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Trade Capacity Building and Private Sector Development in the Greater Mekong Sub-Region

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Introduction

Trade capacity-building in developing and least developed countries (LDCs) is of prime importance in this era of globalisation. Trade is one of the means of achieving socio-economic development and bringing a country on the path towards growth. While the government plays a very important role in formulating policies and creating a conducive environment, increasingly the private sector is also gaining importance. This paper specifically looks at the trade capacity building in the Greater Mekong Sub-region (GMS), elaborates the trade and investment environment, the role of private sector and analyses the challenges and opportunities that await the region.

The GMS comprising Thailand, Vietnam, Myanmar, Yunnan (China), Cambodia and Lao PDR with a population of about 303 million people is predominantly agrarian in nature with 80 percent of the population dependent on subsistence agriculture. Along with its strong agricultural base, the GMS contains vast amounts of natural resources, such as timber, fisheries, a wide variety of minerals, petroleum, natural gas, coal, and also offers some of Asia's best hydropower potential. Political and governance issues as well as weak institutions and infrastructure, resulted in inadequate attention to the development of the private sector in these economies.

With the exception of Thailand, which has had a free market economy for decades, the GMS economies were previously centrally planned and characterised by state-owned means of production. Over a span of just 60 years, GMS countries have moved through a number of political-economic formations – colonies, monarchies, military dictatorship and communist republics.

Despite marked disparities in economic development between its members, the sub-region is extremely dynamic with annual growth rates averaging above six percent per annum in recent years.

The motivation to open up their economies paved the way for sub-regional economic cooperation, but equally important was the

Table 1: Socio-economic indicators 2005

		Cambodia	Yunan*	Lao PDR	Myanmar	Thailand	Vietnam	Total
Population	in mn	14.1	92.3	5.9	50.6	65.	83.8	312.2
GDP at market price	in US$mn	5,400	75,362	3,200	8,700	180.600	52,100	325,362
Real GDP Growth	in percent	6.0	11.3	7.0	2.9	4.5	8.4	6.7
GDP per capita (Current)	in US$	348 (2004)	681 (2003)	402 (2004)	168 (2003)	2,544 (2004)	500	795
Total Trade	in US$mn	6406	7978	1268	5428	215,169	66,742	302,991
FDI Inflows	in US$mn	131	436	17	556	3437	2400	

* Yunnan and Guangxi data as of 2003

Source: Cross border Infrastructure to Maximise the Benefits of GMS Economic Cooperation, www.imf.org/external/np/seminars/eng/2006/mekong/na3.pdf (accessed on March 15, 2007)

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reduction in political and security tensions that beset peninsular Southeast Asia throughout the 1970s and 1980s. The end of the Cold War brought about an improved political and security climate in the region, and at the same time the member countries recognised that their future well-being depended on economic and social cooperation.

Table 1 validates the disparities that exist among the GMS countries in terms of foreign direct investment (FDI) flows and total trade. However, as far as real gross domestic product (GDP) growth is concerned, countries like Vietnam, Cambodia and Lao PDR are doing much better than China and Thailand.

From Battlefield to Market Place

The GMS is one of the fastest growing sub-regions in the world. From the year 1994 to 2004, GDP in the sub-region grew at an average annual rate of over six percent, in spite of a number of adverse shocks including the 1997 financial crisis, slowdown in the global and regional economies in 2001, onset of the severe acute respiratory syndrome (SARS) in 2003, and more recently, the ongoing threat from avian flu and the persistent rise in oil prices[1].

GMS economies are diverse and, therefore, can benefit from close cooperation. For instance, the trading relationship between Thailand and Lao PDR illustrates complementarities at work in terms of different factor endowments and levels of economic development. Thailand provides a significant portion of Lao PDR's demands for manufactured goods and buys a significant share of Lao PDR's resource-based exports such as hydroelectric power and timber.

The direction of trade over the past few years suggests a rapid expansion of GMS economies' trade both among themselves and with the rest of the world. Over the 2000-2004 period, the recorded trade with the world rose at a rapid compound annual average rate of 22 percent, but trade flows within the GMS increased even faster at a rate of 25 percent[2].

