Economic Cooperation and Integration in Greater Mekong Sub-region (GMS): Some Perspectives

Madan K. Dahal

Introduction to GMS

Background

The GMS economies comprise five countries and one province: Cambodia, Lao People's Democratic Republic (Lao PDR), Myanmar, Thailand, Viet Nam, and Yunnan Province of the People's Republic of China (PRC)—all of whom share the Mekong River, the world's twelfth longest river at 4,200 kilometers. The origins of GMS can be traced to the 1957 establishment of the Mekong Committee, which then comprised the four riparian countries of the lower Mekong Basin. But the region was racked by conflict, so there was little progress over the following three decades. The process gained substance only in 1992, when ADB initiated a formal program of cooperation among the six current GMS members. But the GMS has also benefited greatly over the years from additional contributions and involvement by the United Nations Economic and Social Commission for Asia and the Pacific (ESCAP).

GMS's combined land area is 2.34 million square kilometers. Its population was 257.5 million in 2003, with a population density of about 115 people/km^2. The GMS economies are predominantly based on subsistence agriculture, but they are gradually diversifying into several modern economic sectors and rooted in a more transparent, market-based system. GMS is a vast area of enormous wealth and variety of natural resources, including a rich agricultural base—timber and fisheries-minerals, and energy in the form of hydropower and coal and petroleum reserves. These resources fuel economic development and support rural livelihoods in an interrelated fashion. Water from the Mekong River supports agriculture, and its fish yields are a source of both protein and income. It can also be used to generate electricity and as transport corridors.

Five of the six GMS economies are still undergoing a transition to a market—based economy and opening their sectors to foreign participation. With the exception of Thailand, which has had a free market economy for decades, the GMS economies were previously centrally planned and characterized by state―owned means of production. Low levels of productivity, inadequate amounts of goods, and severe economic problems compelled the Governments in five of the GMS countries to reduce the state's productive role in the economy and allow the business sector to take a greater role in developing the countries both economically and socially. The structural reform process is not complete, but the private sector now functions openly and in most cases has surpassed the state―owned portion of the economy.

The GMS members share other similarities as well. Although Thailand is more developed economically, all of them have extensive needs in hard and soft infrastructure, education, private sector development (particularly small to medium size enterprises), technology, human resource development, a heavy reliance on subsistence agriculture, and other issues. Many of these matters, such as telecommunications, transportation networks, and energy, are more effectively conducted in a regional setting compared to each country developing on its own.

Among the key objectives for the GMS, as identified by the Asian Development Bank, are:

- Facilitating sub―regional trade and investment;
- Facilitating sub―regional development opportunities, particularly for energy, tourism, and other projects;
- Facilitating the resolution of trans-border issues, such as disease and environmental degradation ; and
- Fulfilling common resource or other needs.

The great majority of GMS people live in rural areas where they lead subsistence or semi-subsistence agricultural lifestyles. More than 75 percent of the population of Lao PDR, for example, is rural and even in Thailand, the most urbanized of the Mekong countries, there remain large agricultural communities, particularly in the north and northeastern parts of the country. While traditional lifestyles and deep―rooted customs and beliefs have been scarcely altered by time, the area is now undergoing greater change than ever before. With the onset of peace in the 1990s, the peoples of the Mekong are experiencing rapid changes and improvements in their living standards and conditions.

The rich human and natural resource endowments of the Mekong region have made it a new frontier of Asian economic growth. Indeed, the Mekong region has the potential to be one of the world's fastest growing areas. Yet, still much of its remains poor. The gross domestic product per capita is about $1 a day in most of the region. Despite significant economic growth, poverty is still widespread.

Economic Performance

The GMS is one of the world's fastest—growing sub—regions. With the exception of Thailand, which was directly affected by the Asian financial crisis, growth has remained about 4% or higher in all of the economies for the past decade. GDP growth in all six economies was robust in 2003, ranging from 5.0% in Cambodia to 7.1% in Viet Nam. The GNP-weighted average growth for GMS in 2002 was higher than 6%, significantly higher than the average of 4.8% recorded in 2001.

All economies except Cambodia are expected to have grown by about 6% or higher in 2004, with Viet Nam again topping the list at 7.5%. Cambodia's growth is likely to be about 5.4%, because of security concerns in early 2003 and ongoing political uncertainties. Various domestic and external factors have played a role in continuing this growth trend in 2004. Factors contributing to growth have been strong consumer spending, improved agricultural output induced by favorable weather, increased exports, and fiscal stimulus packages in many economies. Except for Myanmar and Lao PDR, consumer price inflation remained low and manageable in the GMS economies during 2003. The low inflation resulted from a variety of factors including improved food supply, relatively stable exchange rates, and slow growth in money supply. Although inflation remains endemic in Myanmar (24%), Lao PDR (15.5%) subdued some of its inflationary pressures late in 2003 by introducing a range of restrictionary fiscal measures.

