On the edge in Asia

Tuvshintugs Batdelger Mongolia’s economic prospects and challenges

Suiwah Leung Reforms vital for Vietnam to stay on track

Kirill Nourzhanov Divergent prospects flow from oil riches

Anushka Wijesinha Can Sri Lanka build a prosperous future?

Andrei Lankov Dangers in stasis, dangers in change for North Korea

and more . . .
From the editors’ desk

What is happening to Asia’s edges—spatially, metaphorically, economically? This issue of the EAFQ examines the prospects of places that tend to be overlooked by many international policy specialists. These essays have been selected for their potential to illuminate Asia in four important ways.

Sitting next to the region’s great powers can be tricky. Today both Myanmar and Mongolia are steering economic, political and diplomatic development alongside their giant neighbours. For Mongolia, its relationships with China and Russia have motivated a bold and inclusive foreign policy, one that has successfully cultivated new ties from western Europe to Australia. In the case of Myanmar, the post-dictatorship government is using its fresh democratic credentials to escape the suffocating embrace of China.

We look to places where edges mean borders and frontiers. In Bangladesh and northeast India the management of cross-border issues is enduringly problematic. And as the tragic experience of Bhutan’s minorities show, the edge can be a profoundly unhappy place.

Being on the edge in Asia also can imply a heightened sense of anxiety. Issues explored in this Quarterly—from dam developments on the Mekong and land disputes in Cambodia to the parlous security situation in Pakistan and the dangers of North Korean brinksmanship—all give extra reasons to worry. It is unclear that Asia has the institutional structures or the unanimity of purpose to support long-term solutions.

Finally, at the edge we should be getting ready for the next big thing. Post-conflict development remains a major challenge in a number of countries. Vietnam has shown the way. Sri Lanka and Myanmar aspire to such success. The lessons they can all learn from the resource-rich states of central Asia should not be ignored.

For now, the edges of Asia are where we can judge the early indications of the most overwhelming changes. In the countries adjacent to China and India, the 21st century will present disorderly opportunities, grave possibilities and the chance of something better.

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Mongolia’s economic prospects and challenges

TUVDHINTUGS BATDELGER

In recent years Mongolia has become one of the most rapidly expanding economies in the world. According to the Economist Intelligence Unit, it was one of the top performers in 2013, with economic growth of 11.7 per cent, and it is projected to be the second top-performing economy in 2014, after South Sudan (about 15 per cent).

Mongolia is a sparsely populated country with a total population of 2.9 million. Because of the economy’s rapid expansion over the past few years, the World Bank now classifies Mongolia as a mid-low income country for per capita income, and it is expected to enter mid-high income in the near future according to Mongolia’s Ministry of Economic Development.

The main driver of this rapid economic expansion has been the development of the mining industry. Mongolia is richly endowed with natural resources. With increasing commodities prices in the world market for the past 15 years, the mining sector’s share in GDP increased from 14 to 25 per cent. Mongolia’s main export commodities are copper, gold and coal, and Mongolia is now one of the major coal exporters to China, briefly overtaking Australia in 2011 and 2012.

Moreover, it is expected that during the next five years major mining projects of copper (Oyu Tolgoi project) and coal (Tavan Tolgoi project) will reach their full potential, likely further increasing economic expansion. By some estimates, Mongolia’s GDP will reach US$25 billion by 2020, which is 2.5 times the size of today’s economy.

These developments haven’t gone unnoticed in the world market. Mongolia has become one of the most attractive economies for investors. In 2013 alone the Mongolian government sold US$1.8 billion of bonds in world markets, which is a testament to the strong upside expectation of the economy.

However, the Mongolian economy faces serious challenges to reach its full potential and take advantage of the mining boom’s opportunities.

Since Mongolia is becoming increasingly dependent on the export of raw minerals, world price fluctuations for commodities have destabilising effects on the nation’s economy.

Therefore a major policy question is whether Mongolia has enough safeguards in place to protect itself from drastic fluctuations in its terms of trade. Inside Mongolia there is broad agreement about the need to conduct countercyclical macroeconomic policies—especially that the government should be saving during good times to be able to maintain the level of expenditure during economic troughs and stimulate the economy when needed. However, looking at
the past 10 years of policymaking, Mongolian governments have found it hard to implement these policies in practice.

During and after the 2008–09 world economic crisis the difficulties of implementing and maintaining these policies were on full display. One problem was that, in order to win elections, political parties had great incentive to promote and execute populist policies, such as cash distributions to citizens. To stop these kinds of policies, which greatly hurt macroeconomic stability, major political parties agreed to control this practice and the parliament passed the Fiscal Stability Law in 2010, putting limits on government debt, increases in expenditure and the budget deficit. However, even this law was not enough to discipline the government.

Since the country desperately needs to develop and expand its infrastructure to promote economic diversification, the government has found it hard to resist spending more. Its efforts in raising capital by issuing bonds in foreign and domestic markets, and spending it through the newly established Development Bank of Mongolia (DBM), have undermined the spirit of the Fiscal Stability Law. At the end of 2013 the budget deficit was at 8 per cent of GDP (including the DBM’s loans) and the overall debt level already exceeded the limit of 40 per cent of GDP set out by the law.

It should be noted that the exchange rate’s sharp depreciation was also exacerbated by a decrease in the country’s terms of trade. In contrast to previous years, the terms of trade fell by 15 per cent in 2013. Subsequently, the current account deficit for the year reached US$3 billion, or 28 per cent of GDP, and foreign direct investment decreased by 48 per cent, according to Mongol Bank Balance of Payment statistics.

This sudden reversal in foreign direct investment also reflects another great challenge for the country. It is evident from the experiences of resource-abundant countries that the quality of institutions is a key ingredient in successfully taking advantage of the opportunities presented by the mining boom. That is, if a country’s institutional quality remains weak, the country will not be able to attract foreign investment, which is of paramount importance to reaching full economic potential.

Mongolian institutional quality is still lagging behind its stellar economic growth numbers. The quality of institutions can be partly measured by rankings, including perceptions of corruption, where Mongolia was ranked 83rd of 177 countries on the 2013 Corruption Perceptions Index.

Government’s increasing role in the economy . . . makes it an attractive breeding ground for rent-seeking by government officials.

Perhaps the most disturbing is the corruption index. Government’s increasing role in the economy (government expenditure, including the DBM, is estimated to be around 47 per cent of GDP) makes it an attractive breeding ground for rent-seeking by government officials. Although Mongolia is making some progress in tackling corruption at state and regional levels, with some high-profile cases having been through the Mongolian justice system, it could be that these cases are just the tip of the iceberg.

Such challenges are not unique to Mongolia, and are experienced by many countries with abundant natural resources. Countries that have been able to put in place good institutional arrangements have overcome these obstacles and the so-called ‘resource curse’, whereas countries struggling with corruption, governance and accountability have not.

Most importantly, the outcome of these challenges will greatly affect the livelihood of Mongolians. As of 2013, the poverty rate is 28 per cent. Whether the country can translate the mining boom into a better livelihood for all citizens remains to be seen.

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MONGOLIA IN THE REGION

Time for economic foreign policy

JULIAN DIERKES

Mongolia has been extraordinarily successful in building a foreign policy around the Leitmotiv of ‘third neighbours’ for the past 20 years. Reinforced by the country’s democratisation and the promise of mineral resources, this foreign policy has helped Mongolia to claim much more attention on the global stage than one might expect from a vast country of only three million inhabitants. Despite this success, Mongolian policymakers will have to reconsider their focus on political relations in helping Mongolia to grow further and into a more diversified economic future.

The basis of Mongolian foreign policy involves balancing economic, military and political considerations between China and Russia. This foreign policy approach has been well-maintained since 1990, especially in the absence of alternative safeguards for Mongolia’s security.

There have been flare-ups in relations with neighbours, of course, such as China’s blocking of the railroad link between the two countries over the Dalai Lama’s visit in November 2002, or the Russian grab for Mongolian uranium in 2009. But on the whole, Mongolia has been able to maintain constructive relations with its immediate neighbours.

Beyond this, the Mongolian government has successfully pursued its long-term goal of cultivating close friendships with powerful but distant countries. Among these third neighbours, the countries targeted have been Australia, Canada, members of the European Union (especially Germany), India, Japan, South Korea, Turkey and the United States.

Engaging these third neighbours has had a real impact on Mongolia’s economic, political and social development. For example, Mongolia’s per capita foreign development aid has fluctuated around US$100 since the mid-1990s, on par with aid offered to some least-developed countries. While this level of material support (particularly from European countries and the US, but more recently also from Australia) may have had much to do with the democratic turn that Mongolia took in 1990, it has been reinforced by the active Mongolian engagement of its third neighbours.

This engagement, coupled with Mongolia’s increasingly prominent involvement in UN peacekeeping operations since 2005, has also given the country a far greater international presence than might be expected. As of early 2014, Mongolia contributed roughly 1 per cent of all personnel currently deployed by the UN in peacekeeping operations (935 military experts and troops out of a total of 98,200). This visibility has found its most obvious expression in Mongolia’s accession to the Organization for Security and Cooperation in Europe (OSCE), and hosting the Community of Democracies in Ulaanbaatar in April 2013 and World Environment Day in June 2013. These are all
indicators of a successful soft power deployment that is also leading to real material impacts, primarily through development aid.

Now Mongolia’s circumstances are changing massively. Per capita GDP has grown from less than US$1000 to over US$3500 in the new millennium, and the past three years’ double-digit growth puts GDP on an upward trajectory and a likely entry into the ranks of upper middle-income countries in the near future. Accordingly, development aid to Mongolia is likely to shrink. Japanese aid will be converted from grants to loans in the near future and other programs will surely follow suit even when some countries’ contributions, like Australia’s and Canada’s, are just revving up.

As inward-bound development aid is changing, Mongolia has set up its own aid program, making food donations to North Korea in the past year. From receiving aid, Mongolia may thus be making a slow transition to providing aid.

In this transition, private enterprise and investments from abroad as well as domestic sources are playing a greater role for Mongolia’s development. Decisions about the giant Oyu Tolgoi gold and copper project will be made primarily within the management of majority owner Rio Tinto, and will be much less subject to governmental deliberations than development aid was. Mongolia continues to consider whether the government should still participate in such investments and at what level, but it is clear that foreign capital will be private capital, not foreign governmental contributions. A foreign policy that is primarily aimed at building and maintaining intragovernmental political friendship will not have much of a direct impact on such investments.