As would be expected, the share of intra-GMS trade in total trade is higher for the smaller economies than for the larger ones. But the larger countries, especially Thailand and Vietnam, show notable increases in the past few years. Among the countries, Lao PDR's share is the highest, probably reflecting its landlocked geography. Recorded trade flows from the Lao PDR to other GMS countries declined during 2001-2004 to a still-high share of 63 percent.

Some of the potentially important factors contributing to this increase in intra-GMS trade are proximity of the countries to each other and better physical connectivity through cross-border infrastructure.

Further, there exist bilateral trade and investment agreements and regional cooperation agreements through the Association of Southeast Asian Nations (ASEAN), the GMS Economic Cooperation Programme and the Ayeyawadi-Chao Phraya-Mekong Economic Strategy (ACMECS) framework[3].

Bilateral trade between the GMS countries has also been increasing because of trade-promotion policies being implemented at the borders. For instance, according to Cambodian officials, annual trade volume between Vietnam and Cambodia is expected to grow by 27 percent per year to reach US$2.45bn by 2010. Similarly, bilateral trade between Laos and Vietnam can be quadrupled to reach US$1bn by 2010. Trade between Vietnam and Cambodia reached US$240mn in 2006, a year-on-year increase of 30 percent[4].

Vietnam signed a bilateral trade agreement (BTA) with the US a few years ago and Thailand is currently negotiating BTAs with the US and Australia respectively. Indian companies are also making a foray in this region. The Confederation of Indian Industries (CII) has joined hands with Asian Development Bank (ADB) and established a Mekong Development Forum in November 2005, which seeks to expand India's share of trade in the GMS region.

While Myanmar, China and Thailand are its major trading partners, trade with Vietnam, Lao PDR and Cambodia has been negligible. The volume of border trade has increased, reaching the peak level of US$411mn in 2000-01 of which 65 percent is accounted for by trade with China. To facilitate trade at the border, Myanmar has allowed the use of other currencies such as Kyat, Yuan, Thai Baht and Lao Kip.

China at present has signed BTAs on border trade with Myanmar (1994 and 1997) and Vietnam (1998).

Table 2: Share of Intraregional Trade to Total Trade (percent of total trade)

Country	1998	1999	2000	2001	2002
Cambodia	31.5	22.0	19.5	27.3	24.5
Lao PDR	65.7	70.6	65.5	68.6	67.8
Myanmar	18.5	27.6	28.9	34.0	35.6
Thailand	5.3	6.0	6.8	7.7	8.9
Vietnam	10.9	11.9	14.9	14.6	13.9
Yunnan, PRC2	1.7	1.7	2.1	2.1	1.9

Source: Regional Cooperation Strategy and Program 2004-2008: The GMS- Beyond Borders, ADB, 2004

As can be seen from Table 2, the share of comparatively developed countries like China and Thailand is minuscule compared to countries like Cambodia and Lao PDR.

Trade Capacity Building

Trade capacity building is a form of development assistance provided by donors to help developing countries participate in and benefit from global trade. Trade capacity building can be broadly defined as development assistance aimed at helping countries build the physical, human, and institutional capacity to participate in global trade. It includes assistance to negotiate, implement, and benefit from trade agreements, such as agreements within the World Trade Organisation (WTO), and regional and bilateral free trade agreements (FTAs). It is also referred to as aid for trade (AfT) or trade-related technical assistance (TRTA), especially within the context of the WTO.

Multilateral institutions like the ADB and United Nations Economic and Social Commission for Asia and the Pacific (UNESCAP) have played a very active role in building the trade capacity of the GMS countries. The ADB through the GMS programme, initiated in 1992, has supported regional cooperation for strengthening cross-border physical connectivity. Key activities of the GMS include development of economic corridors, focussing on road investments to improve access, institutional and policy changes for trade facilitation and transit policy harmonisation to reduce logistics cost across the sub-region.

Individual countries have also initiated trade capacity building measures and policies to facilitate cross border trade. For instance, there has also been a major reorientation in the routes used for the transit cargo. Before the introduction of the New Economic Mechanism in Lao PDR, international trade was generally conducted through Vietnam. Now it has been estimated that around 95 percent of Lao's transit trade moves through the ports in Thailand designated to handle this traffic, while the remainder moves through the ports in Vietnam. Cambodia on its part has initiated an Integrated Framework (IF) programme to embed trade-related development into the overall development agenda of the country.

