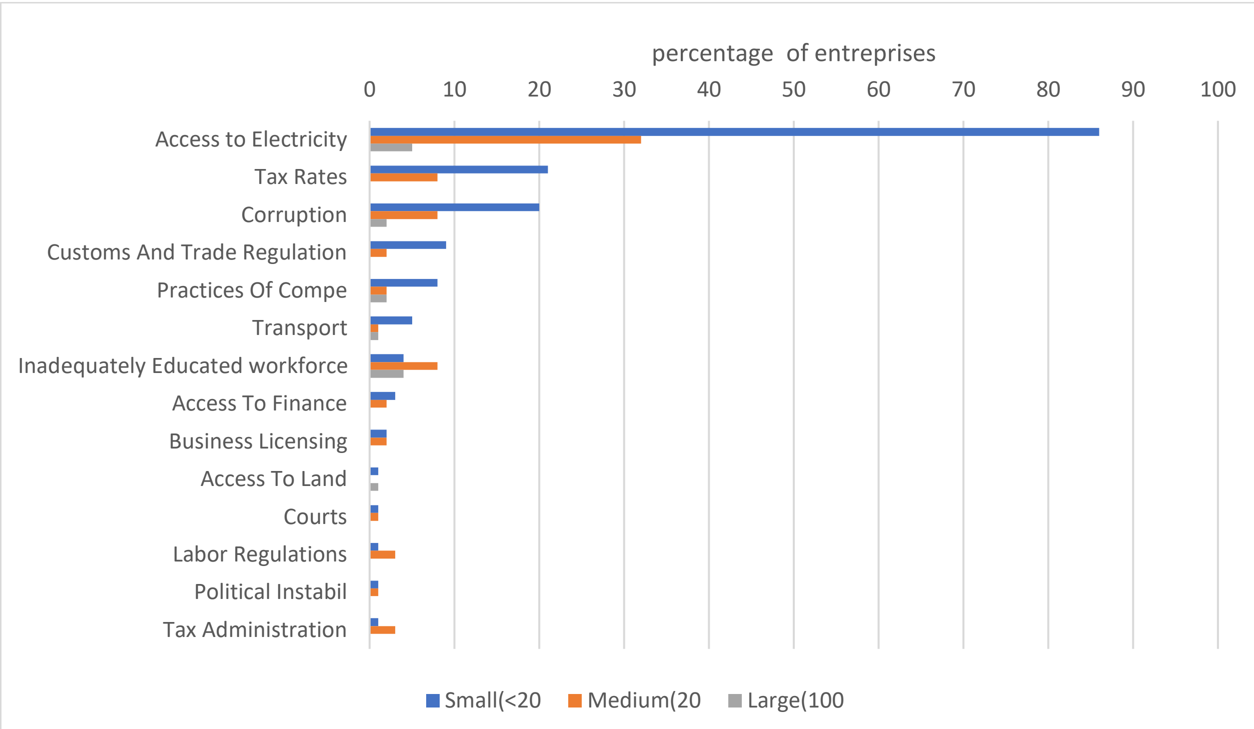


Source: UNCTAD calculations, based on data from World Bank enterprise surveys in 2013

On the other hand, the costs of inputs such as electricity, water, and labor are high. Companies surveyed by the World Bank mention lack of access to electricity (86 percent of small businesses), tax rates (21 percent of small businesses), and corruption (20 percent) as the main obstacles to carry out their activities. Figure 22 reports the main obstacles based on the size of the business surveyed. What is interesting is that while the main obstacle observed for the average African company is access to finance, only 3 percent of Djibouti companies indicated this as their main obstacle. In addition, medium-sized enterprises (between 20 and 99 employees) mentioned lack of skills as the second most important obstacle. For example, Djibouti Container Service (DSC) has identified major skills gaps in key sectors where Djibouti has growth potential for the private sector

(World Bank, 2018b). These human capital deficits are holding back growth. Although there are seven technical high schools one in the hospitality sector and six in the manufacturing and trade sectors), they are few in number and not sufficiently efficient (UNCTAD, 2015).

Figure 22: Obstacles encountered by Djibouti companies, in percentage

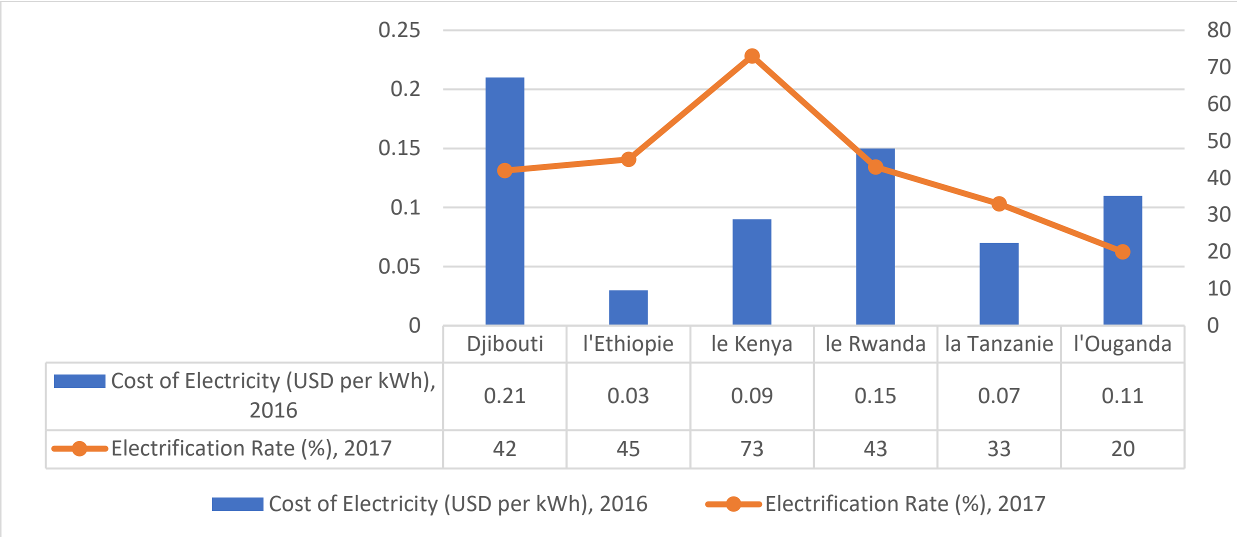


Source : UNCTAD calculations, based on data from World Bank enterprise surveys in 2013

Water, electricity, and labor are the three factors that, due to their high cost and scarcity, represent the main obstacles to economic development and private sector growth. These trends have been exacerbated by an unfavorable climate, with droughts and a general lack of water, combined with economic shocks that have led to a steady deterioration in the country's competitiveness, its financial situation and its economic and social infrastructure.