During Mongolia’s democratic period, discussions of increased economic integration with the Northeast Asian region have come and gone without having emerged as a driver of Mongolian foreign policy. There is, of course, significant potential here. But with the shift in global attention and activities from global trade negotiations to the ‘spaghetti bowl’ of numerous bilateral trade agreements, Mongolia’s nearly exclusive focus on political relations may leave it isolated from any agreements that might emerge.

While the trilateral FTA negotiations between Japan, South Korea and China are still at a preliminary stage, the fact that they have already continued for three rounds in a context of less-than-cordial relations in East Asia signals the importance that these negotiations might have in future. There is also no obvious incentive from the perspective of the negotiating parties to include Mongolia in any agreements that might emerge. While the trilateral FTA negotiations between Japan, South Korea and China are still at a preliminary stage, the fact that they have already continued for three rounds in a context of less-than-cordial relations in East Asia signals the importance that these negotiations might have in future. There is also no obvious incentive from the perspective of the negotiating parties to include Mongolia in any agreements that might emerge.

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Beyond intraregional relations, another great obstacle to the emergence of Northeast Asia is surely North Korea. Here, Mongolia has also been unusually active through bilateral visits and some investments.

While Mongolia should not abandon the success of its politically popular third neighbour policy and replace this with a ‘three neighbours’ policy focused on China, Japan and South Korea, a shift to policies that are designed to strengthen economic relations, not only political friendships, is likely to cement Mongolia’s development as well as its world standing. A recent shifting of the trade portfolio between ministries is one indication of the debate about an economic foreign policy that is and should be coming to Ulaanbaatar.

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ANXIETIES IN MYANMAR

Road to constitutional amendment going nowhere

MELISSA CROUCH

SINCE Myanmar’s Joint Parliamentary Constitution Review Committee submitted its report to the Union Parliament on 31 January 2014, the constitutional amendment saga has taken another twist.

The committee was given the task of reviewing the 2008 constitution, which had been drafted by the previous military junta. It was required to make recommendations to the parliament, yet it ultimately avoided this responsibility. Many activists now agree that the amendment process is not genuine.

When the committee was established in 2013, there was some scepticism mixed with a glimmer of hope. Confidence in the process grew as a clear timeframe was set, making it possible that any proposals might have time to go through the necessary approval process before the 2015 elections.

A call for public submissions was even issued. This generated a flurry of constitutional campaigns and conversations across the country as political parties, social organisations, ethnic groups and religious groups held discussions and finalised submissions to the committee. Reports suggest that the committee received a huge number of submissions.

Yet public confidence in the process was shaken when the committee’s initial deadline to submit its recommendations to the parliament, 31 December 2013, was extended to 31 January 2014. For many democracy activists, especially the older generation, this announcement heightened fears of prolonged constitutional discussions leading to negligible outcomes, like in the past.

The constitutional review process has also been marked by Aung San Suu Kyi’s failed request for an audience with the president. In November 2013 and on several occasions since then, she has called for a meeting with the president, the speaker of the lower house and the commander-in-chief. She has insisted that this is a necessary step to discuss the constitutional amendments.

The committee’s report appears to have confirmed the fears of sceptics. It simply collated data on the number of provisions that were suggested to be amended and those that should stay the same. The committee failed to come to any conclusions on the substance of the constitution’s text—that is, which provisions should be amended and how.

The most controversial aspect of the report was that it noted that there were three key aspects of the constitution that should not be amended. This was based on what appears to have been a petition signed by 106,102 people, although it does not confirm the source of this petition.

The first was the role of the military. The report noted that the petition wanted the military to retain its role in politics (and as the country’s armed forces). It also noted that the petition’s signatories were in favour of retaining the section that grants immunity from prosecution for past and present members of government.

Third, the same 106,102 people
of the petition recommended that the provisions on the constitutional amendment process be retained. This process requires 75 per cent approval of parliament, and for some provisions also requires more than 50 per cent of eligible voters at a national referendum. These provisions would remain an obstacle to be overcome for any future amendments.

Yet this alleged petition has been heavily criticised and suspicions have been raised about its validity.

Some activists are now drawing parallels between the current situation and the lead-up to the approval of the 1974 constitution. In the early 1970s, Ne Win’s socialist regime claimed to have widely consulted the people and gathered a large number of signatures in support of the draft constitution. This alleged show of support for the constitution was used to justify its approval, yet it only entrenched another 14 years of Ne Win’s rule.

Where will Myanmar’s road to constitutional amendment lead today? After the committee’s report was delivered, on 3 February the parliament established a committee for its implementation. Consisting of 30 members of parliament, this new committee must now make a final report on constitutional amendments.

Yet if this second committee proceeds on the basis of the validity of the first report, the road to amendment will not see any reduction in the role of the military in politics. Nor will it promote greater fairness in the presidential nomination process. This has serious implications for the elections in 2015, and suggests that the reform process itself has stalled.

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AUTHORITY SHIFTS

Balancing reform and justice in the transition

ADAM P. MACDONALD

The reform agenda enacted by President Thein Sein has been impressive on many fronts. The last three years signal he has a real desire to change major aspects of the state and society.

But these reforms have not reached the security portfolios and institutional independence of the military. The military carefully cordoned off these realms via constitutional provisions before transferring power, effectively becoming a veto player in political proceedings. As a result, many believe that the military’s removal from the political apparatus is necessary for the country’s transition towards democracy.

While much commentary has

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legitimately focused on these matters, another interrelated issue is whether seeking justice for abuses committed during the military junta’s reign will be a priority for any future government. Such abuses include suppression of the Saffron Revolution, inept and perhaps deliberate inhibition of aid responses to areas hit by Cyclone Nargis, and multiple rights abuses, such as land seizures in the ethnic borderlands, to name a few. But the military’s rights abuse record continues even in the transition era, as a recent Women’s League of Burma report attests—documenting 100 cases of rape by the military since 2011.

Although the opposition party, the National League for Democracy, will most likely win the 2015 elections—barring electoral manipulations—it has been largely silent on the issue of justice, for good reason. While defeating the governing Union of Solidarity and Development Party would remove the military-supported regime, it is likely the military itself will remain a powerful political actor whose cooperation will be needed in the effective running of the state.

It is doubtful that Myanmar can transition away from authoritarianism towards democracy without the military itself undergoing significant change. In particular, a complete reconfiguration of civilian–military relations is required. This would include the development of civilian
expertise and presence within security portfolios, parliamentary oversight of the military, the transformation of the Tatmadaw—the Myanmar Armed Forces—into a professional service, and its eventual removal from all levers of state power. These endeavours would necessitate changes in responsibilities and duties between civilians and the military. The changes would also ideally stem from a deeper normative shift in relations in terms of legitimacy and authority. 

But within such a project, where does the pursuit of justice fit in—if at all? Is justice a prerequisite for the entrenchment of democracy, or an undertaking that should be pursued once democracy is firmly established? Could such moves alienate the military and other power-holders, undermining the reform process on the whole?

The proliferation of actors in the political landscape who have different identities and sources of legitimacy has eroded earlier (and simpler) characterisations. Those characterisations included reformers and democrats on one side, and the military and their surrogate regime, led by former officers, on the other. In particular, officers turned politicians, such as President Sein and Speaker Chairman Shwe Mann, have created new identities and new loci of power and support that distance themselves from the military, without coming into open conflict. The divide between the military-as-institution and the (former) military-as-government shows how power has been dispersed among numerous actors, opening avenues for new identities, interests and relationships to emerge.

But attempts to bring former junta members to account would implicate many within the government and the military. They would most likely bind together in an attempt to avoid prosecution, erasing the growing divergence amongst them. Reformist elements within these organisations might then be sidelined as a more obstructionist position was assumed against civilian politicians. A significant obstacle is that members of the previous military regime are immune from legal actions as guaranteed in the Constitution (Article 445); and constitutional amendments will require military consent.

With this in mind, it is very likely that Myanmar in the future will establish some form of truth and reconciliation commission, as many states have done after emerging from authoritarian rule. Acknowledging the unique factors within Myanmar’s past and current transition, much can be learned from historical examples, including Chile, Argentina and South Africa. The South African case is particularly intriguing as many applauded the focus that was
Awaiting the boom

Making the next Asian miracle

ANDERS ENGVALL

Myanmar’s reforms are lifting the economic outlook for one of Asia’s economic laggards as indicators show prospects for an economic boom.

For decades, Myanmar was the regional basket case as irrational policies, isolationism and domestic conflict wrought havoc on the economy and society. At independence in 1948, the outlook seemed bright. The country had one of the best education systems in the region, it was integrated with world markets through the port of Rangoon, and possessed ample natural resources and a sufficiently well-functioning administrative system. All of these advantages were spoiled during decades of authoritarian rule.

Resources degenerated over decades of stagnation—particularly through declining quality of education and infrastructure—leading to falling productivity.

Economic reforms in Myanmar were actually initiated before the country’s political reforms. And while many of the early economic initiatives primarily served to enrich cronies through fire sales of state assets, there were also important policy shifts.

Even before the 2010 elections, macroeconomic policies had improved. A key indicator of improved management is the stabilisation of inflation below 10 per cent since 2008–09. This is a marked achievement in a country where spells of rapid price increases used to be the norm.

Infrastructure developments during military rule largely served strategic purposes, and wasteful investments expanding railways to remote upland areas have given no sustained economic return. But there were improvements in physical infrastructure developments in the decade before 2010 as focus was shifted to improving the main north–south corridor and links to markets in neighbouring countries.

Administrative barriers to both domestic and international trade remain, but abolition of the restrictive trade regime and unification of the exchange rate in 2012 have produced impressive export growth. Resource-based commodities, primarily natural gas and minerals, are leading Myanmar’s trade growth. The country’s location between the expanding economies of China, India and mainland Southeast Asia not only provide opportunities for transit trade but are also advantageous for supplying these resource-hungry markets with commodities.