ADB also introduced the concept of economic corridors to promote physical linkages in this region and at present, there are three economic corridors at different stages of development.

Production, trade, tourism and other economic activities provide a range of benefits from better access to raw materials to attract FDI. The East-West Economic Corridor under the GMS programme, links the South China Sea to the Bay of Bengal, that is, from Vietnam's Danang Port in the East to Myanmar's Mawlamyine in the West. The Mawlamyine-Danang land route is only 1,000km whereas the sea route that passes through the Malacca Straits is 4,000km. The North-South Corridor links Kunming (Yunnan, China) and Chiang Rai (Thailand) through north-western Lao PDR and the the Southern Economic Corridor connects the three big cities: Ho Chi Minh, Phnom Penh and Bangkok. Besides these economic corridors, the GMS countries have also implemented the GMS CBTA.

Box 1: GMS Cross Border Transport Agreement (CBTA)

- Negotiation of all annexes and protocols has been finalised and signed on March 20, 2007 in China.
- Waiting for ratification from GMS countries. Full implementation of CBTA has been scheduled in 2008.
- The agreement involves single window clearance, single-stop inspection and one-stop service.
- Multilateral agreement that covers all aspect of cross border movement of goods, people and vehicles.

Countries in the region have increasingly come to attach more importance to trade liberalisation. For instance, in Lao PDR in 1987, the Government started an overall reform of the trading system, allowing private sector participation, rationalising the web of state trading companies, and eventually dismantling its monopoly of foreign trade in a large number of commodities.

By 1992, timber exports alone were subject to quantitative restrictions and only imports of rice and motor vehicles were subject to licensing. In recent years, most quotas have been eliminated and the tariff structure has been rationalised. Since the early 1990s, Government policies have opened the national economy to market signals, including foreign trade, with the expectation that an export boom would improve the terms of Laos's progressive integration into the world economy. The initial opening of the economy brought about a dramatic increase in exports, which grew (in nominal terms) at 22 percent yearly between 1990 and 1996 and doubled as share of GDP, reaching 18 percent.

However, since the Asian crisis, export growth in GMS has remarkably slowed (2.3 percent yearly up to 2002), while imports have not been curbed accordingly, perpetuating large trade deficits. Overall, Laos remains relatively closed to trade. Trade (export plus import) in goods stood at 56 percent of GDP over 1998-2002, which is low when compared with neighbouring Cambodia (80 percent) and Vietnam (87 percent).

Role of the Private Sector

The private sector plays an increasingly important role in the development of an economy. However, in transitional economies, their participation is constrained by a number of issues such as inadequate infrastructure, half-baked information and, therefore, lacks the capacity to cope with the challenges of market-based economic forces.

Given the general scarcity of physical infrastructure, capital, and technical and institutional capacity in most GMS countries, host governments themselves woo private investors under the ADB's watchful eye. In fact, privatisation is the watermark of GMS projects. The role of host government is to "create an enabling environment" to attract private sector investors, both domestic and foreign.

The business firms can pursue joint ventures (foreign and domestic public and private companies partner with each other), public-private partnerships (public sector companies partner with private investors, foreign or domestic) on Build-Own-Operate (BOO), Build-Own-Operate-Transfer (BOOT), Build-Operate-Sell (BOS) and Build-Operate-Transfer (BOT) basis. In all of these, whether or not the government contributes to direct financing, it nonetheless plays an extremely important role by making the terms of investment attractive to the investors. These terms include tax holidays, exemption from customs duties, full repatriation of revenues and profits and purchase agreements (such as power purchase agreements in the case of energy projects).

Small and medium-sized enterprises (SMEs) comprise the bulk of private production units in the GMS. Enhancing private sector competitiveness in the GMS must thus necessarily focus on SMEs. Enabling these enterprises to realise their economic potential is expected to increase business activity, investment and trade, and generate employment, which, in turn, will result in increased incomes and consumption and ultimately, sustained growth. In addition to infrastructure and an enabling policy environment, SME development requires more direct forms of support such as: (i) business development services including business planning, networking, and matching with other business opportunities; (ii) short-and long-term financing; and (iii) support in creating and strengthening of producers and trade associations.