Djibouti is one of the countries that offer electricity services at a fairly high cost. But it is important to note that this cost has decreased over the years. In 2012, one had to pay FDJ 60.3 to benefit from a kWh of electricity. This price has dropped to FDJ 50.9 in 2020, a decrease of FDJ 9.4 (Republique de Djibouti, 2022). The country's capacity to generate electricity is based primarily on diesel-fired power plants, and electricity imported from Ethiopia comes from hydroelectric projects. The country's reliance on expensive imports of diesel and electricity from Ethiopia contributes to Djibouti's significantly high electricity costs compared to East Africa. Electricity in Djibouti is eight times more expensive than in Ethiopia and three times more expensive than in Tanzania (Figure 23).

Figure 23: Cost of electricity and electricity rates, 2016 and 2017



Source: Research HKTDC (2019)

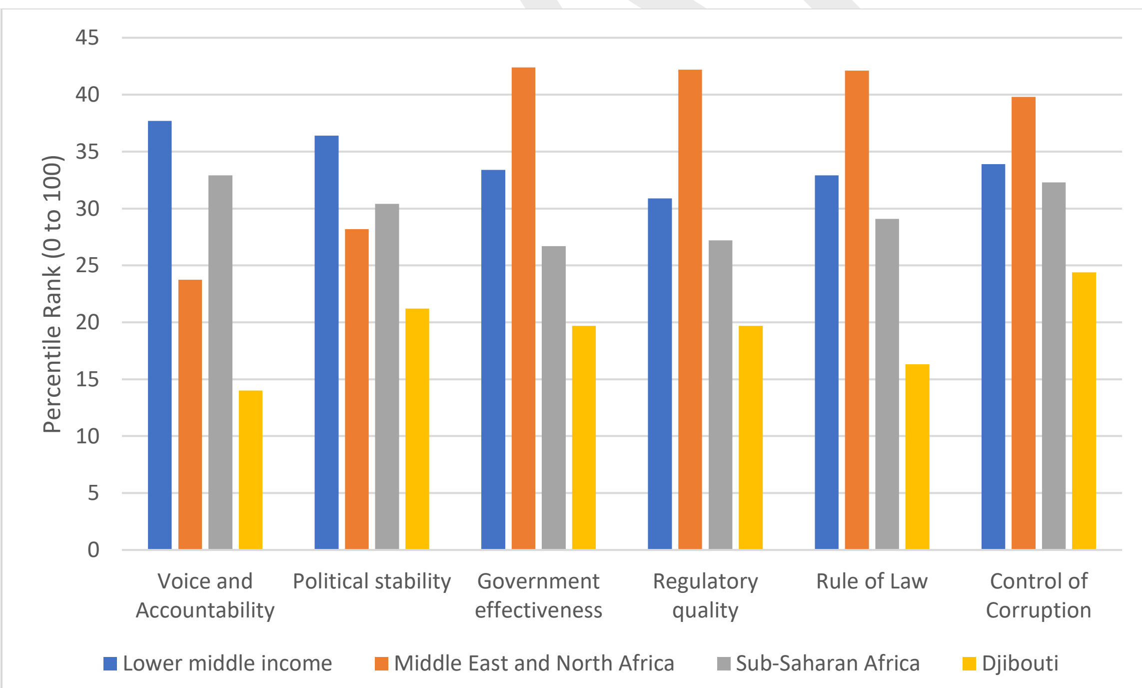
An ambitious plan to transition from 100 percent fossil fuels to 100 percent renewable energy by 2020 was outlined in the Vision 2035 long-term development plan, published in 2014. Despite significant wind, solar and geothermal energy potential and significant investments, this goal has not yet been achieved. Nevertheless, the electricity situation in Djibouti is expected to improve over the next few years, particularly in terms of supply. First, electricity imports from Ethiopia will increase as large-scale hydroelectric projects come on stream in that country, particularly the Grand Renaissance Dam. Second, Djibouti is seeking to develop its renewable energy sector. The Djibouti Electricity Company used to have a monopoly on the generation, transmission and distribution of electricity until 2015, when the authorities liberalized power generation in order to encourage the development of renewable energy sources.[31] According to the Renewables Readiness Assessment by the International Renewable Energy Agency (IRENA), renewable energy accounts for 35 percent of total energy supply, virtually 100 percent of which is bioenergy (IRENA, 2022). IRENA estimates that Djibouti has significant renewable energy resources. Geothermal, wind, and solar energy can be developed to bring better quality energy services to the country's populations. Regional cooperation is essential to meet the growing demand.[32] For example, the Africa Clean Energy Corridor initiative requires investments of $25 billion per year (until 2030) in electricity generation, and an additional $15 billion in grid infrastructure.[33] The initiative also includes support for long-term energy planning, in the form of training workshops, assessment of energy pools to strengthen the capacity of countries to plan, operate and monitor power systems.[34] As a result of Djibouti's renewable energy readiness assessment, the country has included renewable energy in the electricity master plan, and the electricity law provides tax exemptions for all renewable energy equipment and has developed a national strategy for energy conversion focusing on renewable energy.

[31] https://oxfordbusinessgroup.com/overview/fuel-growth-diversifying-energy-mix-and-securing-adequate-supply-eye-expansion-central-development
[32] https://www.irena.org/cleanenergycorridors/Africa-Clean-Energy-Corridor
[33] https://www.irena.org/cleanenergycorridors/Africa-Clean-Energy-Corridor
[34] idem

In order to address the problem of water scarcity to ensure access to safe drinking water for the entire population, as mentioned in Section 3.2.2, Djibouti has implemented a project to supply drinking water from Ethiopia. This cross-border project, which costs $339 million, aims to provide sufficient water for the development of an industrial base in Djibouti. It also intends to supply several regions in the hinterland that have limited access to water. This project was inaugurated in June 2017 (République de Djibouti, 2022).

During the preparation of the NDP "Djibouti ICI" and the voluntary national review on the monitoring of the SDGs, the stakeholders and populations who were being consulted judged the public administrations to be inefficient with decreasing productivity, attesting to the deterioration of administrative governance (Republic of Djibouti, 2022). According to the global governance indicators, the weakest indicator is the Voice and Accountability Index, where Djibouti only ranks 14 (on a scale of 1 to 100, with 100 being the best performance), and is ranked 173rd out of 193 countries. This is the equivalent of the 47th place out of 53 African countries. Compared to the average for Sub-Saharan Africa, Djibouti has the lowest rank on all indicators (Figure 24). The major challenges will therefore be to accelerate the effective implementation of decentralization and deconcentration policies by completing the legal and institutional framework for decentralization. It is necessary to strengthen the capacities of decentralized local authorities (regional councils) with adequate supervision and support.