All GMS economies except Thailand continued to have fiscal deficits during 2003, partly reflecting higher expenditures aimed at stimulating the economy. Thailand posted its first surplus since the Asian financial crisis began. Difficulties in raising government revenues largely account for ever—increasing budget deficits in Lao PDR, Cambodia, and Myanmar. Difficulties with revenue collection continue to pose a threat to macroeconomic stability in Lao PDR and Myanmar; in Cambodia, the impact of revenue collection problems is mainly felt through the constraint it places on the Government's capacity to implement social and other expenditure programs. In the external sector, exports surged in all economies in 2003 except for Myanmar. The increase has been particularly impressive in Thailand, Viet Nam, and Yunnan Province of PRC, due largely to improved external demand and, for Viet Nam, to high crude oil prices.

All economies except Thailand continue to run current account deficits, although none of the deficits appear non sustainable. Net foreign direct investments（FDI）in Thailand, Lao PDR, and Viet Nam increased sharply in 2003, after having slowed in almost all GMS economies in 2003.

Economic Challenges within GMS

Since all GMS countries are in transition from centrally planned to market economies, there are common problems that Cambodia, Lao PDR, Myanmar, and Viet Nam（CLMN Countries）face. Each is, however, at a different stage in this transition, and other country—specific factors suggest that there are also differences in the types of challenges that each must address. At the other end of the spectrum lies Thailand, a market economy that is still grapping with many of the challenges of a developing Asian country.

In Cambodia, the effects of the destruction of social, economic and political institutions during the Khmer Rouge period are still evident, but progress has been made, and the focus is shifting from rehabilitation to economic advancement through growth and development. Lao PDR is the least developed of the GMS countries. It is land—locked, sparsely populated, and has a mountainous terrain. It has a very narrow resource base that limits its capacity to diversify production and exports. Institutions remain weak, and human resources are underdeveloped. The pace of economic reform has been slow, so its transition to a full fledged market economy remains a long—term challenge.

Myanmar's economic constraints range from a highly managed foreign exchange regime to a plethora of controls on production and export in its most important sector; agriculture. Myanmar has limited excess to assistance from international donors because of its political situation. Yunnan Province, RPC, and Viet Nam are the more economically advanced of the GMS transitional economies. Viet Nam has been making steady progress toward a market economy, but it needs to accelerate the pace of reforms including those relating to governance.

Thailand has the most developed and largest market and is important source of knowledge and capital. It is also a communication and transportation hub and is the vantage point from which many potential foreign investors view the GMS. Despite recent impressive growth, reducing poverty remains a significant challenge, particularly near the northeastern border with the Lao PDR and in the border region with Cambodia and Myanmar. There is also a need to continue reforms to consolidate growth. Completing Thailand' s banking and corporate restructuring is vital for the recovery of business investment and the medium—term prospects for the GMS economies.

General Attractions and Advantages of the GMS

Like other developing regions, the GMS has its fair share of obstacles to overcome. Yet at the same time, it offers exciting opportunities for business activities. One of the GMS's greatest assets is its strategic location. Lying at the crossroads of the world's two most populous countries, China and India, the GMS provides a strategic foothold for accessing those two markets. Even the domestic market of the GMS is substantial, with approximately 250 million people who are gradually becoming more interconnected and increasing their purchasing power. Furthermore, the GMS, via Thailand, aspires to be South-East Asia's regional transportation and services hub, along with one of Asia's primary energy producers because of the hydropower potential in the Lao People's Democratic Republic, Myanmar, Yunnan, and to a lesser extent, Cambodia.

The GMS is also well—endowed with vast tracts of fertile land. For instance, in Myanmar 9 million hectares are currently under cultivation, representing only 13 per cent of the total land area of the country. The Ministry of Agriculture and Irrigation estimates that another 9 million acres can be sown in fallow and cultivatable unused land. With the agricultural base already established, the GMS is a perfect opportunity for many agro—based industries such as food production, processing, and packaging.

The rich natural resources found in the GMS are also enticing investment opportunities. A wide variety of resources such as timber, minerals, gems, coal, oil, natural gas, and metals abound in the sub—region and, in many cases, are only beginning to be exploited. In Cambodia, the north—east area contains a wide variety of minerals, coal, and other valuable resources, but almost no extractive activities are being undertaken. In fact, the exploration phase is still only in the preliminary stages, yet dozens of mines and deposits have already been discovered.

Likewise, the energy sector is operating at a small fraction of its total capacity—a little more than two per cent of the full potential. Several sites have been identified for hydropower projects in the Lao People's Democratic Republic, Myanmar, and Yunnan, but only a few are in the construction process or already on—line. An inventory of hydropower in the GMS estimates that the sub—region has the potential for 1,090 TWh per annum, while the energy demand in the GMS by the year 2020 is expected to reach only 600 TWh per year, leaving a substantial amount available for exporting out of the region.

Some of the GMS countries are considered among the least developed in the world and therefore receive special trade preferences from several industrialized countries. Cambodia and the Lao People's Democratic Republic, for instance, received Generalized System of Preferences (GSP) status on selected goods. Although these favorable terms will eventually be phased out under World Trade Organization (WTO) rules and replaced with a collective system of concessions yet to be determined, they are expected to remain in place for several years to come.