The rural economy is going through a rapid transformation as exports of rice, beans and other agricultural commodities expand. Rice exports more than doubled in 2013, primarily fuelled by cross-border trade with China, and are set for more rapid growth this year. Rural development is not only benefiting from new opportunities in agricultural exporting, which had been prohibited for decades, but also from important policy shifts giving farmers freedom to decide which crops to grow. Rural

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More on reconciliation than criminal prosecution (with many Apartheid members granted amnesty) because it ensured the process did not inflame racial divides. But some criticised the focus, arguing that justice is a precondition and not an alternative to reconciliation. Given the power of Myanmar’s military and the permeation of retired officers into government and business, perhaps the South African case could be a blueprint for how to pursue these matters without disrupting the overall reform process.

Seeking justice is an important issue. But continued support for incremental change would most likely overrule such desires in the short to medium term. The eventual task of approaching the sensitive subject of the military’s political role and legacy will have to be managed in such a way as to create strong and cooperative relations with the military. In particular, it must be emphasised that—if any legal proceedings or tribunals occur—the aim is not about punishing the military as an institution. Rather, the aim is to support a transformative process to change the military internally into a professional service that can build new external relations with the political apparatus and society as a whole.

This may not be satisfactory to many, but reformers must walk a careful line within the contemporary political balance of power. They must promote gradual change while at the same time not drawing hostility from those who still hold significant power in Myanmar—reform and justice must be balanced to keep the system functioning.

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credit remains scarce but expansion of state credit to farmers at favourable rates has increased. Land law reforms may provide additional relief as farmland will be eligible as collateral, opening a pathway for increased private credit to the agricultural sector.

It will be essential that policymakers focus on spreading the benefits of growth across the population. Inclusive growth, alleviating widespread poverty and improved welfare will build support for economic reforms and may also lay the foundations for solving the country’s long-running domestic conflicts.

Essential investments in healthcare and education will only be possible if the government is willing to commit a substantial share of its revenues from exports of gas, oil and minerals to the social sector. This would be a dramatic change from the past, when income from extractive industries was used to fund the bloated armed forces, the construction of the new capital, Nay Pyi Taw, and other projects of limited social benefit.

Remaining weaknesses in macroeconomic management are also a threat to long-term developments. Sustained inflows of foreign investment, export revenue and foreign aid risk making the overvaluation of the kyat permanent, and should be managed carefully. A short decline in the currency value in the second half of 2013 provided important relief to exporters. But there is no indication that the authorities will continue to bring down the strong currency, due to fears of a return to the hyperinflation that was common in the past. The currency rate continues to constrain the development of manufacturing, and, while this obstacle remains in place, efforts to set up industrial zones will be futile given Myanmar’s cost disadvantages compared to the main East Asian production bases.

Still, the reforms to date have led to a convergence of growth rates in Myanmar to the East Asian average. If remaining weaknesses are addressed, there is scope for further acceleration and that would turn Myanmar into the latest Asian economic miracle.

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CHAIRING ASEAN

Myanmar dressing for a role on the world stage

CHIT WIN

In the aftermath of the devastating Cyclone Nargis in 2008, ASEAN and the UN organised an international pledging conference in Myanmar to rally international financial support. It was the biggest international event of its kind in the country’s history. General Thein Sein, then the prime minister, chaired the meeting. Surprisingly, he wore Myanmar’s traditional business attire (taikpone and longyi) rather than his usual military uniform. Some might have overlooked this fashion signal, but it seemed to endorse the need to transform Myanmar into a civilian rather than a military regime. After three years, Thein Sein went from prime minister and general to president—dispensing with his green uniform once and for all.

In 2014, Myanmar is set to host the top-level ASEAN summits for the first time, under the theme of ‘Moving Forward in Unity towards a Peaceful and Prosperous Community’. Apart from the usual fancy and fashionable tailor-made dress occasions, will Thein Sein decide to wear an international outfit rather than the usual Myanmar attire? Wearing a business suit could be seen as a strong signal to the international community of Myanmar’s return to the international arena. As one of the few countries that has successfully kept its traditional outfit as business attire, it would be a pity if Myanmar decides to change into Western dress. But through the attire it displays on the world stage at this event, Myanmar can show that it is part of ASEAN and the broader international community.

This is a crucial year for Myanmar. It still faces domestic challenges, or ‘growing pains’, such as communal conflict, progress on the peace process, constitutional amendments and the huge logistical exercise of the census which requires co-operation from ethnic armed groups. This year it will choose the next steps in its reforms through two critical political processes. First is progress toward peace through countrywide ceasefires and political dialogues with ethnic armed groups. Second is amending the constitution, including article 59(f) which dictates the qualifications required of any prospective president.

But if Myanmar wants to demonstrate ‘we can do it’ for ASEAN leadership—as it did for the Southeast Asian Games in December 2013—the country has to be careful domestic issues, especially the communal conflict that still haunts Myanmar, do not attract scrutiny by ASEAN.

Myanmar’s policymakers will not want any of the nation’s domestic issues to become part of the core ASEAN agenda, and so hamper ASEAN meetings during its chairmanship. As such, Myanmar is expected to be extremely careful in tackling domestic issues. In addition, Myanmar may accept friendly gestures supporting its chairmanship. Therefore, the international community should do what it can to collaborate with Myanmar in order to support its further democratisation process during its chairmanship.

On the other hand, there has been media speculation about Myanmar’s capability in stewarding ASEAN, with criticisms ranging from the logistical to the substantive. Singapore-based ASEAN analyst Moe Thuzar predicted that Myanmar would have to host around 240 to 400 meetings, including major regional summits and ministerial meetings. She suggested that Myanmar might have gained experience from being a member of ASEAN for more than 16 years, but pointed out that domestic affairs such as communal conflict might affect its chairmanship. She also suggested that ASEAN could measure Myanmar’s performance through the prism of the South China Sea dispute between China and some ASEAN member states.

With logistical and resource constraints compounding domestic challenges, Myanmar may feel that
its job has been accomplished with photo opportunities and a magnificent opening ceremony that goes off without any security or logistical glitches—all without touching on sensitive and complex regional issues such as the South China Sea controversy.

But such an approach could lead to relatively modest outcomes for Myanmar. Justine Drennan has warned Myanmar to learn from Cambodia’s bitter experience, when it was perceived as being under the heavy influence of China, its major donor. In the case of Myanmar, Nay Pyi Taw has a convention centre that was a token of friendship from the Chinese government. But—in an unexpected move—Myanmar recently opened another glamorous convention centre in Nay Pyi Taw for the sole purpose of hosting the ASEAN Summit, a symbolic move that may be interpreted as Myanmar taking charge.

One should not underestimate Myanmar’s long-term vision of becoming a regional powerhouse. Its strategic geographical position as well as its size affords it this opportunity. Myanmar foreign policymakers still remember the nation’s glory days at the Trusteeship Council of the United Nations and in the Non-Aligned Movement where it was a driving force of the success of these organisations during the 1950s and 1960s. The position of ASEAN chair may awaken Myanmar’s foreign policy ambitions once again.

Against all these domestic and logistical odds, while ASEAN may have tempered expectations of Myanmar’s leadership, the fashion signal of President Thein Sein will be worth our attention. Whether he wears a lounge suit or traditional attire might at least reveal Myanmar’s willingness to engage with future challenges.

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After several years of macroeconomic turmoil, 2013 finally saw a return to some semblance of stability in the Vietnamese economy. There is no time to lose. The government needs to push through significant reforms in key areas in order to lift long-term growth. Macroeconomic aggregates have been mixed. Headline inflation averaged 6.7 per cent, due partly to subdued credit growth and an easing of food prices. Core inflation (excluding food and energy costs) stood at 10 per cent, after increases in a number of administrative prices, such as education and health costs. Core inflation is expected to continue declining this year and next due to below-trend growth.

Strong performance in both exports and remittances saw Vietnam’s current account record a surplus of 5.9 per cent of GDP in 2012, and an estimated surplus again of 5.1 per cent in 2013. As a result, pressure on the dong has eased, and the official and black market exchange rates have converged. But overall GDP growth is at a sub-trend 5.3 per cent in 2013, rising to a forecast rate of 5.5 per cent by 2015.

There is now clear evidence that Vietnam has climbed on to the production network in electronics and accessories, mobile phones and parts, computers, and automobile parts. Export of mobile phones and parts is estimated to have reached US$18 billion in the first 10 months of 2013, surpassing even garment exports. This is the result of significant foreign direct investment over the past five years by multinationals such as Intel, Samsung and Nokia. Samsung has been the outstanding export performer so far, and Vietnam risks over-reliance on one company.

Nevertheless, all these multinationals have linked Vietnamese manufacturing to the global production-sharing supply chains and transformed the composition of its export basket. Export of electronics, mobile phones and accessories grew from less than 4 per cent of total exports in 2003 to more than 32 per cent 10 years later. At the same time, traditional labour-intensive manufacturing has also done well, averaging growth of more than 17 per cent in 2013, with garment exports growing at 18.5 per cent.

Industrial policy is once again fashionable. It is claimed, however, that the new focus is not on ‘picking winners’ but on developing an enabling environment for industries and firms to move into new products and into higher value-added activities within existing product lines. While there is...
certainly a role for trade facilitation in promoting industrialisation and growth in Vietnam, what will bring higher long-term growth are reforms in state-owned enterprises (SOEs), bank restructuring, and improved public finance and administration.

The costs of doing business—including but not limited to wages—must be kept competitive. These include the costs of telecommunications, insurance, electricity, gasoline, shipping and customs facilities, rentals for offices and expatriate personnel accommodation. But most of these areas are dominated by SOEs. Hence the progress of SOE reforms will have a profound impact on the competitiveness of all Vietnamese firms.

In the garment industry, where the lack of domestic supply of both quantity and quality textiles is identified as one of the major constraints to development, SOE presence is still as high as 21 per cent. Removing state firms from activities that are purely in the private domain will help to develop backward linkages, enhancing flexibility in catering to changes in international consumer tastes, and reducing the reliance on imported textiles and fabrics. Finally, in the large conglomerates of state enterprise groups and general corporations, involvement in non-core activities such as real estate, insurance, and banking raises the risks of contingent liability and fiscal bailouts.

Progress in reform is slower than expected, despite a number of decisions made during 2013 about the disclosure of financial and non-financial information, linking SOE manager remuneration with performance, and removing the requirement to sell state assets at least at book value. Current legislation is not clear about what information is to be disclosed, and to whom. The question of what to disclose is supposed to be addressed in Decree 61 to be implemented in 2014, but inter-agency coordination is lacking and needs to be resolved.