Figure 24: Good Governance Indicators, 2021, unweighted average by region



Source. UNCTAD based on the Worldwide Governance Indicators.

4.2. Exploiting the link between trade and structural transformation

To reduce export volatility, Djibouti needs to strategically target economic diversification. Moving forward in a sustainable manner requires creating linkages between different parts of the economy and developing private investment opportunities that will generate the jobs and value added needed in Djibouti to eradicate poverty. In 2019, the country exported only 458 products (out of a possible 5,018 products according to the HS six-digit classification), compared to the African average of 1,566 products. [35]

The identification of export potential and structural transformation are based on the results discussed in UNCTAD (2021) and UNCTAD (2022). UNCTAD (2022) uses the product space method, which gives a first indication of the products that could be produced by a country. However, this method is subject to uncertainties in the case of poor quality trade data, as the technical calculation cannot differentiate between statistical and actual exports. According to the enterprise survey mentioned in Section 4.1, there are few companies in the manufacturing sector (22 percent of the companies surveyed), the majority of which are in food and beverage production and vehicle manufacturing. Nevertheless, even though this production capacity is limited, it offers opportunities to promote diversification. Encouraging investment and production in mechanical manufacturing promises spillover benefits in terms of technology use, knowledge, and skills. To promote diversification, it is essential to invest in new activities.

According to UNCTAD (2022), the largest potential markets in terms of demand are Asia and Europe. Nevertheless, Africa remains an important strategic market due to increasing population and GDP growth, as well as increased market access and investment opportunities under the African Continental Free Trade Area (AfCFTA).

Exploiting regional export opportunities

The most demanded potential new products in African countries are plastics and their derivatives (e.g., ethylene polymers, (HS 3901)), iron and steel products (HS 7306), dairy products, and chemicals. Figure 25 lists the top 9 product groups, summarized at the product level by 4-digit HS codes, that have export potential using the product space method. The largest potential markets in terms of demand are Egypt with 27 percent of the total demand, followed by Morocco (10 percent) and Nigeria (9 percent). The AfCFTA will play an important role in increasing market access and connectivity with countries. To date, Djibouti has preferential access to the Egyptian market under COMESA and IGAD, but not to Morocco and Nigeria. The AfCFTA should open up additional trade opportunities.

An important step toward increasing exports is not only to promote diversification, but also to address the trade barriers that hinder current export growth. On the continent, these obstacles stem from tariff and non-tariff barriers such as lack of infrastructure, divergent regulatory requirements, lack of information on export opportunities, and lack of business contacts. Because of these

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[35] Export and import data should be treated with caution. As a transportation hub, exports and imports may be reported in Djibouti's trade statistics, but are then transported to the mainland.

barriers, there is a large untapped potential for intra-African trade of $21.9 billion (UNCTAD 2021).

According to UNCTAD (2021), Djibouti has an untapped export potential to Africa of $2.8 million, equivalent to about 41 percent of current exports. The sectors with the greatest potential are "Edible vegetables, and certain roots and tubers" (HS 07), particularly leguminous crops, and "Tea, coffee, maté and spices" (HS 09) (Figure 24). The " Edible vegetables and certain roots and tubers" sector shows an untapped potential of $913,000, of which $347,000 is not realized due to non-tariff barriers, and $565,000 is expected to be achieved by 2025 due to GDP and population growth. Red beans represent the largest share of the sector's export potential. In 2019 alone, interest in Djibouti's red beans increased by 115 percent compared to the year 2018[36]. With the partial tariff liberalization envisaged under the AfCFTA, where LDCs benefit from a longer liberalization period (10 years versus 5 years for non-LDCs), an additional $103,000 in export growth could be achieved.

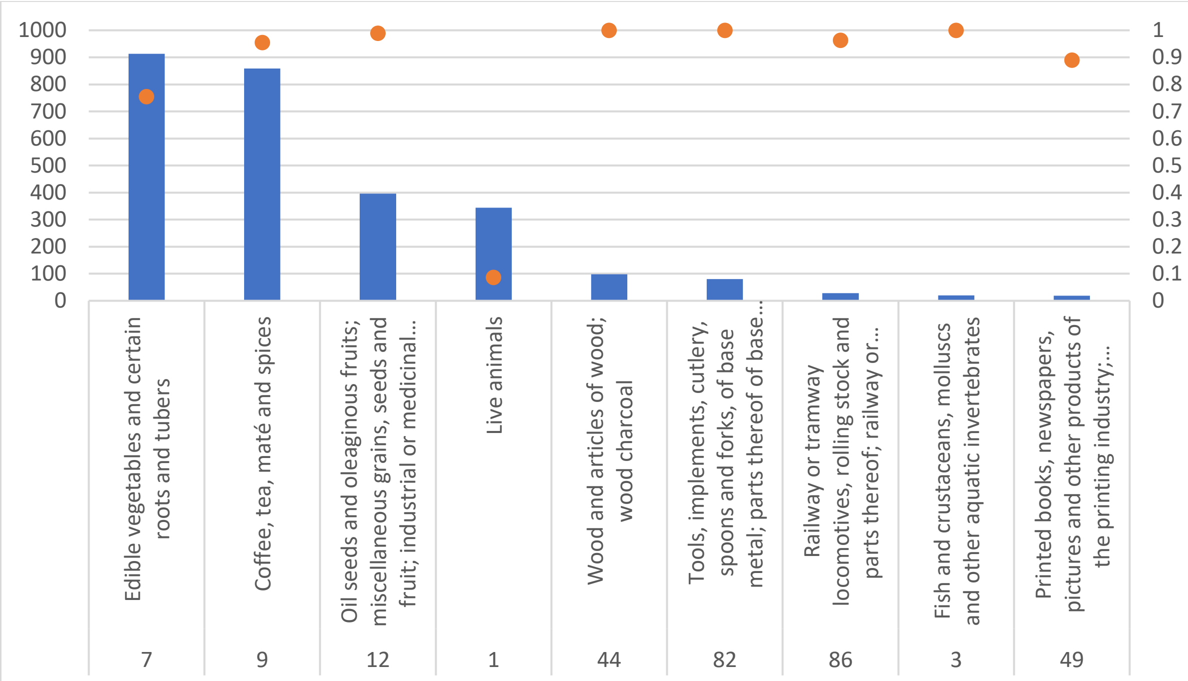
The second largest sector with untapped potential is tea, coffee, maté and spices (HS 08): $859,000 of which black tea and coffee are the main products. In 2019, Djibouti's black tea market increased by 53 percent compared to 2018.[37] Increased access to African markets as a result of the tariff liberalization under AfCFTA could add an additional $41,000 to Djibouti's exports.