The skill level of the GMS labor force is typically seen as a drawback for the region in attracting attention from foreign investors. Although the overall level of education and skill is below other parts of Asia, the GMS offers a large, low cost, and ambitious labor force. Viet Nam, for instance, is reputed to have one of the most disciplined and hard working populations in Asia and, along with the other GMS members, its workforce is eager for training and is highly adaptable. Thailand's large labor pool provides an excellent combination of intermediate and advanced skills with competitive wages.

1. Logic of Economic Cooperation in GMS

The fundamental rational for regional cooperation, in whatever form, rests on recognition by a group of countries of shared opportunities and or constraints that provide the basis for joint action. Regional cooperation is ultimately a function of enlighten self interest of the participants. It is enlightened, because it brings from a joint recognition of shared interests among the participating countries, and an appreciation of limits on a given country's abilities to act unilaterally in the pursuit of these interests. It involves self interest, because to be sustainable, the consequences of cooperation must be seen as ultimately serving the domestic or national interest of the participating countries. Regional cooperation therefore is likely to be successful to the extent that the participating countries see a clear need for cooperation; tangible net benefits from such cooperation in terms of both improved development outcomes and broader national interest; and see the risks to national sovereignty arising from such cooperation as manageable.

Although the GMS region is characterized more by diversity than by similarity, important and growing interrelationships within the region link the economic prospects of individual economies. To some extent, the differences themselves contribute to the growing linkages. Many traditional factors that motivate economic cooperation are found within GMS. Complementarities in resources and income levels suggest important opportunities for intraregional trade and investment. The trading relationship between Thailand and Lao PDR is an illustrative example of these drivers at work. Differences in factor endowments and levels of economic development explain much of the trade pattern between the countries. Thailand is Lao PDR's most important trading partner. Thailand provides a significant portion of Lao PDR's demands for manufactured good, and buys a significant share of Lao PDR's resource—based exports such as hydropower and timber.

Economic cooperation can lower transactions costs and align resources with comparative advantage more closely by reducing structural and institutional impediments to movements of goods, people, and capital. Also, GMS partners can exploit economies of scale by acting together, increasing efficiency in some sectors and making activities possible that might not be otherwise. The economic cooperation in the GMS promotes social and economic development in the six participating countries by strengthening economic links among them. Through the joint development of public goods, (e.g., transportation, energy resources, telecommunications) sub—regional cooperation can help overcome domestic constraints in individual economies resulting from limited resources and markets. Joint investments in infrastructure and accompanying policies that permit the more efficient flow of goods, services, and people, can promote access of individual countries to key inputs, including capital and human resources, as well as expand their markets. The resulting increase in trade and investment flows will contribute to the participating countries' ability to integrate faster with the regional and global economy.

The steady progress in the transition toward more market—oriented regimes was an important factor contributing to the viability of economic cooperation in the GMS. While centrally—planned regimes resulted in limited commerce among the GMS countries, economic reforms that began in the 1990s helped create conducive environment for increased trade and investment and other forms of economic cooperation. Economies of scale and specialization resulting from sub—regional cooperation facilitate investments to the GMS countries as a group beyond their individual abilities to attract investments. By generating economic synergy and dynamism, sub — regional cooperation can contribute to the goal of sustained economic growth of individual countries that can also help improve the living conditions of the poor and improve the quality of life of the people.

Changes in the environment and unequal opportunities resulting from economic growth and interaction can also affect mobile populations, communities located near infrastructure projects, and ethnic minorities living in border areas. A common framework and set of priorities are thus essential to effectively address the special needs of these groups and to provide them with better opportunities. Sub—regional cooperation also provides the GMS countries with an unique opportunity to address environmental issues of a trans—boundary nature and the management and equitable use of common resources, such as watersheds, reservoirs and wetlands.

In short, a few factors seem to have played a key role in motivating regional cooperation in GMS, some of which are as follows:

1. Capacity building for development through cross—border infrastructure development.
2. Exploitation of complementarities and untapped human and natural resources.
3. Overcoming shared problems through watershed management; GMS countries

share a common watershed. They have realized potential threat of environmental degradation.
4. Attracting FDI through widening and diversifying member countries' production base.
5. Building sense of security among member countries.
6. Stepping stones to multilateral liberalism through strengthening competitive position.
7. Managing trade frictions.
8. Achieving economic clout.

Individual countries are motivated by different factors; Thailand seeks to be the economic hub of the Mekong sub—region. Its relative advantages are in marketing, finance, technology and tourism. Thailand is looking to neighboring countries to overcome its domestic shortages of fuel oil for electricity, natural gas/oil, hydro electricity and iron ore, copper, lead and other minerals. Thailand hopes to export its labor intensive equipment and industries as its comparative advantage in labor cost is eroded.

China, particularly Yunnan province, recognizes the potential to expand exports of simple consumer products, machinery and equipment, and resources such as iron ore, marble, coal and phosphate to markets in Myanmar, Laos, Thailand, Cambodia and Vietnam. Exports to third countries through ports in Thailand, Myanmar and Vietnam would reduce high transport and taxation costs. Yunnan is eager to attract investment and technology from Thailand that would allow China to develop depressed areas in its interior and thereby reduce national economic income disparities.