The GMS countries have chosen to focus on trade facilitation to establish an attractive environment. Clearly private sector led, export oriented trade and investment is the economic model that governments in this region have adopted.

SMEs are flourishing in Vietnam following the implementation of preferential policies, according to a Government report. Since 1986, a number of SME-related laws have been passed, including the Enterprise Law and the Law on Encouragement of Domestic Investment.

As a result of the various policies, the number of SMEs has increased to 190,000 in 2005. Regulations have also helped create a legal foundation for the development of a SME support network. So far, almost two-thirds of provinces and cities across the nation have launched programmes assisting SMEs with technology, personnel training and trade promotion.

Along with a boom in their numbers, SMEs have improved the efficiency of their operations. These achievements have allowed SMEs to contribute about 45 percent of the GDP and more than 27 percent of the nation's total development investment. SMEs also provide jobs for about 25 percent of the nation's workforce.

The first major focus on private sector development in the GMS started with the ADB supported GMS Economic Cooperation Programme. The third ministerial meeting for GMS sub-regional cooperation in Hanoi, in April 1994, called for the creation of a "sub-regional Growth Zone through constructive Business Facilitation"[5] explicitly recognising the importance of the business community. Initiated in 1992, the GMS Economic Cooperation Programme is an ambitious master plan to create a frontier of rapid economic growth through regional economic cooperation. Majority of the capital investment through the programme has been in the areas of transportation, infrastructure, power/electricity and trade and investment facilitation.

The first manifestation of this commitment to opening borders was the promulgation of the "Agreement on Commercial Navigation on the Lancing-Mekong River", which was signed in April 2000 by the governments of China, the Lao People's Democratic Republic, Myanmar, and Thailand. The Agreement, which came into effect in June 2001, was designed to promote trade and tourism, strengthen cooperation in

Box 2: The Role of Private Sector in Vietnam

Vietnam is one of the fastest growing economies in Asia recording an average annual growth in GDP of about 7.5 percent over the last decade. Growth of 8.1 percent in 2005 was fuelled by a robust increase in domestic demand and strong export performance. The Government of Vietnam is increasingly recognising the pivotal role that the private sector has played in economic development and job creation. Primary estimates indicate that the private sector generated almost 90 percent of the 7.5 million jobs created during the five years to 2005 of which 64 percent were generated by small enterprises.

Most of the 1.6 million new jobs in Vietnam likely to be created annually in 2006-2010 are expected to be generated by the private sector.

Source: Country Strategy and Program 2007-2010, Asian Development Bank.

Table 3: Doing Business in select GMS Countries						
Country	Indicators					
	Number of Documents for export	Time for Export	Cost to export (US$ per container)	Number of Documents for Import	Time for Import (days)	Cost to Import (US$ per container)
	2007	2007	2007	2007	2007	2007
Vietnam	6	35	701	9	36	885
Cambodia	8	36	736	12	45	816
Lao PDR	12	66	1420	16	78	1690
Thailand	9	24	848	12	22	1042
China	6	18	335	12	22	375
Singapore	5	6	382	6	3	333

Source: Doing Business, World Bank, www.worldbank.org

commercial navigation, and to help attract greater investment along the upper portion of the river.

A number of initiatives have been undertaken at the regional level to facilitate trade. For one, there is the Mekong Private Sector Development Facility (MPDF). The MPDF promotes small and medium enterprise development at the macro, meso and micro levels of the economy, and achieves economies of scale by implementing programmes across Vietnam, Cambodia and Lao PDR. Activities are tailor made to suit local challenges and opportunities, and to respond to changing economic conditions.

Similarly, there is the GMS Strategic Framework for Action on Trade Facilitation and Investment (SFA-TFI). The priority areas of this Agreement are trade logistics development, business mobility improvement among others. This agreement re-enforces the revised Kyoto Convention, ASEAN Transit agreement and the WTO agreements.