Case studies of the garment, footwear and electronics industries have all found that lack of finance is a constraint to small and medium enterprises (SMEs) and start-ups. In the case of Vietnam, simply removing the regulation forcing banks to lend (allegedly for prudential reasons) only to firms with a proven past history of operations would open the way for funding start-ups. This is not to say that bank managers necessarily have the skills or the risk preference for lending to start-ups and SMEs, particularly when they can make more profitable and secure loans to SOEs. But building a strong and commercially oriented banking sector by implementing the reforms that are already in the government’s plans would encourage bank lending to all productive enterprises, including SMEs.

Here again, progress needs to be accelerated. The issue of non-performing loans (NPLs) continues to undermine confidence in the banking sector and hinder credit growth. Moody’s estimate in February 2014 of NPLs at 15 per cent of banking assets raised serious questions regarding the official estimates by the State Bank (SBV) of 4.6 per cent last October, and an even lower estimate of 3.6 per cent at the start of February 2014. The subsequent statement on the SBV website of a NPL ratio of 9 per cent if more stringent definitions were used was, in fact, an admission of regulatory forbearance on its part. One of the problems is ‘gaming behaviour’ on the part of some commercial banks which purchase bonds from their corporate borrowers so that those companies can use the funds to reduce their NPLs with the banks. Some banks overvalue collaterals to minimise provisions for NPLs. The recent Decision 843 is supposed to give the State Bank more power in auditing commercial banks’ NPLs, but the credibility of the SBV itself needs to be re-established first. The setting up of the Vietnam Asset Management Company (VAMC) in July 2013 is generally viewed as another way of getting NPLs off the books of commercial banks. Whether the VAMC can resolve the NPL issue in due course depends importantly on the amount of capital that it is able to raise. Meanwhile, more relaxed foreign bank ownership rules should help strengthen the banking sector and make it more commercially viable.

In addition, improved government finance is necessary for investments in infrastructure and human resources—essential ingredients for long-term growth.

In short, continued stability on the macroeconomic front, together with impressive growth in manufacturing exports, indicates that the medium-term prospect for Vietnam has improved somewhat in the past 12 months, albeit with significant downside risks. Time is of the essence. Providing the government can move on with SOE reforms and bank restructuring while maintaining fiscal discipline—and providing that the world economy remains in an upward trajectory—it is still possible for Vietnam to succeed in lifting its longer-term growth.

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AT THE CROSSROADS

Dangers in stasis, dangers in change for North Korea

ANDREI LANKOV

At a cursory glance, North Korean policy over the last two decades may seem profoundly irrational. The country has continued to cling to a grossly inefficient and anachronistic economic system, once patterned on the Soviet economy of Stalin’s era. Predictably, the North Korean economy folded in, leading to a disastrous famine in the mid to late 1990s (it has since recovered, but only partially).

At the same time, in its immediate region, one can see seemingly irresistible and shining examples of how very similar problems have been solved. China in the 1970s and Vietnam in the 1980s faced challenges that were remarkably similar to those that North Korea faces now. These two countries faced up to their economic challenges through reforms that implemented de facto switches to market economies while maintaining the old ‘communist’ ideological facade.

North Korea’s decision, under Kim Jong-il, not to do the same might appear irrational to outside observers. But if one examines the peculiarities of the situation in detail, from the North Korean perspective it makes a great deal of sense.

In many regards North Korea has more in common with the now-defunct East Germany than with China: it is a part of a divided country whose two parts have massively different living standards. While in divided Germany the per capita income of the West was two to three times greater than the East, in Korea the South enjoys a per capita income at least 15 times greater than the North.

If North Korea starts reforming itself in accordance with the Chinese model, information about South Korea’s affluence (thus far largely hidden from most North Koreans) will unavoidably spread among ordinary citizens. North Korean propaganda presents South Korea as a country populated by the same ethnic nation, so the North Korean people’s discovery of the size of the disparity would deliver a mortal blow to the legitimacy of a reforming North Korean government. North Koreans would labour under the illusion that unification would result in instant riches. As a result, reforms hold the potential to trigger an East German-style popular revolt, rather than a Chinese-style economic success.

Kim Jong-il thought that Chinese-style reforms were prohibitively risky for the viability of the regime. But will this policy be continued by the emerging Kim Jong-un regime? It remains to be seen, of course, but there is a major difference between father and son. This difference is not Kim Jong-un’s Western education and experience but rather his youth.

The major problem that the North Korean elite faces is simple: whether it reforms or not, the North Korean system is gradually disintegrating from below. The state-controlled, centrally planned economy shrank dramatically in the 1990s and many factories remain non-functional. Rations are distributed only sporadically and most North Koreans make a living through a diverse set of technically illegal activities associated with the private economy. Most importantly for the regime, information about the outside world, and South Korea in particular, is spreading inside the country thanks to DVDs and other modern technology.

This means that in the long run the system’s days are numbered, though the system could still survive for some decades to come.

Under the rule of Kim Jong-il, it was reasonable to expect that the system would continue for another 10–20 years so long as the government did not undertake any dramatic and destabilising changes. This was more than enough time for Kim Jong-il and his entourage, who were men in their 60s and 70s. But a 20-year life expectancy for the regime is not sufficient for its new leader, who is, after all, only 31 years old.

Kim Jong-un has some valid and rational reasons to do something to which his father was deeply opposed: to attempt to change the country, reviving its economy and improving its living standards.

Any possible North Korean version of Chinese reforms is likely to be significantly different from Deng Xiaoping’s reforms in China.

The North Korean leadership has to be especially cautious and move...
slowly. In China, the reformers in charge have been very careful to maintain the disingenuous communist facade, even while building capitalism. Similar measures will be even more vital for North Korean reformers, who will almost certainly describe their efforts as a means by which they will perfect Juche-style socialism. Given the nearly irresistible allure of South Korean prosperity, North Korean reformers will also treat their own people with great brutality, crushing all signs of dissent.

For the outside world, the nuclear issue is, of course, of great importance. In this regard, it is clear that North Korean reformers have little incentive to surrender their nuclear weapons.

While denuclearisation might bring some investment from the outside world, it will also make the country quite vulnerable to foreign attack. More importantly, it will make the government helpless if a local revolutionary movement erupts and then gets foreign support—as was recently the case in Libya. After all, the unlucky Libyan dictator, Muammar Gaddafi, is the world’s only dictator who agreed to jettison his nuclear program in exchange for economic benefits. There is good reason to believe that the West would have been far more reluctant to support anti-Gaddafi forces in Libya had the country remained a nuclear state under a dictator renowned for his unpredictability. This harsh lesson was not missed by the North Korean leadership.

Kim Jong-un’s government faces a choice. On the one hand, it can continue to follow his father’s policy of stasis, maintaining the status quo at the cost of economic stagnation. If it does so, the regime may remain stable for another one or two decades, but in the longer run it is almost definitely doomed. On the other hand, Kim Jong-un might decide to move his country toward market capitalism while maintaining a firm grip on power. There is some chance that he would succeed in this endeavour, making North Korea another ‘developmental dictatorship’ of the type we have seen so frequently in East Asia since 1945. However, it appears more likely that attempted reforms would merely speed up the regime’s demise.

Little is known now about the direction that Kim Jong-un will ultimately take, but recently emerging signs seemingly indicate that he is inclined to take the reformist path. Given his age and the challenges he faces, this might be a rational solution, but it remains highly risky. He might succeed indeed, but there is a significant possibility that he will fail in a dramatically spectacular way.

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Will sites of struggle become Cambodia’s sources of hope?

SARAH MILNE

At the beginning of this year it emerged that ANZ, Australia’s banking giant, had helped to finance a 20,000-hectare sugar plantation in Cambodia that involved military-backed land grabs, forced eviction of local farmers, food shortages and child labour, allegedly affecting more than 1000 families.

The agri-business project in question, led by a well-known and well-connected Cambodian tycoon and ruling party senator, is just one of hundreds of Economic Land Concessions that have transformed Cambodia’s countryside over the past decade. Such privately held concessions, for agriculture and mining, are now said to cover 22 per cent of Cambodia’s surface area. At first glance, the concessions appear to offer a much needed win-win for business and human development in one of Southeast Asia’s poorest countries: investors are virtually guaranteed double-digit growth rates; concessions are held in the long-term, on vast tracts of apparently empty state land; and local people are promised vital employment.

But this development vision is illusory, and even harbours the potential for political unrest, because it is built on the shaky foundation of contested resource ownership, or unresolved property rights.

For agri-business to take root in rural Cambodia’s patchwork landscapes, from which around 80 per cent of the population still derives its livelihood, a great deal of practical and discursive work is required. At a fundamental level, this entails the reorganisation and reworking of property, including clarification of its categories and forms, as well as its rules of access and ownership.

Inevitably, this task of property formation is contested and political in nature. Sprawled beyond the easily mapped paddy lands of Cambodia’s rice-belt is the other two-thirds of the country: a relatively sparsely populated and unruly landscape of savannah, flooded forest, mixed agriculture, fallow and jungle. This poorly understood expanse of ‘forested land’ is largely anthropogenic and has sustained Khmer and indigenous people for centuries, including through the upheavals of Cambodia’s 30-year civil war.

In this setting, customary property rights derive from traditional livelihood activities like shifting agriculture and the collection of non-timber forest products. But these rights are also infused with the complex and dynamic ‘property effects’ of Cambodia’s past, which involved massive human displacement, protracted territorial struggles and a radical socialist abolition of private property. How then does a nascent post-conflict state, seeking growth and stability, make sense of this melting pot of overlapping and
evolving resource claims?

Answering this question is not easy. There are multiple possible ‘right’ ways to approach it, each with its own complications.

Facing this challenge 20 years ago, Cambodia entered its post-conflict land reform process. A daunting range of actors, along with their ideas and agendas, were thrown into the mix: well-intended donors, the World Bank, NGOs, international advisors, and an array of variously motivated government officials including decision-makers, law-makers, map-makers, village chiefs and provincial governors. Most of these actors subscribed to the conventional logic that clear private property rights were essential for the efficient functioning of markets, and must therefore underpin Cambodia’s modernisation and economic development. Thus the ambitious multi-million-dollar Land Mapping and Administration Project was born in 2002. Hosted by the Ministry of Land Management Urban Planning and Construction, with lead roles being played by German advisors and the World Bank, this project initiated the massive task of systematic land titling for the millions of Cambodians whose land occupation and ownership was not officially registered.