Myanmar broadly supports the concept of accelerated economic links if they will help to revitalize the economy and facilitate national development. Laos supports sub—regional economic cooperation if it reinforces the transition to a market oriented economy and attracts foreign trade and investment. Laos seeks to develop transportation, tourism, energy and mineral resources. Cooperation would also give land—locked Laos better port access. Cambodia is generally supportive of sub—regional economic cooperation if it provides a mechanism to rehabilitate its war damaged economy. Vietnam recognizes the potential of sub—regional economic cooperation to facilitate economic development. It seeks investment funds to develop its human resources, transport and communications infrastructure, and energy sectors, and manufacturing industry.

The willingness to open up their economies paved the way for sub—regional economic cooperation, but equally important was the reduction in political and security tensions that plagued peninsular South-East 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 eventual GMS members recognized that their future well—being depended on economic and social cooperation.

2. Initiatives for Economic Cooperation and Integration

Economic cooperation and integration in GMS are taking place at three levels; sub—regional, regional and multilateral. How we define each of these geographic groupings determines our definition of the types of initiatives in economic cooperation and integration. We define the sub—region to consist of the grouping of economies that are GMS members. The region is defined to include all 10 countries that are currently members of the Association of Southeast Asian Nations (ASEAN). Multilateralism or globalization is defined as a residual, and refers to countries outside the sub—region and region.

Early Attempts

The early focus of the GMS centered on seven priority sectors; transport, telecommunications, energy, environment and natural resources management, human resource development, trade and investment, and tourism. A set of project profiles was developed for each of these sectors, and in some cases as many as 34 projects were identified for one sector. A brief summary of the sectors is as follows:

Transport: The framework for transport intends to create a sub—regional transport sector that would facilitate trade. The plans included road, railway, water, and air transportation projects, but road projects were given the highest priority, especially the Bangkok—Phnom Penh—Ho Chi Minh—Vung Tau road and the East—West Corridor running from Viet Nam to the Thai-Myanmar border.

Telecommunications: Several of the GMS members did not have direct telecommunication links between them, and so these connections became a priority objective. Plans were also made to upgrade existing infrastructure to fiber optic lines, digitize the national networks, expand facilities, create common standards and technology, and adjust regulations, policies, and tariffs.

Energy: The energy projects sought to mobilize the GMS's vast potential in hydropower, coal, and hydrocarbon energy. With such an abundance of resources, it was assumed that energy costs would be low for the members once they harnessed this potential. Projects identified included power generation and transmission, natural gas transmission, institution building, and environmental collaboration. A major goal was to shift energy program from isolated, single country projects to cross—border cooperation and complementarities, in particular exporting energy to other members of the GMS.

Environment and natural resources management: The Mekong River basin contains numerous watersheds dispersed across boundaries, and this interconnectedness requires cooperation in watershed management, forest management, pollution control, and maintaining bio—diversity. The 11 projects initially identified for this sector revolve around institution building, management of waste and hazardous substances, and management of natural resources.

Human resource development: The GMS has a large workforce, over half of the total population of 250 million, but it is underutilized due to unemployment, underemployment, and a shortage of appropriate skills for modern economic activities. The majority of the 11 initial projects identified in this sector focused on education, skills training, and training the trainers, but other projects dealt with health issues such as HIV/AIDS prevention and malaria control.

Trade and investment: The GMS members face common problems related to trade and investment. Among these problems are structural adjustment issues arising from the transition to a market economy, underdeveloped legal and regulatory frameworks, limited financial markets, and an inexperienced private sector. The GMS members decided to embark on a series of projects to facilitate trade and investment within the sub—region and outside it as well. The eight original project profiles in this sector fell into four categories; facilitating and enhancing trade flows, improving investment climates, building a strong science and technology base, and increasing the role of the private sector in economic development.

Tourism: The GMS governments endorsed six priority projects related to sub—regional tourism promotion, long—term planning, capacity building, and linkages and networking. Despite identifying the seven sets of projects, several problems arose in the mid—1990s that slowed the pace of economic cooperation. First, with such a wide variety of projects identified, along with each country's own national planning, duplication of projects and activities occurred because of insufficient coordination. Second, bureaucratic inertia held back many of the projects, and this was compounded by what appears to have been overly ambitious expectations for implementing projects. In most instances, the relevant agencies and ministries in the Governments of the Sub—region had a severe shortage of personnel with the requisite skills to implement many of the technical projects. Moreover, bureaucrats and government officials were not always committed to fostering sub—regional cooperation. A third set of problems related to political controversies in some of the member countries. Instability in the Government of Cambodia and the ongoing civil war clearly hindered the country's full participation in the GMS framework. The boycott levied by several Western States against Myanmar inhibited multilateral lending and investment, again making it difficult to fully realize many of the projects envisaged for the GMS. Fourth, and perhaps the most devastating problem, was the advent of the East Asian economic crisis that erupted in mid—1997 in Thailand. The fallout from the crisis brought sub—regional economic cooperation to a standstill, as countries all across East Asia concentrated on restoring domestic financial and economic stability.