There are very few manufacturing sectors among the main sectors with export potential to Africa. These are "Wood and articles made of wood" (HS 44: $98,000), "Tools, implements, cutlery" (HS 82: $80,000) and "Railway parts and components" (HS 86: $28,000).

[36] https://www.selinawamucii.com/insights/market/djibouti/kidney-beans/

[37] https://www.selinawamucii.com/insights/market/djibouti/black-tea/

Figure 25: Djibouti Untapped export potential to Africa, Top sectors with potential >$1,000



Source: UNCTAD based on UNCTAD 2021.

Due to the small size of the domestic market, Djibouti depends on imports. For example, according to a study by the Republic of Djibouti (2014), low agricultural yields and low fertilizer use are partly the result of difficulties in accessing agricultural inputs. The AfCFTA will also improve access to needed inputs and intermediate services. With respect to imports from Africa, there is untapped potential in the sectors of "Animal and plant fertilizers" (HS 31) worth $29.3 million, "Sugars and sugar refineries" (HS 17) worth $19 million, and "Vehicles" (HS 87) worth $12.8 million, "Organic chemicals" (HS 29) accounting for $10.5 million, and "Apparel and apparel accessories" (HS 62) worth $8.7 million to name the top five sectors.

Agriculture and the blue economy

Severely handicapped by unfavorable agro-climatic conditions (low rainfall as well as aridity and salinity of the soil), the contribution of the agricultural sector (agriculture, forestry and fishing) is very modest (UNECA, 2021). Nevertheless, diversification of agriculture and agro-industry remains an important channel to reduce the vulnerability of the population to drought and climate change. The greatest opportunities in agriculture lie in dairy products, meat production, and edible vegetables, including cashews. More investment is needed to add value, including in modern refrigerated slaughterhouses. To date, the country has only one government-owned slaughterhouse.

In addition, Djibouti's advances in maritime trade and the gradual establishment of a logistics and trade hub position the blue economy (BE) as a source of growth in the medium term. The basic foundations for the economy will contribute to diversification and structural transformation within the framework of a rational and judicious exploitation of natural resources, including marine and aquatic resources. The potential of Djibouti's blue economy is immense, representing nearly 19 percent of national GDP and about 27 percent of the total employment (Republique de Djibouti, 2021a). The value added of the blue economy is estimated at $566 million, of which 81 percent is generated by the transport sector, 14 percent by electricity production and distribution, and 3 percent by tourism. (Table 5)

Table 5: Value added by the blue economy between 2017 and 2018, in $

Economic activity	**Value added by the blue economy**
Agriculture, forestry and fishing	7 185 401
Production and distribution of electricity, gas, steam and air conditioning	82 838 360
Transportation and storage	458 095 239
Accommodation and catering activities	15 958 867
Information and communication	2 195 148
Total	**566 273 015**

Source: UNCTAD based on UNECA (2021), Socio-economic and ecological assessment of the blue economy in Djibouti

Efforts have been made to promote entrepreneurship: for example, the Djibouti Social Development Agency (ADDS) has provided fishing boats under leasing contracts (UNCTAD, 2015).

Industrial sector

Developing processing activities and value-added services is a powerful way to build a sustainable competitive advantage. Value-added logistics services are an important part of supply chains. For example, for Singapore, the leading regional and international logistics hub in Southeast Asia, the port-related logistics industry is one of the strategic business sectors, as it also provides value-added services such as labeling, assembling, packaging and quality control contributing to employment and competitiveness of port services. For example, limited manufacturing functions such as assembling are operated in Singapore to meet the demands of customers (UNESCAP, 2002). Similarly, ports in China and Taiwan Province of China have allowed manufacturing facilities in free trade zones[38] close to the ports. The Djibouti international free zone could be used specifically for the assembly of vehicles and for consumer goods, the majority of which are re-

[38]According to the Revised Kyoto Convention of the World Customs Organization, Specific Annex D, Chapter 2 "Free zones are defined as a part of the territory of a contracting party into which goods brought in are generally considered not to be in the customs territory for the purposes of import duties and taxes" (https://www.wcoomd.org/-/media/wco/public/fr/pdf/topics/facilitation/instruments-and-tools/conventions/kyoto-convention/revised-kyoto-convention_fr.pdf?la=fr)

exported.[39] It should be noted that the zone, inaugurated in 2018, will take ten years to develop at a total cost of $3.5 billion, and will be administered by the Government of Djibouti and three Chinese companies (UNCTAD, 2019). Four industrial clusters are envisioned for the zone: logistics, trade, business support, and manufacturing. A few companies have already expressed interest in establishing themselves in the zone: Wilmar, a Singaporean agribusiness company; Osram, a Taiwanese lighting manufacturer; and Golden Africa, a Kenyan food group.[40] It is necessary that the benefits and opportunities created by the zone be shared among all population groups, whether through job creation for Djiboutians, or through fiscal redistribution. In fact, investors in the zones are required to employ Djiboutian staff for at least 30 percent of their workforce by the end of the first year of operation and at least 70 percent after five years of operation (UNCTAD, 2019).

In addition, Djibouti Damerjog Industrial Free Trade Zone is an industrial free trade zone project focused on heavy industry, petrochemical projects, and livestock farming.[41] A significant part of the funding for these investments comes from China, as well as from Djibouti's new sovereign wealth fund (see Section 4.5 for financial challenges).

Services sector

Apart from commercial services related to ports and free zones, the potential for the tourism and digital economy sectors is very promising.