As the land reform process unfolded, however, it became subject to political manipulation by the government and its increasingly self-confident rulers. For example, by 2007, it was clear that the land titling initiative had taken on a particular geography whereby some property claims were privileged over others, and the presence of ‘inconveniently’ located people was rendered invisible or simply overlooked in official map-making processes.

Thus, through partial and selective implementation, the titling program was used by the state to achieve its own more self-interested goals, namely legitimisation and reinforcement of the government’s hold over vast areas of valuable but as-yet-untitled land, including millions of hectares of forest estate, national parks and a range of urban slums.

By virtue of the classification ‘State Land’ these areas became available to investors and elites. Some acquired long-term concessions after paying handsome ‘fees’ to government and ruling party members; others, often government officials themselves, simply grabbed land because they had the power and connections to do so. This deft manoeuvring, conducted under the purview of international donors and advisors, highlights the predatory nature of Cambodia’s current regime. In particular, it shows how state power and authority have been used to facilitate the private accumulation of land and resources by elites.

The fundamental problem here is that the millions of hectares of Cambodian land now appropriated for private interests were not necessarily unoccupied or empty. Just as the peasants of Europe were dispossessed from their land to make way for the market economy, Cambodia is witnessing the alienation of tens of thousands of people from their land and livelihoods to make way for ‘development,’ often involving state-sanctioned violence.

Initially, villagers stood by in shock and fear as they lost their land and resources. But in recent years their responses have galvanised into resistance, giving rise to a looming political discontent that was reflected in the dramatic and still-unresolved national election results of July 2013—perhaps the greatest challenge yet to the ruling party.

Protests over land are now almost a daily occurrence. Some resistance efforts have garnered international attention, for example when indigenous villagers dressed up as ‘avatars’ in Phnom Penh. But most resistance is of the everyday kind: blocking off of provincial roads to create disturbance, delivery of thumb-printed letters to local government officials, formation of village networks to share information and defend land. These dynamics are the visible ‘edge’ of social change in Cambodia, and they will continue so long as the property contests remain unsolved.

Today, ANZ is learning the hard way about the violent and messy underpinnings of property in Cambodia. Donors have also suffered over land issues in recent years: both the Australian aid program and the World Bank have been accused of financing forced evictions through their provision of aid to the Cambodian government. Given this unpredictable environment, where outsiders tend to get their fingers burnt, how should international investors and donors proceed? So far, their actions have involved a fickle mixture of risk-aversion and public relations—strategies that ultimately reinforce the status quo in Cambodia. But what would happen if international leverage and resources were brought to bear differently, for example by nurturing local people’s desire for justice and change? This would be fiendishly complicated; but as a matter of moral obligation, it is well worth the risk.

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POST-WAR PROGRESS

Can Sri Lanka build a prosperous future?

ANUSHKA WIJESINHA

As you walk in to the arrivals area of the international airport at Katunayake, a large brightly lit billboard declares ‘Dream City, Happy Life!’ It is advertising Sri Lanka’s latest infrastructure and real estate project, the Colombo Port City. The billboard has an impressive digital drawing of this new city, and you could be fooled into thinking it was something coming up in Dubai or Qatar. At a recent investment forum held by the project’s promoters, local and international private-sector firms listened intently to the new investment opportunities arising from this US$1.4 billion project which will create, out of the sea, a new 229 hectare city. The ambition and optimism of this project reflect the wider sentiment about Sri Lanka’s economic prospects after the end of the war in May 2009.

After decades of low growth and stifled economic development because of the debilitating conflict, the Sri Lankan economy has demonstrated impressive post-war progress. 2010–13 GDP growth has averaged 7 per cent and is likely to exceed that in 2014. Poverty rates have fallen sharply (from around 20 per cent in 2000 to under 9 per cent in 2013) and greater price stability has been achieved (from inflation at over 20 per cent in 2008 to between 5–10 per cent in 2012 and 2013). Sri Lanka’s private sector is bullish, and has successfully tapped international capital markets with its sovereign bonds, at yields that would be the envy of many debt-ridden European countries.

Public infrastructure projects have occupied much of the attention of post-war economic planning, with several new projects—including two ports, an airport, a power plant, and three expressways—coming to fruition after years of delay.

As a small economy just getting back to vibrancy after being held back for decades, where is the financing for this impressive hardware push coming from? The answer: China, mostly.

Most projects have been fully or partially financed through Chinese government loans (and some by Chinese companies). China has now emerged as the number-one lender to Sri Lanka, accounting for as much as one-fourth of all donor commitments. The Chinese presence is also quickly moving beyond loans for development projects, with Chinese companies (typically state-owned ones) becoming the leading foreign investors recently.

The type of FDI Sri Lanka desperately needs is one that produces technology spillovers and links the country to new markets abroad.

Last year, China became the largest source of FDI into Sri Lanka. Political and business ties are increasing rapidly, and Sri Lanka is due to sign a free trade agreement (FTA) with China this year, although very little is known about its possible terms. Chinese state-linked companies are investing in hotels, a golf course, an iconic telecommunications tower, and mixed-purpose real estate developments. The Colombo Port City is the latest project, one for which the Chinese developer is getting a 25-year tax concession for developing waterfront real estate.

If there is one noticeable trend in Sri Lanka’s post-war FDI trend, it is that the majority of investments have been in projects related to real estate (including mixed-use property development) and tourism. In contrast, there has not been a substantial flow of FDI into industrial activities. More generally, too, manufacturing has taken a backseat in Sri Lanka’s recent economic performance. Much of it has stemmed from the growth in domestic non-tradables like construction and wholesale and retail trade, while manufacturing’s share of GDP has remained stagnant at around 17 per cent, and nearly 60 per cent of Sri Lanka’s GDP now comes from the services sector, especially the nascent IT and software services industry, which has expanded domestically and begun to win lucrative niches abroad. Between 2007 and 2013 exports tripled to US$600 million, and employment and the number of companies doubled.
In the manufacturing sector it appears that both domestic and foreign investors are unsure of Sri Lanka’s prospects. Although manufactured exports like apparel, rubber products and the like, have shown resilience and indeed made impressive global inroads through innovation and value addition, Sri Lanka’s middle-income transition is bringing up new challenges.

With rising wage and other input costs, Sri Lanka can no longer compete at the lower end of the spectrum. Yet it is also struggling to move higher up the spectrum, with limited capacity for innovation and upgrading technology. This is shown by the continued low investment in R&D (less than 0.2 per cent of GDP, and of that less than 10 per cent is by the private sector) and a very narrow talent pool of knowledge workers (less than 15 per cent of all state university graduates are in science and engineering, and only one in ten schools teaches high school science).

Education continues to be a critical constraint in Sri Lanka’s forward-and-upward march, particularly higher education. State institutions are unable to meet the demand (around 140,000 students who qualify to enter annually have to be shut out) and long- overdue reforms to permit private investment in higher education were introduced and then rolled back amidst political pressures from vested interest groups.

The type of FDI Sri Lanka desperately needs is one that produces technology spillovers and links the country to new markets abroad. And a broader talent pool with skills beyond basic education will be essential to Sri Lanka’s destination attractiveness.

Of course, skills will not be the sole determining factor. A consistent and favourable policy environment matters. While policies to ensure a stable and creditable macroeconomic performance post-war have been encouraging for investors, some policies on private-sector development have sent wrong signals and got investors worried. Examples include a controversial bill that expropriated 37 private enterprises (thinnily guised as an act to ‘revive underperforming and underutilized assets’); the forced closure and relocation of a high-performing rubber gloves exporter’s factory (owned by a leading blue-chip company) due to misplaced public protests and a misguided government response to it; ongoing moves to ban the sale of land to foreign ownership; and the imposition of very high tax requirements on foreigners leasing land, creating significant disincentives for foreign investment.

Amidst all of this, Sri Lanka’s transition from low income to lower-middle and subsequently upper-middle income (government projects GDP per capita exceeding US$4000 by 2016) is bringing with it new challenges that aren’t easily addressed.

The aspirations of Sri Lanka’s people are changing, and catering to those desires, particularly in the growing urban class, will be a key medium-term economic and political challenge for the government. In the south, attitudes towards types of jobs are changing. The continued growth of migrant worker remittances is putting cash into the hands of people at the lowest social level and, along with a fall in import duties, has resulted in a rise in ownership of consumer durables like TVs and refrigerators. In the conflict-affected north and east, basic needs are fast being fulfilled—like reconstruction of roads and bridges, expanded electricity access to homes, and kids getting back to steady schooling.

As these needs are met, people’s aspirations of greater political rights and freedoms and the desire to determine their own development path not imposed by the centre will come strongly to the fore. The rejection of the ruling UPFA and resounding victory of the Tamil National Alliance in the recent Northern Provincial Council elections is one manifestation of this. The next round of provincial council elections, set for late March 2014, is likely to be a test bed for the ruling party before it calls national elections well ahead of schedule.

Beyond this, however, two major imperatives are likely to continue to occupy the attention of Sri Lanka’s highest decision-makers. On the one hand, a ruthless focus on consolidating power at the centre, navigating growing international pressures on human rights issues, and preserving post-war popularity among the government’s primary vote base—the Sinhala Buddhist majority; on the other hand, delivering the promised high post-war economic growth, undertaking critical growth-boosting reforms, and meeting the fast-evolving socioeconomic aspirations of people across the country. Whether the relentless preoccupation with the former will distract effort from the latter will be a critical determinant of whether Sri Lanka builds on the post-war gains and transitions towards a prosperous future.

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Bhutan is famously known for the unique approach it has taken to measuring its population’s overall wellbeing. ‘Gross national happiness’ (GNH) is a set of criteria that considers sustainable development, support of cultural values, environmental conservation and good governance to offer a nuanced index through which the country judges its success. In recent years GNH has captured the imagination of other bodies seeking to offer positive developmental goals. In 2011, for example, 68 countries endorsed a move by the UN General Assembly to adopt Bhutan’s holistic approach to development.