GMS Beyond 2000

The GMS Summit of Leaders, in November 2002 in Phnom Penh, endorsed the 11 multi—sector, large—scale GMS flagship programs that represent major advances in sub—regional economic cooperation among the six Mekong countries. The flagship programs include transportation/economic corridors, telecommunications and energy interchanges, cross—border trade and investment, support for greater private sector participation in development, development of human resources, joint initiatives for the management of the sub—region's shared environment and natural resources, and the promotion of the GMS as a single tourism destination. The flagship programs, which envision an integrated, prosperous, and equitable Mekong sub—region, are designed to support the GMS Strategic Framework for the next 10 years (2003-2012).

The flagship programs aim to closely link the six Mekong countries and facilitate sustainable cross—border trade and investment. To implement the 11 flagship programs, a long—term development matrix has been prepared by the Asian Development Bank in close consultation with the GMS countries. The matrix provides a synopsis for each of the flagship programs, including their respective components, description, status and scope, estimated costs and possible financing sources, implementing agencies, completion schedules, and issues and constraints. The matrix is a "work in progress" and subject to suggestions and proposals for additional projects and financing.

GMS projects and initiatives under the flagship program for regional power interconnection and trading arrangements focus on the optimal utilization and development of the region's energy potential and provision of cross—border power and natural gas.power transmission links to allow efficient electricity trade. Significantly, the GMS Inter—Governmental Agreement on Power Trade, signed in November 2002, paved the way for the development of a power trade operating agreement. Support initiatives include the establishment of institutional mechanisms within the sub—region to support the momentum toward increased cooperation in the field of electric section.

The flagship program for telecommunications backbone and information and communications technology is designed to establish the basic infrastructure needed to interconnect the national networks of the six GMS countries. A total of 13 transmission links originally grouped into three loops (East, West, and North) and improved interconnection have been identified for priority implementation. These 13 priority networks have been regrouped into a two—phased project, namely, the Telecommunications Backbone Project—Phases 1 and 2. In addition to investment in backbone facilities, the program includes important policy reforms and much—needed capacity building initiatives expected to pave the way for private sector participation.

The flagship program on facilitating cross—border trade and investment involves important subcomponents, including improving the data system for trade and investment, establishing single—stop customs inspection stations and products and services in support of small—and medium—sized enterprises (SMEs), and reducing barriers to trade in agricultural products. The program also relates closely to the other flagship programs, such as transportation, telecommunications and energy cooperation initiatives, and the Framework Agreement for the Facilitation of the Cross-Border Transport of Goods and People. All six GMS Governments have signed this landmark agreement, and are negotiating and finalizing — by 2005— the annexes and protocols which will provide the implementing guidelines for the cross-border pact. To provide further impetus to reducing non—tariff barriers, GMS countries will soon pilot—test, single—stop customs facilitation arrangements at selected border crossings. Joint control by juxtaposed countries' customs authorities through shared facilities or mutual recognition of harmonized customs inspection procedures will help reduce transportation costs associated with delays at border controls.

Since the onset of the GMS Program, it has been recognized that cooperative action is critical to resolve environmental problems that transcend national boundaries. Environmental cooperation under the GMS Program increasingly concerns broader trans—border issues, such as the cumulative effects of development in the sub—region. The strategic environment framework flagship program has been developed to guide investment decisions in critical sectors and areas, and mitigate potential adverse effects of economic development. It combines analytical, participatory, and policy-oriented processes that together constitute a strategic platform for guiding investment decisions in the GMS. The first phase developed a strategic platform to guide infrastructure investment decisions in the GMS, consistent with the demands of environmental and social sustainability. The second phase facilitates decision making, first by creating a data warehouse which will structure and organize relevant data and information at the national and sub—regional levels to make them readily accessible to the decision maker; second, by providing performance assessment methodologies; and third, by establishing a framework and platform through which knowledge will constantly be added to the existing database.

This flagship program for flood control and water resource management complements the initiatives of the Mekong River Commission (MRC) and includes four major groups of floodplain management measures: (i) land use planning-to minimize risks to people living in vulnerable floodplain areas; (ii) structural measures — such as building platforms for dwellings and making roads flood—proof to minimize hazards to people living in floodplains, and construction of flood mitigation structures such as detention basins and embankments to reduce flood damage to urban settlements; and (iii) flood preparedness—to strengthen institutional capacities to prepare for floods, and build capacity for responding to flood emergencies.

The flagship program for developing human resources and skills competencies provides a framework for wide—ranging cooperation, to jointly address regional challenges affecting the human resource development. Initiatives under this flagship program include support systems for harmonizing training standards and skills certification systems, a system for accrediting training institutions and capacity building of vocational training institutions, mitigation of the trans—border spread of communicable diseases, improvement of health and education services for ethnic minorities in border areas, and short—term training for enhancing capacity of GMS officials in development management.

In tourism, partnerships between public and private sectors in the GMS have helped establish, through joint marketing, the GMS as a single tourist destination that offers a rich array of cultural, historical and natural resources. As a result, the GMS is one of the fastest growing tourist destinations in the world, attracting over 16 development flagship program will support key infrastructure critical to promoting the sub—region as a "single destination site." "Soft infrastructure" will also be improved, including inter—country visa recognition and greater mobility for tour operators and guides. GMS cooperation in tourism has embarked on facilitating the movement of tourists to and within the sub—region through, among other things, the establishment of a GMS visa, which is envisaged to work like the Schengen visa in Europe. Special effort will be directed at extending tourism to poor and remote areas, including through the development of eco—tourism. The quality of tourism services will be improved through training and other measures. The private sector will be encouraged to take charge of tourism development within a well—defined social and environmental regulatory framework.