Tourism: The sector links and integrates several sectors of the economy, including travel, accommodation, catering, and leisure, and represents the most complete value chain in the services sector, attracting many SMEs (UNCTAD, 2022). However, these linkages may suffer from an over-reliance on imported inputs (UNCTAD, 2022). In light of the regionalization trend induced by the COVID-19 pandemic and limited business tourism, focusing on beach tourism in the short to medium term appears to be most promising. Djibouti's stability and geographic proximity to landlocked Ethiopia position the country as the natural maritime destination in the region. Djibouti's competitiveness with the offerings of regional and extra-regional competitors (e.g., the Gulf States, Kenya) and how best to link with the Ethiopian authorities' current efforts to develop tourism assets (e.g., adding a "maritime leg" to the available tours) need to be assessed (Banque Mondiale, forthcoming). In 2019, Djibouti adopted a strategic framework law for the development and promotion of tourism in Djibouti and a tourism master plan. The goal is to reach the number of 500,000 tourists per year by 2030. Geographically, this approach focuses on three tourist areas with specific regulations: Tadjourah, Day and Assal for thalassotherapy tourism; Dikhil and Lake Abbe for ecotourism and Obock as a reception point for cruise lines (WTO, 2022).

Digital economy: In the services sector, information and communication technologies (ICTs) play an important role in developing and linking various components of value chains, which boosts

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[39] https://oxfordbusinessgroup.com/overview/leveraging-strengths-partnering-free-trade-zones-port-facilities-attract-investment-wider-range

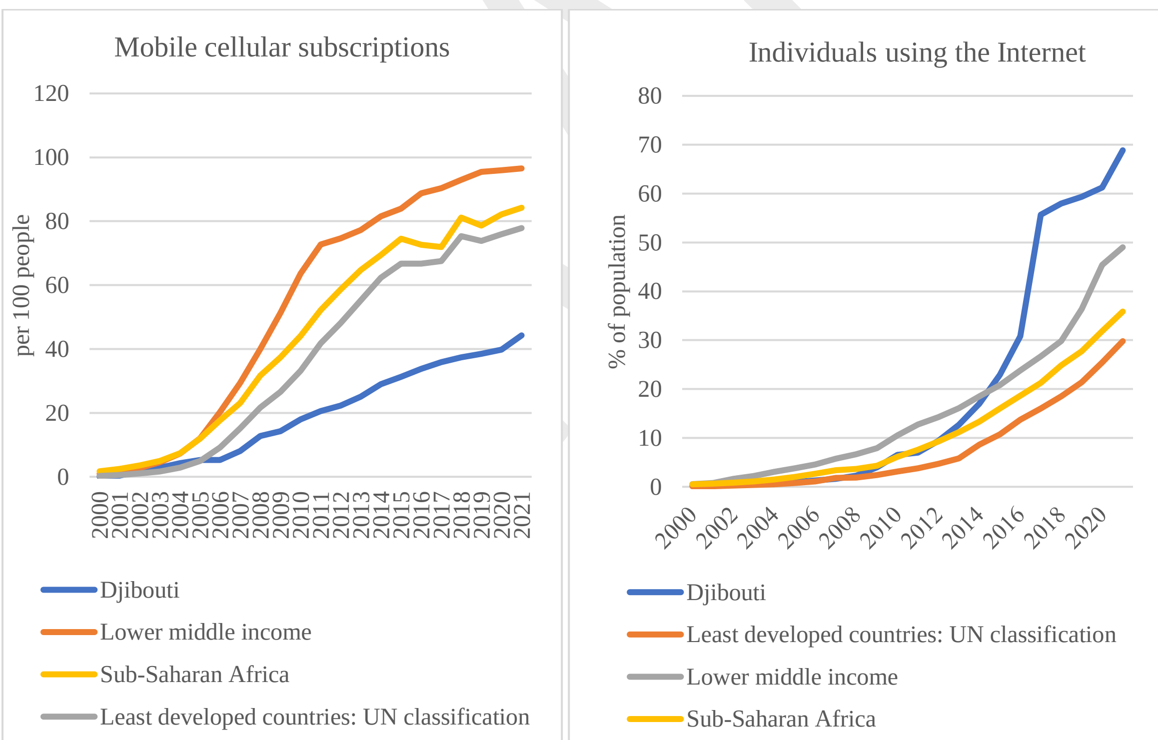
[40] https://oxfordbusinessgroup.com/overview/leveraging-strengths-partnering-free-trade-zones-port-facilities-attract-investment-wider-range

[41] https://www.ft.com/content/15aefce3-2e6b-4e1a-b480-bfc066f7d8dd

competitiveness through enhanced product quality and diversity, and facilitates access to relevant market information. The importance of the digital economy is highlighted by the creation of a new ministry, the Ministry of Digital Economy and Innovation. Thanks to its exceptional geostrategic position, Djibouti has real potential to become an international digital hub. To date, 14 submarine cables have been installed, which has improved the population's access to the internet. Between 2010 and 2021, the percentage of the population using the internet has gone up from 6 percent to 68.9 percent. As shown in Figure 26 (right) this increase is higher than the average for Sub-Saharan Africa and LDCs. In contrast, however, mobile cellular subscriptions are low at 44 per 100 people, compared to 77 for LDCs and 84 on average for Sub-Saharan Africa.

Despite the opportunities, the biggest challenges are high prices, gender and regional inequality, and sustainable financing. For example, while 61 percent of men own a cell phone, only 51 percent of women do. In addition, mobile data prices (for high consumption), represent 10.1 percent of GNP per capita, compared to, for example, 7.3 percent in Ethiopia, 6.7 percent in Kenya and 2.2 percent in Sudan.[42]

Figure 26: Use of and access to information and communication technologies (ICT), 2000-2021



Source : UNCTAD based on the International Telecommunication Union (ITU) database [accessed November 2023].

[42] https://www.itu.int/en/ITU-D/Statistics/Dashboards/Pages/Digital-Development.aspx

There are some developments that promise a further increase in ICT activity.
In 2021, Djibouti decided to open the capital of the incumbent national operator Djibouti Telecom to private investors.[43] Recently, South Sudan and Djibouti signed a fiber optic interconnection agreement [44] and Djibouti became the tenth member of the Digital Cooperation Organization.[45] In addition, in 2021 the World Bank approved a $10 million credit, funded by the International Development Association (IDA), to accelerate digital transformation. Improving ICT infrastructure will also allow for small and medium-sized enterprises to increase their use of and access to innovative financing technologies (UNCTAD, 2022).

The impact investment ecosystem in Djibouti highlights the development of the ICT infrastructure and solutions to promote a digital economy and the deepening of financial inclusion as facilitators of regional economic integration and cross-border trade in the Horn of Africa region through entrepreneurship development. The "SDG Investor Map Djibouti" also highlighted "Microfinance for the unbanked population and SMEs" as an investment opportunity. This includes increasing the reach of selected financing options for the unbanked population as well as for SMEs by using technology and alternative information, such as digital footprints and behavioral and psychometric analysis to support credit scoring[46]. The central bank has developed a strategy in 2020 to introduce new fintech solutions in the country and is regulating digital banking (BTI, 2022).