But the four measures that comprise GNH, while laudable, fail to capture one important element that affects a nation’s residents, and one that is quite relevant for Bhutan: the equal treatment of minority populations. What is less well known is that the GNH narrative has masked a dark chapter of Bhutan’s recent history, a chapter that continues to bedevil a significant portion of the population today. Bhutan’s ethnic minorities have suffered profound mistreatment. While this article focuses on the Nepali-Bhutanese, or Lhotshampa, other groups, particularly the Sharchops, have been equally if not more mistreated.

Differences in religion, language and ethnicity are one aspect of the Nepali-Bhutanese issue. The Ngalong, the minority ruling class in Bhutan, are Buddhist and speak Dzongkha, while the Nepali-Bhutanese, who have traditionally resided in the lowlands of southern Bhutan, are primarily Hindu and speak Nepali.

These ethno-religious differences, extant for decades, were highlighted by the Bhutanese government’s growing fears in the 1970s and 1980s that the separatist movements in nearby regions (such as calls for an independent Ghorkaland in an area that included Sikkim, parts of Bhutan, West Bengal and eastern Nepal) would manifest in Bhutan. As a consequence, policies singling out ‘the other’ within Bhutan became oppressive. For example, a centuries-old code of conduct called Driglam Namzha, originally meant to offer guidance on dress and etiquette, was reinterpreted in ways that restricted the language and customs of Nepali-Bhutanese.

By the late 1980s discrimination against the Nepali-Bhutanese took several forms. First, in addition to continuing cultural and linguistic...
discrimination, the jobs and landholdings of many Nepali-Bhutanese were taken away. Second, in 1988, a first-of-its-kind census, applied strictly only in the south where Nepali-Bhutanese primarily lived, divided the population, including units of individual families, into different categories of genuine citizens and non-citizens. Finally, beginning in 1989 and continuing through the early 1990s, tens of thousands of Nepali-Bhutanese had their documentation (land certificates, voting records and the like) taken away and left the country. They crossed through India and into Nepal, where between 80,000 and 100,000 lived for more than two decades in refugee camps.

BHUTAN’s position is that the Nepali-Bhutanese left willingly, and Bhutanese officials at the time even required those leaving the country to sign forms indicating the voluntary nature of their departure. Nepali-Bhutanese were additionally asked to ‘show their teeth’ in photographs as a way of showing that they were happy to leave.

Yet the stories of those who lived in refugee camps in Nepal belie this narrative, and they speak to a damning expulsion of up to one-sixth of the country’s population. One example of the yearning of Nepali-Bhutanese to return is that even the most vociferous exiled groups for many years sent happy birthday messages to Bhutan’s king and asked for the chance to return home.

Today, Bhutan estimates that 25 per cent of its population is Nepali-Bhutanese. Many live in southern Bhutan and remain in what has been called a ‘liminal legal space’, fearful of losing their jobs, afraid to promote their rights, suspicious of local leaders, and ever wary of having their status revoked. There is little triangulated information about this remaining population because the media do not cover the issue and international visitors to the region are highly restricted. Most information that does exist comes from those who have left. And those Nepali-Bhutanese who now live abroad say that relatives who remain within Bhutan will not discuss these issues by email or telephone for fear of retribution.

What hope exists for the Nepali-Bhutanese? Will those in the country begin to enjoy political representation, freedom of speech and security of status? Will those out of the country have the chance to return? Two things have changed in recent years that could signal the possibility of reform.

First, Bhutan is an emerging democracy. The Fourth King, Jigme Singye Wangchuck, administered structural changes to Bhutan’s laws that officially removed his absolute power as monarch and paved the way for a democratic constitution and elections, which occurred for the first time at the parliamentary level in 2007–08 and at the local level in 2011. Second, the exiled Nepali-Bhutanese, after spending more than two decades in refugee camps in eastern Nepal, have since 2009 been permitted to resettle—that is, to move permanently to some developed countries which offer citizenship to selected refugee populations. To date, approximately 80,000 Nepali-Bhutanese have moved to resettlement countries such as the United States and Australia, where over time they may be able to make use of access to international power-holders, education and media resources to leverage rights claims concerning the Nepali-Bhutanese issue.

So far, however, no change in Bhutan has been forthcoming.

Neither national nor local elections have produced candidates willing to take up the Nepali-Bhutanese issue (despite the election of some Nepali-Bhutanese), and it is a taboo topic in the public domain. Lily Wangchuk, the president of Bhutan’s Druk Chirwang Tshogpa party and a social activist, has noted that formalised structures for public debate have not yet filtered down to the informal realm. This, of course, is where honest discussions about the Nepali–Bhutanese may begin to take shape at some point, but certainly not yet.

AND while the Nepali-Bhutanese diaspora in resettlement countries has increased exponentially in recent years, its members are too young to maintain a sole focus on reforms in Bhutan. Websites intended to reach out to Nepali-Bhutanese worldwide currently emphasise resettlement issues, rather than Bhutanese politics. To date, not one Nepali-Bhutanese has been permitted to return to Bhutan.

Many commentators have noted that Bhutan is at the start of a long path towards democracy. It is too early to predict if that path, even if straight and smooth, will permit a space for reflections on the wrongs done to Nepali-Bhutanese and other ethnic minorities and, even more importantly, ways to remedy them. In the short term, it’s worth noting that in the past year the narrative of GNH has taken a back seat to other pressing domestic issues, such as unemployment and corruption. But the issue of ethnic minority treatment is not even on the horizon.

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ON THE FENCE

A view from the India-Bangladesh border

JASON CONS

On 18 December 2013, the Indian National Congress party government introduced a bill in parliament to facilitate the realisation of the 1974 Land Boundary Agreement with Bangladesh. This bill was the latest in a long series of attempts to enable the exchange of 161 enclaves—tiny pieces of Indian territory completely bounded by Bangladesh and vice-versa—by absorbing them into their bounding states.

Residents of these enclaves face an absurd territorial dilemma, where to effectively exercise their rights as citizens they must illegally cross two borders. Yet enclave exchange has proved a persistent and proverbial fly in the ointment of India–Bangladesh relations. Even the bill’s introduction was heatedly contested, with members of a range of opposition parties raising vociferous protests calling the bill a ‘Bangladesh giveaway’.

What are we to make of such protests? And what do they tell us about the India–Bangladesh border more generally?

The Land Boundary Agreement’s controversy hinges on both local and national disputes over the meaning of the border and its broader relationship to nationalist politics. Indeed, such struggles offer clues to the politics of postcolonial territory that haunt discussions of Bangladesh and its future in both countries.

India’s border with Bangladesh (formerly East Pakistan) has been a locus of contention since 1947. Hastily and haphazardly demarcated, the line dividing Bengal occasioned massive migration and violent dislocation of both Hindus fleeing the newly formed East Pakistan for India and Muslims moving in the opposite direction.

Since Partition the border has in practice gradually been worked out, formalised, and ossified into a highly securitised political boundary. The border itself is a communal marker—the nominal division of a Muslim majority population from a Hindu majority one. And, indeed, that religious divide continues to dominate much debate over border politics.

Communal division is salient in discussions of migration and the steady illegal flow of people and goods across the border (in both directions). While an ongoing political debate continues between the two states over the scale of migration, the reality and imagination of (Muslim) Bangladeshis entering India on a permanent or temporary basis has long been a central lever in nationalist politics within India.

Another key issue is the spectre of violence at the border, particularly the debates over the regular exercising of lethal force by India’s Border Security Forces (BSF) on peasants and ‘smugglers’ crossing it. Between 2007 and 2010, Human Rights Watch found that there were at least 315 Bangladeshi nationals reported killed by the BSF. As geographer Reece Jones persuasively argues, the BSF exercises a de facto right to carry out lethal justice, a reality that has made reporting on border shootings by the Bangladeshi media so regular as to have become banal.

An even more visibly present marker of this communal divide is the 3300-km floodlit border fence erected by India and surrounding much of Bangladesh. The fence has become a site of often graphic displays of violence. A troubling case-in-point is the 2011 shooting of Felani Khatun, a 15-year-old girl shot while crossing from India into Bangladesh and left to die, tangled in the barbed wire atop the fence. In Bangladesh, photos of Felani’s hanging body became a potent marker of lethal border security. Its iniquities were further highlighted by the acquittal of the BSF officers charged with her death by an Indian court in 2013.

While the border thus dramatises the Partition’s unfinished business—the incomplete communal division...
of Bengal—it would be a mistake to imagine that its politics are only influenced by communal debates and religious nationalism. The fence also lays bare complex questions related to climate change—particularly the expectation that ecological transformation in the deltaic state will directly produce countless so-called climate refugees in the coming years.

Indeed, a number of recent commentators have claimed that the India–Bangladesh border offers a preview of the ways that climate transformation is likely to effect political boundaries in the rest of the world. Such arguments oversimplify the complex politics of migration and ecology at the border, but highlight the sensitive nature of border securitisation in Bengal.

It is also important to note that the border, and the bilateral relationship, is far from static. Indeed, particularly since the restoration of democracy in Bangladesh in 1991 with the ousting of General Mohammed Ershad from power, tensions along the border have dynamically fluctuated with elections in both states.

The border, as residents report, is markedly less tense when the nominally secular Awami League is in power in Bangladesh and the Congress party is in power in India. Indeed, many critics of the Land Boundary Agreement bill saw its introduction as a Congress party attempt to provide support to Sheikh Hasina’s Awami League government in Bangladesh’s January elections.

In the summer of 2013, residents of a border enclave in Northern Bangladesh described to me the ways in which local border economies are intimately tied to such shifts. As they told it, a profitable boom in feed corn production in the enclave was, in fact, underwritten by cartels who had secured capital through cattle smuggling in the more relaxed border climate following the Awami League’s 2008 return to power.

Such fluctuations mark life in the borderland, on both sides of the fence, with uncertainty. Moreover, they raise questions about what might happen to...
border life should Narendra Modi and the Hindu-right BJP ride the wave of Gujarat’s economic miracle to power in India in 2014.

Given all this, it is not hard to see why so many policy initiatives to address border complications fail, or to see why the exchange of tiny amounts of territory should prove such a fraught and intractable proposition.