GMS countries recognize the important role of the private sector as an engine of economic growth in the sub—region. In this regard, the flagship programs are collectively relevant because they are based fundamentally on providing a supportive framework for private enterprise. The flagship program for enhancing private sector participation and competitiveness addresses specific factors. A particular concern is the managerial, marketing, and other skills of SMEs and accessibility of financial services. To help SMEs and other commercial interests find a voice for their needs and views, the GMS Business Forum is being strengthened and its activities expanded.

Initiated in early 2003, GMS cooperation in the agriculture is geared toward achieving its mission statement as follows: "Help reduce poverty through partnerships with rural communities to promote agriculture trade, food security, and sustainable livelihoods." Fourteen project concepts have so far been prioritized in the areas of livestock, health, sanitary and phyto―sanitary standards, gender―targeted extension services, information technology for agriculture, post―harvest management, fish industry statistics, rural aquaculture, and cross―border supply chain management.

Economic Cooperation and Integration at Sub-regional Level

At the sub―regional level, the GMS economic cooperation program is helping the Mekong economies forge the links and trust that are vital to exploit complementarities, to address shared problems, and to generate economies of scale. Essential infrastructure remains underdeveloped in the GMS economies. ADB is playing a catalytic role in promoting trade and spreading development benefits throughout GMS through priority initiatives such as the East-West, North-South, and Southern Economic corridors. Power transmission interconnection options and the development of fiber optic transmission links also fall within the geographic scope of these corridors. As a result of greater ease of physical linkage, small towns are beginning to flourish and expand, new businesses are being established along many of the routes, and new markets are emerging, bringing a host of new entrepreneurial and employment activities.

The facilitation of cross―border trade and investment is another key feature of increasing sub―regional economic integration in GMS. The GMS program supports a range of measures to facilitate trade and investment that are designed to promote integration. These include improving procedures for customs clearance and increasing transparency in its application, and enhancing technical skills to improve the application of various regulatory systems. ADB is currently implementing a regional technical assistance to facilitate cross―border trade and investment. It includes the pilot testing of single-stop procedures of customs inspection at selected border sites. The GMS program is also helping member economies prepare for a single GMS visa system. Besides promoting tourism and reducing the direct cost of cross-border control and management, a single—visa system would have indirect but positive effects on trade and investment.

A number of other economic cooperation initiatives currently operate in the sub—region. These include the Development Triangle Initiative (DTI) involving Cambodia, Lao PDR, and Viet Nam; and Thailand's Economic Cooperation Strategy (ECS) that promotes development and closer integration with neighboring Cambodia, Lao PDR, and Myanmar. These initiatives complement the GMS program. There has also been a plethora of bilateral trade agreements (BTAs) in the broader region of late, with Singapore leading the region in concluding such deals. Thailand is the only GMS country that has been pursuing this option in any significant way, although Viet Nam has concluded a BTA with the US and so has Lao PDR. Thailand concluded its first bilateral agreement with Bahrain in 2003, and has made significant progress in negotiating bilateral deals with the PRC, India and Australia.

Economic Cooperation and Integration at Regional Level

At the regional level, Association of Southeast Asian Nations (ASEAN) and ASEAN Free Trade Area (AFTA) are driving trade liberalization and the opening of markets. All Mekong economies except Yunnan Province are ASEAN and AFTA members. AFTA has been the driving force behind regional trade liberalization in the Mekong economies. An agreement has been struck for PRC to join AFTA, so Yunnan will be a key region through which closer links will be forged between PRC and the current GMS members of ASEAN. The impact of trade liberalization through reciprocal trade preferences associated with AFTA membership may be observed most markedly between Yunnan Province and the Mekong region.

Tariffs have already fallen sharply for a wide range of commodities, and the Cambodia, Lao PDR, Myanmar, and Viet Nam (CLMV) countries are getting closer to their target dates when 0—5% tariffs will apply to most intra—ASEAN trade. For Viet Nam, this deadline is only about one year away, in 2006. Lao PDR and Myanmar must apply tariffs by 2008 and Cambodia, by 2010. Those countries' combined inclusion lists

(ILs) now comprise 72.2% of their total tariff lines, in contrast to 64.3% in 2002. In terms of tariffs, the rates of Common Effective Preferential Tariff (CEPT) on 60.6% of products that the CLMV countries trade in the region is already within the 0—5% tariff band.6 The average CEPT rate for the CLMV countries is now 6.2%, down from 6.8% in 2002. By late 2004, the ILs of the CLMV countries will probably cover 76.8% of their tariff lines. Of these, 66.7% will probably have tariffs within the 0—5% band.