While investment is allowed in all sectors to increase financing opportunities, shipping and transit, fishing, retail, communications, electricity, water, postal services, and salt remain restricted to domestic investors.

4.3. Mitigating and adapting to environmental shocks

Djibouti signed a memorandum of understanding with African Risk Capacity in 2019 to strengthen the natural risk management capacity. As a coastal nation, Djibouti is one of the 50 most vulnerable countries in the world as far as extreme climate risks are concerned, according to the Global Climate Risk Index (BTI, 2022). This vulnerability is especially present in the area of food security. According to the ND-Gain Index[47] the country is the most vulnerable in terms of child malnutrition. Likewise, Djibouti is the 52nd least prepared country in terms of climate change, especially due to a low innovation and educational performance.[48] Thus, vulnerability to climate

[43] https://www.agenceecofin.com/gestion-publique/1207-90007-le-gouvernement-de-la-republique-de-djibouti-annonce-l-ouverture-du-capital-de-djibouti-telecom
[44] https://www.agenceecofin.com/infrastructures/2109-101367-le-soudan-du-sud-et-djibouti-ont-signe-un-accord-d-interconnexion-par-fibre-optique
[45] https://www.arabnews.fr/node/243511/monde-arabe
[4646] UNDP Project Proposal on Islamic Microfinance, 2022
[47] The Notre Dame Global Adaptation Index measures vulnerability on the one hand, and the country's ability to leverage investments and convert them into adaptation actions on the other.
[48] https://gain.nd.edu/our-work/country-index/rankings/

change is explained by high exposure to the effects of global warming coupled with a low capacity to adapt.[49]

Djibouti's long-term development strategy, Vision 2035, also states that developing measures to mitigate the effects of climate change through anti-desertification measures and sustainable water management practices is a strategic objective for the 2020s. The action plan for the implementation of the intersectoral strategy for the management of major risks has not yet been adopted and lacks preparedness and mitigation instruments. To improve food security, the Government of Djibouti has signed agreements to lease agricultural land to Sudan and Ethiopia. The adoption of new eco-technologies to better collect and conserve water and avoid erosion of cultivable land is a necessity for the proper management of natural resources. UNECA (2021) reveals vast and significant potential resources for the country's development, provided they are exploited with strict respect for the environment. This could also contribute to food security.

In January 2021, the World Bank announced that it would invest more than $5 billion to connect the east coast of the African continent of Djibouti to the west coast of Senegal through projects that promote livelihoods and restore degraded landscapes. Aimed at improving the livelihoods of populations affected by the COVID-19 pandemic, this investment will focus on climate change mitigation (BTI, 2022).

The country's largest mangrove forest, Khor Angar in northern Djibouti, has shrunk by 50 percent to a mere 60 hectares due to deforestation and decreasing freshwater inflows. The Global Environment Facility (GEF) has contributed $2 million to restore this fragile ecosystem, which was once an escape destination from the city of Djibouti and a source of local income for fishermen.

Djibouti has committed through the Nationally Determined Contributions (NDC) to reduce greenhouse gas emissions by 40 percent by 2030, an ambitious target set in 2015, which can be achieved through mitigation measures and the development of economic sectors such as renewable energy (geothermal, solar and wind). As already mentioned in Section 4.1, one of the objectives of Vision 2035 is the energy transition from heavy fuel oil-fired power plants to 100 percent renewable energy by 2035. The introduction of the National Climate Change Strategy (NCCS) in 2017 should strengthen the coherence between existing national frameworks and actions to combat climate change. Nevertheless, there is no public funding mechanism to support climate change resilience. In addition, the lack of coordination between ministries has prevented a cross-sectoral approach to integrating climate risk information into decision-making and planning.

With regard to strengthening resilience and adaptation to climate risks, the country adopted the National Adaptation Program of Action (NAPA) in 2006. It identifies the most vulnerable sectors: agriculture (especially in wadi areas), forage and livestock farming, water (salinization of aquifers, flooding and erosion), forestry and ecosystems (degradation of coral reefs, regression of mangrove areas and changes in fish stocks). But the vulnerability also extends to hydraulic and coastal infrastructures and the transportation network. Aware of the impact of climate change on the economy, the National Development Plan "Djibouti ICI" 2020-2024 has introduced the environment as a cross-cutting axis. The management of household and industrial waste is another

[49] https://ecoloadjibouti.com/afrique-entre-envie-de-developpement-et-realite-climatique/

area that deserves more attention. The capacity of landfills is limited and an integrated waste management strategy is being developed (Nations Unies Djibouti). According to the NDC Djibouti has voluntarily committed to reducing greenhouse gas emissions by 40 percent by 2030 through a combination of mitigation measures and the development of renewable energy sources. In order to achieve this goal, Djibouti must invest more than $3.8 billion (approximately 110 percent of GDP in 2021) (République de Djibouti, 2015).

The development of solar, wind and geothermal energy continues, in order to meet national electricity needs, reduce the price of electricity, and achieve a 100 percent green energy mix by 2025. Achieving SDG 13 on climate action is on track, but major challenges remain. The investment needed to maintain a similar level of emissions as in 2010 amounts to $5.5 billion. (African Development Bank, 2022b).

Finally, we should highlight the establishment of the Institutional Framework for the Protection of Biodiversity and the creation of the Ministry of Environment and Sustainable Development (MEDD) (cabinet reshuffle of May 2021). The creation of this new ministry is evidence of the authorities' willingness to focus on development that meets the needs of current generations without compromising the development of future generations through a better balance between social, economic and ecological aspects [50].

To address all these risks, the government adopted a national contingency plan for social protection in crisis situations in June 2022. This plan is part of a participatory initiative undertaken by the Ministry of Social Affairs and Solidarity (MASS) with a view to provide it with a tool for crisis management and humanitarian response to disasters in accordance with its various mandates. The development of this plan was preceded by a diagnosis of shock-responsive social protection in Djibouti. The main recommendations of the diagnosis, to enable the social protection sector to respond to disasters, are the following:

- Strengthen the entire social protection system to better reach vulnerable populations and expand the coverage of different programs.
- Adjust the design parameters of existing programs to take into account the risks to which households are exposed to as well as their vulnerabilities.
- Mobilize financial resources and explore innovative financing mechanisms (see Section 4.5)

To do this, disaster response must also be part of a crisis management cycle, which this contingency plan aims to define. Regional initiatives, such as the African Union's Green Recovery Action Plan (2021-2027), promise to improve access to climate finance and improve the efficiency in the use of financial resources.