The fate of the latest attempt to realise the Land Boundary Agreement remains unclear, though a short survey of border history leaves one sceptical about its prospects. The Agreement, and its 40-year history, are about much more than just the enclaves and their residents. They take on symbolic dimensions, coming to represent both unfinished pasts and uncertain futures. The dramas of such legislative initiatives obscure the real costs of repeated political failure—the ongoing uncertainty and anxiety of life for residents who must navigate the dangerous complexities of the border on a daily basis.

FOR MORE than two decades Sheikh Hasina of the Awami League (AL) and Khaleda Zia of the Bangladesh Nationalist Party (BNP) have ruled Bangladesh. They hate each other viscerally and refuse to communicate, much less negotiate. Both women inherited their political followings from relatives who were assassinated. They have since turned the country’s two largest parties into patronage-based personality cults that specialise in looking backwards.

Bangladesh is the world’s eighth most populous country. It has made tremendous progress in recent years—very much despite its appalling leaders. Their greatest feat might have been when they joined hands in 1990 to oust Mohammad Ershad, a dictator. Ever since, the two autocratically inclined ‘begums’ have given Bangladesh no choice but the choice between the two of them.

The incumbent prime minister has always lost—until now. But now Bangladesh is entering a new phase. In a farce of an election on 5 January Sheikh Hasina won a second consecutive term as prime minister. She laid the ground for this victory in 2011 by junking a provision added to the constitution in 1996 which had called for neutral, ‘caretaker’ governments to oversee elections.

So Zia’s BNP, sitting in opposition, boycotted the poll. They might or might not have won a fair election, had they contested. In either case they convinced a majority of Bangladeshis that the election would be unfair without a caretaker to supervise it. For the 20 million-odd voters who showed up (out of 92 million eligible) the choice was even more limited than usual: the only candidates were either in the ruling party or beholden to it. In the majority of seats no voting took place at all. There is a big difference between two lousy candidates and just one.

Nor was the boycott the only problem. Before the polling, the government had put Zia under house arrest. Ershad, who now leads the country’s third-largest party, was held at an army hospital. The next-biggest party, the Jamaat-e-Islami, had been banned from taking part on the ground that its overtly Islamic charter is in breach of Bangladesh’s secular constitution.

On the world stage Sheikh Hasina has joined a short list of leaders who have been elected technically but without an electoral mandate. Like the rest, she has silenced critics in the media, captured the courts and
ensured that only her supporters are entitled to a fair hearing. Her government has branded the opposition, the BNP and its Islamist allies as ‘terrorists’. Among the first to congratulate her were China, Russia, Myanmar, Cambodia and Belarus. But India has also sent its best wishes. It has come to favour Sheikh Hasina in recent years.

America has called for fresh and credible polls within six months. The European Union is less impatient. But it is wishful thinking anyway and everybody knows it. Foreign powers are loath to cut foreign aid or the trade that underpins the country’s booming garment sector. The UN does not want to risk losing access to Bangladesh’s bountiful blue-helmeted peacekeepers. The only thing that could bring real pressure to the ruling elite—a ban on their travel privileges—is no more likely than fresh elections.

Bringing the begums to the negotiating table looks even trickier than forging peace with the Taliban. In Afghanistan the late Richard Holbrooke was said to have drawn Venn diagrams to illustrate how much the opposing sides had in common. On his way to China Nixon asked, ‘What do they want, what do we want, what do we both want?’ The problem in Bangladesh is that the sets of its Venn diagram are mutually exclusive. The only thing both sides want is for the other not to rule.

It would not be fair to pin all the blame on Sheikh Hasina. Khaleda Zia chose the road that undid her. While the Western powers and 80 per cent of Bangladesh’s population agreed that Zia should have the fair elections she was demanding, she went further and set the course for deadly street violence and crippling hartals (labour strikes). The BNP is now in disarray and has no better option than to wait out Sheikh Hasina’s new government, hoping they bring about their own downfall.

If voting were fair and mandatory, the AL would probably win every time; but it enjoys a popularity that does not always translate into turnout, much like the Democrats in America. And the next time Bangladeshis pick their government the League will almost certainly lose. It is now setting the standards by which it will be treated when the BNP come back to power. In 2013, 500 or so people were killed in political clashes, one of the most violent years since independence.

Bangladesh is uniquely imperiled by climate change. One half of its 160 million citizens live on a delta close to sea level. By the middle of the century a country the size of the American state of Iowa will be home to as many people as live in Brazil today. It would be a miracle if its battling, small-minded politicians were to adopt policies capable of bringing the population to live together, in peace, behind the dykes—that are yet to be built.

Tom Felix Joehnk writes for The Economist.
Pakistan struggles to make its way out of the abyss

ALICIA MOLLAUN

Pakistan is wracked by economic instability and security problems that affect the life of every citizen. These interlinked problems are eating away at the Pakistani state and, if left untreated, they will create more instability, which is good neither for Pakistan, the region, nor the rest of the world.

While some argue that Pakistan is simply ‘muddling through’ its multitude of political, security, economic, and social crises, alarmists talk of Pakistan’s impending ‘state failure’ or a return to military dictatorship.

In 2013, Pakistan ranked 13th on the Fund for Peace’s (FFP) annual Failed States Index—most of its indicators having worsened or remained constant. The FFP categorises Pakistan as a ‘high alert’ country, in the same company as Iraq and Afghanistan. Pakistan fares particularly poorly when it comes to ‘group grievance’ (ethnic and sectarian violence), ‘security apparatus’ (militancy, military coups, bombings), and ‘external intervention’ (this includes the presence of foreign aid and peacekeepers).

Pakistan’s democracy is weak, in part because the military has deprived Pakistani citizens of the opportunity to participate in a democratic society. Throughout its 66-year history, Pakistan has oscillated between military rule and civilian government. General Ayub Khan seized power in 1958, only 11 years after Pakistan’s independence, and to date Pakistan has been ruled by the military for almost half of its existence. This political environment has allowed either civilian autocracy or military rule to flourish. Elections in 2013 were notable because—for the first time in Pakistan’s history—a democratically elected government replaced another after the Pakistan People’s Party, headed by President Asif Ali Zardari, became the first government in the nation’s history to complete a full term.

Elections were a positive step, but is Pakistan’s democratic path sustainable? It may slide back towards civilian autocracy or military rule. Much of this depends on the current government, led by Prime Minister Nawaz Sharif, and its ability to arrest growing insecurity and economic malaise—two factors that heavily influence state stability. Given that he has been prime minister twice before, Sharif has a better shot than most, even though both of his previous governments ended at the hands of the military: his second ousting was at the hands of Pervez Musharraf in 1999.

After winning the election Sharif pledged to improve the security situation in Pakistan, but after almost a year little progress has been made. Thus far, the government has been unable to translate its security policy rhetoric into results on the ground. The security forces, including the police, lack the capacity (and at times the willingness) to uniformly enforce the law across the country. Nowhere is
Insecurity affects the life of every citizen. In a 2013 Pew survey of Pakistani public opinion, 99 per cent of respondents believed that levels of crime were a serious cause for concern, while 98 per cent agreed that terrorism was a serious problem. In the tribal areas, regular terrorist attacks are part of the fabric of everyday life. In the period 2009–12, 16,494 people were killed in terrorist-related violence in the Federally Administered Tribal Areas alone. Poor witness protection, flawed crime-scene management and weak investigative skills lead to extremely low prosecution rates. In 2012, conviction rates in anti-terrorist courts in Sindh were an abysmal 26 per cent. In Karachi, home to over 22 million people, the Taliban are taking over large parts of the city. Those who can afford the expense hire private security guards and live in fortified compounds, or simply emigrate to start a new life.

Even the security establishment is not immune to terrorism. On 20 January 2014 the Pakistani Taliban bombed Rawalpindi’s Royal Artillery Bazaar close to the army’s General Headquarters, in retaliation for the army’s operation at the Lal Masjid in 2007.

Residents in the capital, Islamabad, simply make allowances in their daily routines for the inconvenience caused by police checkpoints, road closures for VIP motorcades and the disruption of cell phone services to prevent terrorist attacks.

What happens in Afghanistan in 2014 with the withdrawal of US combat forces is also of critical importance to Pakistan’s and the region’s stability. The Obama administration frequently says that it wants nothing more than a ‘stable, secure and prosperous Pakistan’.

As well as security problems, economic instability is a major cause of concern in Pakistan. Roughly eight in ten Pakistanis describe the economic situation as bad. While the cornerstone of Sharif’s election platform was the economy, few concrete policies have been implemented to spur economic growth.

A key factor hampering growth and economic stabilisation is the energy crisis, which routinely deprives the majority of Pakistanis of electrical power. Some areas in the Punjab, Pakistan’s most populous state, only have power for as little as four hours per day. Business is the big loser from Pakistan’s energy woes. Textile production has plummeted, with the industry as a whole registering losses of around 200 billion rupees (US$1.9 billion) over the past four years. One of the hardest hit industries is fertiliser production. Pakistan has the capacity to produce more than one million tonnes in exportable surplus urea, but in 2011–12 it imported over 1.1 million tonnes. This has balance of payment implications, as well as negative consequences for foreign exchange reserves and the budget.

In the short to medium term, it is the economy that will either push Pakistan further into the abyss or nudge it towards opportunity. Pakistan has great potential. Its demographics are favourable to economic growth, with 66 per cent of the population under 30. Job creation will be essential to encourage new entrants into the workforce. Investment, both domestic and foreign, must also be reinvigorated.

Sharif has a tough job ahead. A multitude of policy failings by the previous government, in areas as diverse as education and regulation, means there is a real danger that a holistic approach to reform will be placed in the ‘too hard basket’. Failures in governance, failure to implement policy legislated by the parliament and a failure to prioritise real reform has perpetuated chronic underdevelopment and worsened deep inequalities within Pakistani society.

It will be a huge challenge for Sharif to lead his country out of the economic and security quagmire in which it is now stuck. In the short to medium term, Pakistan has a real opportunity to get back on track through taking tough measures to address its economic slide and, in particular, by taking tough measures to improve security. It will require real leadership by the Pakistani government and military to ensure that Pakistan does not continue to muddle through—or become a failed state.