Economic Cooperation and Integration at Multilateral Level

Some GMS economies are pursing globalization directly and independently through WTO membership, while others seek to join WTO. Thailand and Myanmar have been members for some time, and Cambodia joined WTO in September 2003. The other GMS economies are aggressively seeking membership. It is worth noting however, that WTO membership now will have less impact on Lao PDR and Viet Nam than it might have had prior to AFTA. Lao PDR conducts most of its trade with other ASEAN countries, so it already receives MFN and National Treatment (NT) in these countries as a result of AFTA membership. Lao PDR already receives preferential treatment in many non-ASEAN trading partners. WTO membership will not affect that. The only exception is in to trade with the US, but current indications are that granting of Normal Trade Relations (NTR) status may well supersede Lao PDR's accession to the WTO. The signing of the US—Lao PDR Bilateral Trade Agreement (BTA) in September 2003 is a sign of progress toward NTR status. The BTA is necessary for the implementation of normal trade status between the two countries, but will not go into effect until the US Congress enacts legislation authorizing NTR.

Viet Nam has a comprehensive and wide—ranging bilateral trade agreement with the US, and recently signed a trade and investment agreement with Japan that solidifies MFN and NT for its trade and investment. The bilateral trade agreement with the US involves various commitments that will not only complement its push for WTO membership, but will also fast track many of the benefits of WTO membership, currently aimed fort 2005. In other words, the reform measures that Viet Nam is now implementing for the US bilateral agreement, and the benefits that accrue from these measures plus the concessions that the US provides, will lessen the net impact of WTO accession.

But this is a good thing; it reaffirms the complementarities between regionalism and multilateralism. Perhaps the best illustration of this point is a comparison with the PRC's accession to WTO. The benefits of PRC accession to WTO are expected to be substantial, mainly because PRC has long remained relatively closed and isolated from the global community. But unlike the PRC, years of liberalization and opening up associated with participation in sub—regional and regional initiatives means that a significant portion of the benefits have already accrued to countries like Viet Nam and Lao PDR. Thus, the benefits of their WTO membership at this stage will be only incremental.

Considering this, the most significant benefit to Lao PDR and Viet Nam from WTO membership may well be its demonstration effect. WTO membership will signal to the rest of the trading world that these countries were able to satisfy a demanding set of international trade and investment rules and guidelines. The returns from strong demonstration effects should not be underestimated, because they can have a significant impact on forging new trading relationships and attracting FDI.

3. Impediments to Economic Cooperation and Integration in GMS

Despite the unprecedented progress and recent flurry of activities for the GMS, the sub-region is still beset by several lingering problems and the onset of more recent ones. Five of the six GMS members are continuing their transitions to a more open and market-based economy, but progress has been slow and incremental at best and, at times, even regressive. Some of the economic reforms have either not been launched by the governments or have been rescinded, creating an uncertain environment which deters many investors. The "one step forward, two steps back" approach to opening the economy has caused some investors to pull out of the GMS and relocate their investments elsewhere. Moreover, the legal and regulatory frameworks in many of the GMS countries are still below internationally—accepted standards.

A second issue hampering the progress of the GMS is that, despite repeated calls for greater involvement of the business sector, the GMS program still relies heavily on the multilateral agencies and the Governments. A combination of a weak private sector in most GMS economies, regulatory obstacles to the private sector, and insufficient interface between the private sector on one hand and the major GMS multilateral agencies and Governments on the other. A consensus has emerged all over the world that the private sector must be the driving force in economic development, with the Government playing a facilitating role. However, in some of the GMS economies the state-owned enterprise sector still dominates and inhibits the growth of the private sector.

Third, while the crisis—hit countries of East Asia have made important steps towards economic recovery, there are still several fundamental political and economic issues that need to be addressed:

a. While the economic philosophies have changed in the GMS to market-oriented economies, the bureaucracies contain many of the same people who were formerly guiding the centrally—planned economies. The shortage of government officials trained in market economic principles is clearly an obstacle for five of the six GMS countries.
b. The Governments tend to utilize control-oriented approaches to economic management. Slight reforms or openings are made, but often times the Government maintains strict control over business activities and in particular over policy—making.
c. Bureaucracies in many of the GMS economies are designed to prevent abuse as opposed to being efficient. Foreign investors frequently complain about the large amount of red tape involved in setting up and operating a business, importing and exporting, and other related activities.
d. The private sector is still viewed with suspicion by many of the GMS Governments. Although they proclaim to be committed to market—style economics, strict limits are set on competition (particularly with state—owned enterprises), the formation of business associations, labor unions, foreign ownership, and the movement of labor.

Other fundamental weaknesses in the GMS compound the aforementioned problems. The educational systems in the GMS are still weak in terms of the quality of education and levels of enrolment and retention. Also, the labor force in the GMS is in desperate need of upgrading its skills, but training programs are limited and there is typically a dearth of modern technology. Another barrier to development includes the financial systems in all of the GMS economies, which were epitomized by the near collapse of the financial system in Thailand in 1997 and 1998. The lesser developed GMS members have much smaller financial systems than Thailand, and credit is extremely limited at present. Investors' confidence in the GMS economies has diminished over the past few years because of these problems, but the underdeveloped legal and regulatory frameworks throughout the GMS are still a major barrier in attracting foreign investors. The Governments will need to continue making reforms for opening the economy and put in place the necessary legislation and regulations to create an environment conducive to business.