[50] National Volunteer Assessment document - New York July 2022.

4.4. Income distribution and social protection

The previous sections have shown that economic growth has not been inclusive. To reinforce the fight against poverty and mitigate the consequences of structural adjustment policies, social protection became a priority for the Djibouti Government from the 2000s onwards, but inequality measured by the Gini index remains high, with a small decline in inequality from 45 in 2012 to 41.6 in 2017. Access to social protection for vulnerable populations is an instrument for achieving the Sustainable Development Goals (SDGs). According to a study by Brodmann and Coulombe (2017) only 15 percent of tax exemptions on food and 3 percent on fuel go to beneficiaries living in rural areas. However, most of the beneficiaries are the wealthiest of the population.

Across African countries, according to UNCTAD (2021), growth has been accompanied by an increase in inequality in 14 countries (Burundi, Congo, Djibouti, Eswatini, Ethiopia, South Africa, Ghana, Malawi, Mauritius, Mozambique, Seychelles, Tanzania, Chad, and Togo). In contrast, Algeria, Burkina Faso, Cabo Verde, Gambia, Guinea, Kenya, Lesotho, Liberia, Mali, Mauritania, Morocco, Niger, Nigeria, Rwanda, Sierra Leone, Tunisia, and Uganda have experienced inclusive growth.[51]

With the creation of the Secretariat of State for National Solidarity (SESN) in 2008, which became the Secretariat of State for Social Affairs (SEAS) in 2016 and was transformed into the Ministry of Social Affairs and Solidarity (MASS) in 2019, an arsenal of legal texts was adopted by the Government of Djibouti in order to strengthen the areas of competence of this ministerial entity. These legal texts have enabled the MASS to extend its roles and responsibilities in the fight against poverty and the promotion of national solidarity to include the humanitarian response to disasters. Thus, the institutional framework developed and adopted by the Government of Djibouti has provided MASS with the technical, human and financial means to carry out its missions. [52]

The National Assembly passed a law enacting the National Social Protection Strategy 2018-2022, which focuses on four priorities: (1) the right to food security for households below the national poverty line, (2) a guaranteed income for children living in households in extreme poverty, (3) a guaranteed income for the elderly without family support and people with disabilities, and (4) income support for those who cannot work due to life accidents. The International Labour Organization (ILO) has acknowledged the law as the first of its kind to bring together various social protection schemes under a single framework in the country. However, implementation has not yet taken place (BTI, 2022).[53]

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[51] For example, in Gambia, also an LDC, the Gini index declined from 47 in 2003 to 35 in 2015, and nearly half of them had a consumption of less than $1.9 per day in 2003 compared to 10.3 percent in 2015 (UNCTAD, 2021). Inclusive growth in Gambia may be the result of several factors: the development of the agricultural sector as well as spending on poverty reduction programs has helped alleviate rural poverty. In addition, the Human Development Index improved in Gambia in 2003-2015, registering an average annual increase of 0.94 percent, compared to a global rate of 0.82 percent. The Economic Freedom Index and the Corruption Perceptions Index also increased, reflecting improvements in the quality of institutions (UNCTAD, 2021).

[52] https://primature.gouv.dj/attributions-des-ministeres/?msclkid=3c2bb4a6cebf11ec89b34fd1237fb5c5

[53] https://bti-project.org/en/reports/country-report/DJI

In June 2022, the World Bank approved a $30 million grant to protect poor and vulnerable communities. It will provide social transfers to households affected by multiple crises: health, food and climate.[54]

To fight poverty, the concept of microcredit was established by the Fund for Social Development (FSD), the Djibouti Agency for Social Development (ADDS) and the Caisse Populaire d'Épargne et de Crédit de Djibouti (CPECD) (Djibouti Savings and Credit Bank). Through 2016, one-third of Djiboutian households had access to microcredit, primarily provided by one of the three microfinance institutions. Using a 2015 household survey, Ali and Mughal (2022) find no effect of microcredit on poverty reduction, confirming the doubt of microcredit effectiveness discussed in the literature[55] (for a review of the literature, see Ali and Mughal, 2022). The authors argue that often microcredit does not reach the poorest layer of the population. They recommend that the three institutions must distribute credits more effectively, targeting the poorest and the populations dependent on agriculture and fishing, which are highly vulnerable to climate change.

4.5. Sustainable financing solutions

Infrastructure projects have been financed largely through external debt. The financing of new projects needs to be assessed within a budgetary framework and against the implications for employment and structural transformation as discussed in Section 4.2.

Because of its geographic location, Djibouti has a comparative advantage in the logistics and transport sector, which are, however, very capital intensive. The debt burden has limited Djibouti's fiscal space for much-needed investments in the social sectors and in job creation. The debt burden will even increase in the coming years due to deferred debt services (granted during the COVID-19 pandemic), payments for the Djibouti-Ethiopia water pipeline, and railway loans (World Bank, 2022). More sustainable financing solutions are needed, such as greater private sector participation, debt diversification, and domestic resource mobilization.

Tax revenue declined from 14.1 percent of GDP in 2013 to 11.3 percent in 2020, and non-tax revenue declined from 9.2 percent to 7 percent over the same period. Taking into account donations, total revenue amounted to 22.3 percent of GDP. According to UNCTAD (2020), the African average of tax revenue to GDP ratio was 18 percent. Total expenditure (including current and capital expenses as well as dept repayment) declined from 26.8 percent in 2013 to 24.1 percent in 2020, resulting in a negative balance of 1.8 percent in 2020. After a reduction in capital spending in favor of health spending due to the COVID-19 pandemic, capital and recurrent spending on public infrastructure has decreased to 41 percent of total spending in 2021 (from 52 percent in 2020) (World Bank, 2021).

There are some recommendations for mobilizing domestic resources for poverty reduction:

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[54] https://www.banquemondiale.org/fr/news/press-release/2022/06/29/djibouti-new-support-to-protect-poor-and-vulnerable-communities-and-strengthen-resilience-to-future-shocks

[55] Pour une revue de littérature, voir Ali et Mughal (2022).

- Review tax exemptions
- Reduce taxes on food products to favor poor households
- Strengthen the fight against illicit financial flows
- Strengthen public-private partnerships (PPP)

Inclusive growth is also based on objectives of creating marketable jobs in line with the level of training of agents. So far, there has been no shortage of ideas on the axes of Djibouti's development, but while the authorities have been able to identify them, the design and implementation of operationalization strategies have been inadequate. In other words, public governance has not been able to coordinate development actions, establish synergy between ministries and thus act on each of the levers conditioning the success of the targeted objectives and the implementation of related projects (UNCTAD, 2015).