Table 3 shows select indicators for doing business in these countries and how they fare against Singapore, which is a forerunner in trade openness.

Challenges and Opportunities

- It is important to keep in perspective that since most of the countries in this economic bloc are LDCs, it is essential to find a balance between profit making and livelihood. It is very important to identify the ultimate beneficiaries otherwise there will be discontent.

- GMS must address the problem of inadequate public and private sector interface. There should be more effective platforms for various sectors to meet and discuss. There are restrictions on the formation and functioning of business associations in many of these economies. While the GMS Business Forum does provide a platform, it has been ineffective in bringing about any change.

- Perhaps the most critical question regarding free trade and investment in the Mekong region is how it will affect local economies, employment, livelihood, environment, food security and access to essential services for the majority of the people. They should not end up at sweatshops of the foreign firms.

- Development of SMEs requires more direct forms of support such as advisory services for business planning, networking and matching with other business opportunities, short and long term financing which is lacking in GMS.

- Political instability can be a major roadblock to attracting foreign investment and promoting local industry. For instance, the situation in southern Thailand heightens the risks involved and might deter firms from coming in.

Nevertheless, there are opportunities that these countries can explore, for instance:

- Developing the inland water transport – the Mekong River flows 1,865 kilometers and is an important means of transport particularly for mountainous areas inaccessible by road.

- Identifying sectors that can be developed more easily as compared to others. For instance, textile and garment sector in Vietnam and Gold in Myanmar. Myanmar's first opening of its state-operated largest gold mine to the private sector signifies a breakthrough in the country's privatisation programme for its state-owned economic enterprises and the liberalisation would further contribute to the development of the mining sector. The development of SMEs is also very important. SMEs attract labour from agriculture to work in the service and industrial sectors, and from the state sector to the non-state sector. At the same time, the development of SMEs also helps to adjust and diversify the structure of the industrial sector and reduce the need for imports.

Conclusion

There is no denying that institutional changes and additions have been brought about to facilitate trade and promote the role of the private sector in GMS countries. However, there are vast disparities in the economies. While Vietnam has got its bearing, countries like Cambodia need to get their act together. For these economies, competitiveness entails creating and maintaining a business climate conducive to private sector enterprise. With the economic corridors in place, there is an opportunity to exploit the un-tapped potential that these countries have. Their growth will also depend on how the more developed economies like Thailand perform. For instance, Thailand was a major market for hydroelectricity from Lao but in 1998, Lao was hit adversely because of the financial crisis that hit Thailand's economy.

China's interaction with these countries has also been on a rise and trade between China and the other five countries reached about US$32bn in 2005. This would positively affect these economies. Political stability is also essential as foreign investors are still watchful of its uncertainty.

As table 2 shows, that within the GMS, Yunnan province of China and Thailand had the smallest shares of intra-regional trade with other GMS countries, i.e., only around two and nine percent of their total trade in 2002, respectively. These findings have a very important policy implication that for a trade-led growth and development in Cambodia, Laos, Myanmar and Vietnam (CLMV) countries of the GMS to be successful, China and Thailand have to take a more proactive role in expanding more preferential trade deals with these countries.

Particularly, China and Thailand should focus on imports, rather than exports, especially for agricultural and labour-intensive products of rural and the highlands and SMEs along the remote and border areas of CLMV. Thailand and China themselves also need to increase their intraregional trade to a greater extent.

The GMS region has a long way to go as far as building its trade capacity is concerned but it has definitely made a move in the right direction and with dynamic economies like Vietnam setting an example, the region looks poised to find its place under the sun.

Endnotes

1 www.adb.org/Documents/Reports/TMR-foreign-direct-investment/chap-2.pdf (accessed in June 2007).
2 *Ibid.*
3 It bears the names of the three major rivers running through the five countries. Originally, this sub-regional cooperation framework was called the Economic Cooperation Strategy or ECS. The objectives of this initiative are to bridge the economic gap among the four countries and to promote prosperity in the sub region in a sustainable manner.
4 Roundup: Cambodia, Vietnam highlight trade, economic cooperation, People's Daily Online (accessed in March 2007).
5 www.adb.org/Documents/Speeches/2003/ms2003072.asp.

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