The GMS has been fortunate in terminating international hostilities in the region, but certain ongoing political issues will likely impede economic progress. For instance, some of the major multilateral agencies are prohibited by their stakeholders from extending loans or grants to Myanmar, and some Western donor countries have also refused to give loans or allow full trade and investment relations between their private sectors and Myanmar.

Additionally, an imposing challenge for the GMS is the inability to match the current economic and business needs for a modern economy. Shortages of trained workers, low levels of technology, few managers capable of operating modern factories, and a lack of entrepreneurship render some of the GMS countries uncompetitive in the regional and global economies. The sub—region must address these and other fundamental issues if it intends to spur growth and prosperity.

4. Strengthening Economic Cooperation and Integration in GMS

The success of the GMS hinges on the members' willingness and ability to facilitate the flow of goods, people, and services across borders. One of the main concerns of the GMS program is to pursue measures for increasing cross—border exchanges. Below are a few suggested activities that can be conducted in the GMS to help foster cross—border flows. One of the most effective ways of achieving these goals is to fast-track the implementation of various elements of ASEAN economic cooperation and to extend these in a formal way to Yunnan Province of China.

<u>Investment promotion</u>: Explore ways to attract local and foreign investment into the

GMS by marketing the complementary endowments in the area, the flow of production factors across borders, and possibly offer special economic zones with incentives. Possible activities for the growth triangle include: coordinating marketing strategies; institutional capacity building for local investment bodies; inter―agency cooperation measures; harmonized approval and regulatory procedures for cross―border investment projects; acceleration of the ASEAN Investment Area (AIA); and an investment information exchange system.

Trade facilitation: Consider approaches to improving the efficiency and effectiveness of trade procedures, documentation, and data exchange within the GMS. Possible activities include: harmonization of customs and inspections procedures and documentation requirements, developing a consistent classification system of goods; trade related information systems; joint export promotion activities; accelerating the AFTA; and establishing export quality standards for agriculture goods.

Business sector collaboration: Putting in place cooperation mechanisms between the business sectors in the GMS to support other activities and create a sustainable dynamic to create economic activity.

Value chains and cluster development: Taking the previous point one step further, develop networking within and among economic sectors throughout the GMS in order to foster supply and value added chains. Also explore policy and regulatory frameworks that will stimulate industrial cluster development in the GMS.

Industrial planning: Coordinate industrial planning among the members based on the potential complementarities and resource endowments. Promote the ASEAN Industrial Cooperation scheme among firms in the GMS to take advantage of the preferential tariff rates and non-tariff privileges. This will stimulate transnational production and value chains.

SME development: Pool resources and experience for special SME programs within the GMS. These could include special financing packages for SMEs, joint training, joint marketing efforts, and linkages with selected export destinations and foreign firms needing suppliers (i.e., matchmaking).

Human resource development: Embark on cross―national human resource development program for farmers, laborers, and entrepreneurs.

Rural development: Explore modalities for integrated rural development. The GMS is comprised of mostly rural areas that are deficient in basic infrastructure needs such as electricity, water, transportation networks, sanitation systems, education, and health.

Involvement of the private sector: The private sector must be the key player in the implementation of the GMS. Several attempts at fostering regional economic cooperation have failed because of the lack of attention to and involvement of the private sector. The business community is the engine of economic growth, and policy makers who are leading this initiative must make them equal partners in the planning and implementation of the GMS.

The appropriate role of government in the GMS: The governments of the GMS should see their role as providing an environment conducive to business and economic growth within the sub—region. This includes improving the legal and regulatory frameworks for business, allocating sufficient resources for the development of the border areas, and demonstrating a clear commitment to the deepening of the GMS program.

Continued economic liberalization: The full benefits of the GMS will be unobtainable if economic liberalization does not continue. To varying degrees, all of the GMS economies are undergoing reform in response to the inefficiencies and market distortions that became manifest the over past few years, especially during the Asian economic crisis. Moreover, they are facing contradictory pressures from home and abroad to protect domestic markets (including labor) or to further liberalization, respectively. Although the pace of liberalization is a matter for the individual governments to decide, regional cooperation cannot occur in an environment characterized by restricted markets, cronyism, and other unfair advantages to rent—seekers.

Set tangible goals and realistic expectations: Regional economic cooperation will not bring immediate benefits to everyone, nor will it quickly make the GMS globally competitive. Instead, it is a process that evolves over time and requires patience and nurturing. Members will need to prioritize activities and set forth goals that are practical and stand a good chance at being achieved. Unrealistic expectations and overly ambitious goals, which were clearly evident in the early years of the GMS, will lead only to slippage in implementation and disappointment with regional economic cooperation.

Conclusion

GMS has enormous challenges as well as potential for tremendous economic development, which will have significant bearing on the economic future of member countries in the region. Unlike EU and ASEAN, GMS possess a diverged socio— economic status comprising both economically backward and relatively advanced countries. The situation in GMS is better than SAARC. Considering natural and human resources and with participation of Thailand and China (Yunnan province), there is ample opportunity for GMS to sustain a new economic civilization in 21st century.

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