Donor assistance finances the majority of sectoral energy investments in Djibouti. Incentives for private actors are minimal, despite various tax exemption schemes. For example, in free trade zones, enterprises are not subject to any direct or indirect taxes or taxation including income tax (Research HKTDC, 2019). This tax exemption is granted for up to 50 years.[56] In addition, the government added certain food products (yoghurt, pasta, and liquid milk) to the list of products subject to excise duty. According to WTO (2022), the authorities have indicated that the taxation of food products is intended to protect emerging industries.

Inclusive growth requires a reprioritization of spending. Spending to achieve the SDGs involves expenditure to build physical infrastructure and human capital for inclusive growth, jobs and poverty reduction (IMF, 2019).

Although there are several funds to finance adaptation to climate change, such as the Green Climate Fund and the Adaptation Fund, IFRC (2022) shows that none of the 30 most vulnerable countries were among the top 30 recipients of funding per capita. These countries often lack the institutional capacity to demonstrate their readiness to effectively use funds for climate change adaptation. It is imperative that the international community, donors, and development partners address the barriers to accessing these funds. According to UNCTAD (2022b), climate finance under the United Nations Framework Convention on Climate Change (UNFCCC) should be more flexible and in concessional forms to support LDCs beyond reclassification. It also recommends the possibility for central banks in developed countries to purchase low-yielding government bonds issued by LDCs to finance climate change adaptation.

[56] https://www.womenconnect.org/fr/web/djibouti/access-to-markets

5. Conclusion

Djibouti's economy is a small, extroverted economy, which makes it extremely sensitive to any exogenous shock. In the fragile Horn of Africa, Djibouti is an oasis of stability that has successfully leveraged its geostrategic location to transform its small, resource-constrained economy into a fast-growing regional hub. Largely driven by trade with Ethiopia, real GDP growth averaged 8.5 percent over the 2010-2020 period.

The strong increase in GDP per capita was largely driven by massive investments in transport and logistics. However, these investments were, on the one hand, mainly accumulated in capital-intensive sectors with little job creation, and on the other hand, financed by a non-concessional public debt that exposed the country to a high risk of debt distress. As a result, GDP per capita growth has been disconnected from its population, leading to high unemployment and limited progress in human capital development. Thus, this vulnerability profile highlights three areas that pose the greatest challenges to a smooth and dynamic recovery:

- **Weak private sector and high unemployment:** The concentration of investment in the logistics and transportation sectors in recent years has not created sufficient links to the local economy and job creation. Economic opportunities exist but often suffer from a lack of diversified investments. There are four main reasons for this situation: (a) entrepreneurs face an insufficiently favorable business environment in terms of access to electricity, financing, and entrepreneurial services; (b) lack of competition and dominance by monopolies and state-owned enterprises; (c) low levels of voice and accountability as well as corruption that reduce business investment and productivity; and (d) low literacy rates and a mismatch between demand and supply in the labor market.

- **Low human capital and gender inequality in literacy rates**: The prevalence of malnutrition is one of Djibouti's greatest vulnerabilities with respect to its human capital. With less than 0.1 percent of Djibouti's land considered arable and a lack of access to water, it is difficult to maintain sustainable agriculture or for families to feed themselves. Due to a combination of high rates of communicable disease infection, low agricultural production, and extreme poverty, infant mortality rates are increasingly high. In the area of education, the challenge is less about accessibility than about quality. The literacy rate for women is currently 39.5 percent, compared to 60.1 percent for men.

- **Vulnerability to climate change presents a high risk of aggravated food insecurity**: Climate disruption is undoubtedly the most visible risk, as natural disasters such as droughts and floods that hit Djibouti between 2017-2019 caused huge human losses and material damage, showing the fragility of the way of life of a large part of the population and of the productive capacities located in the coastal regions. A temperature increase of 2°C can lead to costs of up to 2 percent of GDP in 2040 and 3 percent in 2060.

Djibouti's Vision 2035 aims to strengthen economic diversification through a wide range of reforms, including improving the business climate, reducing input costs, supporting small and medium-sized enterprises (SMEs), coupled with large-scale infrastructure projects. Significant progress has been made in some areas, but further efforts are needed to address the most critical constraints that limit returns on investment, ownership of those returns, and access to and cost of financing.

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Appendix: Strategic considerations for a smooth and dynamic reclassification

The risk of Djibouti graduating too soon from the LDC category is that its many vulnerabilities could put it in the case of "countries graduating from the LDC category with a multitude of challenges, including poverty and inequality, particularly gender inequality, insufficient structural transformation and productive capacity, and vulnerability to economic and climatic shocks. A five-year preparatory period would be necessary for Djibouti to effectively prepare for a smooth transition, as it would need to prepare for its reclassification while planning for post-COVID-19 recovery and implementing policies and strategies to repair the economic and social damage caused by the pandemic and potential external shocks"[57].

a) Development of the private sector

Economic opportunities exist but often suffer from a lack of investment. There are four main reasons for this: (a) entrepreneurs face an insufficiently favorable business environment in terms of access to electricity, financing, and entrepreneurial services; (b) lack of competition and dominance by monopolies and state-owned enterprises; (c) low levels of voice and accountability and corruption that reduce business investment and productivity; and (d) poor literacy rates and a mismatch between demand and supply in the labor market.

b) Development of human capital and distribution of national wealth

Implementation of national policies to promote food security and nutrition is hampered by poor coordination and limited national capacity. Stronger partnerships to reinforce national capacities in school feeding, nutrition, social protection, emergency preparedness, equitable support to agricultural production, and vocational training for supply chain management. Weak disaster preparedness and response capacity also erodes the resilience of poor households.

c) Adaptation to climate change

According to UNCTAD (2022b), climate finance within the UNFCCC framework should be more flexible and in concessional forms to support LDCs beyond graduation. It also recommends the possibility for central banks of developed countries to purchase low-yielding government bonds issued by LDCs to finance climate change adaptation.

d) Increase fiscal space

In order to increase fiscal space for necessary social sector spending, Djibouti must prioritize concessional borrowing, strengthen debt management, improve the management of public enterprises, and expand its tax base.

[57] Document New York conference, A/CONF.219/2022/3*, Fifth United Nations Conference on the Least Developed Countries, New York, 17 March 2022 Item 273 and 274.