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Harnessing economic potential in India's northeast

DUNCAN MCDUIE-RA

NORTH EAST India is increasingly being viewed as a key region for private investment. More than 90 per cent of the area is bordered by other countries, including Bangladesh, Bhutan, Burma, China and Nepal. There are eight federal states in the northeast, as well as a number of autonomous territories.

The region is characterised by poverty rates well above the national average, by insurgency and counterinsurgency action, by exceptional laws and constitutional provisions, and often-opaque governance structures. For this reason, private investment and the rhetoric and policy surrounding it may seem a minor concern. However, private investment reveals a great deal about India’s northeast frontier—and local and national attempts to benefit from its location on the edge of South Asia.

Private investment seeks to harness the economic potential of the northeast. Unlike other parts of India where land, coasts, rivers and forests have been exploited, the northeast is imagined as almost virginal: a place full of valuable resources that local people cannot, or will not, utilise. The potential for profits is concentrated in extractive industries and, somewhat contradictorily, ecology and biodiversity.

The industrial policies of the federal states in the region illustrate this perceived potential. The Arunachal Pradesh State Industrial Policy 2008 notes that ‘at present, the industrial growth in the State is dismal and at a nascent stage despite enormous potential’. A key objective of the Industrial Policy of Nagaland is to create ‘conditions for rapid industrial development and [a] conducive investment climate’ that would help to ‘accelerate exploration of mines and minerals for enhancing the resource base of the State’ and strengthen the organic agriculture, handicrafts and tourism sectors. Other federal states have followed suit, and outside attention is growing.

The region’s proximity to China and Southeast Asia frequently prompts discussion of its potential for investment. That potential is elaborated in the flagship North Eastern Region Vision 2020 (NEV2020) policy document written by the Ministry of Development of North Eastern Region and released in 2008. The report refers to ‘underdevelopment’ as the region’s ‘economic imprisonment’, and argues that to alleviate poverty in the region

### FRONTIER INVESTMENT

**Harnessing economic potential in India’s northeast**

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**Picture:** NARINDER NANU / AFP PHOTO / AAP
a ‘paradigm shift in development strategy’ is needed to allow ‘people-centric programmes based on harnessing the natural resources of the region’. NEV2020 posits that investment will create opportunities, opportunities will create jobs, and jobs will cultivate a peaceful region.

The region is also seen as an emerging, if challenging, consumer market. Growing incomes from decades of reservations in the bureaucracy for members of tribal communities under the Sixth Schedule of the constitution, bureaucratic expansion and patronage politics, along with the growth in remittances to the region by family members working in Indian cities, have expanded the consumer base. Mobile telephone and internet providers are well established, and the automobile, retail, hospitality, airline and information technology industries continue to eye the region. As a market for consumer items, the northeast is India’s last domestic market to ‘crack’, as it were.

Despite this potential, attracting private investment to the region has proven difficult. The North East Industrial and Investment Promotion Policy 2007 (NEIIPP), a 2007 to 2017 federal government initiative, has transformed the entire northeast into a special economic zone. It provides major incentives (mostly over a 10-year period) for new investments and for the expansion of existing investments. These incentives include 100 per cent tax exemption, 100 per cent duty exemption, capital subsidies of up to 30 per cent, interest rate caps on loans, insurance reimbursements (a major incentive in the unstable northeast), and special incentives for the services sector, biotechnology and power generation.

Finance is coordinated by the North Eastern Development Finance Corporation Ltd, a state-owned corporation that provides finance for firms seeking to avail the benefits of the NEIIPP, and which has showcased ‘success stories’ from the first five years of the policy in its half-term report. The success stories reflect fairly modest ventures and showcase individual entrepreneurship: a silk factory in Assam, a compost facility in Meghalaya, a bakery in Mizoram. The massive projects that are coveted by proponents of private investment, and feared by critics, do not feature.

There are two reasons for this. First, uptake of the NEIIPP has been poor. Massive privately funded projects are not being profiled because there are not many. Despite generous incentives the policy has had a limited impact. Secondly, most large-scale projects in the region are overwhelmingly funded and operated by state agencies, such as the Oil and Natural Gas Corporation (a group of companies in which the Indian government has a 69.23 per cent stake), the Uranium Corporation of India Ltd, and the North Eastern Electric Power Corporation Ltd, though often in partnership with private investors.

In addition to national agencies, the governments of the region’s federal states continue to seek private investment, even with limited prospects of success. For elites in the northeast, both inside and outside the formal political system, showing willingness and openness to private capital can increase the possibility of government subsidies and incentives. Actually implementing the promised investment is another matter, however.

Certainly different states within the region hold different prospects for private investment. A 2013 report by the Indian Chamber of Commerce and PricewaterhouseCoopers, titled *India’s North-East: Diversifying Growth Opportunities*, reflects the usual aspirational sentiments: ‘as multiple avenues for growth and development emerge, it is of paramount importance that the region, as a collective identity, embarks on a vibrant journey to realise the dreams of a better future’. However, the report also attempts to differentiate investment potential within the region, commenting that ‘all the eight states have different developmental prospects and resources to support their efforts in contributing to the regional as well as national economy’. States are compared based on their level of forest cover (the less the better), fertiliser use (the more the better), agricultural productivity, the length and type of roads, power-generating capacity, and education levels, suggesting a region-wide approach may not be feasible when seeking to attract private investment.

**Peace**, or the prospect of peace, is another important way of differentiating between states. Thus Arunachal Pradesh, Mizoram and Sikkim have pushed their own prospects and sought to distance themselves from Manipur, Nagaland and Assam. But while instability might affect private investment in a food-processing plant or hospitality-training college, it does little to dissuade public investment in oil, gas, hydropower or uranium—industries that have shown limited capacity or willingness to lift communities in the region out of poverty.

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Lao dam schemes challenge regional cooperation

SARINDA SINGH

THE construction of Don Sahong dam on the Mekong River in southern Laos is provoking a great deal of international criticism, especially for a dam with a relatively small generating capacity of 260 megawatts.

Tensions over the project are partly the result of competing development objectives among Mekong countries for shared natural resources in the Mekong Basin. But they also reflect the weakness of regional governance forums like the Mekong River Commission (MRC). The widespread public censure that Laos’ dam-building ambitions have attracted signals a distinct shift in regional politics that is only likely to intensify in coming years.

Perhaps the only undisputed issue in current debates is the tremendous socio-economic and environmental value of the Mekong River. This river system sustains the world’s largest inland fishery, providing crucial support for the livelihoods and food security of an estimated 60 million people, many of whom are the region’s poorest.

The Mekong River also boasts remarkable biodiversity, with almost 1000 fish species—second in diversity worldwide only to the Amazon River—as well as harbouring endangered species like the Mekong Irrawaddy Dolphin and Giant Catfish. About 70 per cent of the Mekong River’s fish species are migratory—an unusual characteristic that is due to the river’s massive seasonal variation in water volumes. So despite the appeal of Mekong River dams for developing countries like Laos, they have raised significant concerns because of their huge social and environmental impacts, and their challenges to regional cooperation.

The MRC has long promoted the goals of sustainable development, poverty alleviation and cooperative management of the Mekong River. The commission is a consultative intergovernmental body that works with the countries of the lower Mekong—Cambodia, Laos, Thailand and Vietnam—though it is funded by a number of international donors. Yet recent events in Laos and elsewhere suggest that none of its admirable goals are being advanced.

By virtue of geography, Laos has abundant hydropower potential. The 1880-kilometre stretch of the Mekong River within Laos represents over a third of water flow in the Mekong Basin. Laos currently has the most planned dams along the lower Mekong (12 in total), and the Lao government regularly promotes its vision of becoming the ‘battery of Southeast Asia’. Hydropower is touted as a way of earning foreign revenue, funding poverty alleviation programs and enabling Laos to exit least-developed country status—goals which are seeing recent progress.

However, since the 1980s there has been increasing international recognition of the negative impacts of dams. Trans-boundary impacts, which can result in a highly uneven distribution of costs and benefits between neighbouring countries, are especially contentious.

In the case of the Mekong River, Laos’ enthusiasm for hydropower has prompted other countries of the lower Mekong Basin, which usually favour quiet diplomacy, to express unusually forthright public criticism.

Two dams are especially controversial because they are the first on the Mekong main stream that trigger requirements for ‘prior consultation’ with other MRC member countries under the 1995 Mekong Treaty. First, in late 2012, the Lao government approved Xayaburi—a huge US$3.5 billion, 1260-megawatt project in northern Laos being built by Thailand’s Ch. Karnchang PCL. This approval reversed previous suspensions of the project, but it failed to address concerns raised by...
other MRC member countries over flaws in the consultation and impact-assessment processes.

More recently, the Lao government’s approval of the Don Sahong hydropower project is also facing mounting objections. Though much smaller in size to Xayaburi, critics have highlighted that Don Sahong will block a channel that is crucial for dry-season fish migration on the Mekong River, and that mitigation measures proposed by the developer (Malaysia’s Mega First Corporation Bhd) are untested and likely to fail. The developer’s environmental impact assessment also failed to consider the impact on regional fisheries, despite Don Sahong’s two-kilometre proximity to the Cambodian border.

In late 2013, the Lao government also unilaterally re-classified Don Sahong as no longer a mainstream dam, so that less-stringent conditions for ‘notification’ of other lower Mekong countries would apply instead of ‘prior consultation.’ This decision has attracted widespread censure. A special meeting of the MRC Joint Committee held in Vientiane in January 2014 failed to resolve the issue, with member countries only agreeing to refer it to a later meeting of the MRC Council.

Most observers doubt that a MRC-led resolution will result in a meaningful reconsideration of Don Sahong. The MRC has so far not censured the Lao government for its violations of the MRC Treaty over both Xayaburi and Don Sahong. Such persistent inaction supports the increasingly common view of the MRC as unassertive and ineffective. The MRC’s diplomatic reticence stands in stark contrast to the increasing assertiveness of countries with untapped hydropower potential—including, increasingly, China.

While the MRC is not a regulatory body, its emphasis on diplomacy above all other measures calls into question its reason for existence. Sustainable development and regional cooperation of the Mekong River are admittedly challenging goals, but without a strong champion of good governance, critics are right to be alarmed over a future where sustainable hydropower in the Mekong appears to be a vanishing possibility.

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After the USSR collapsed in 1991, the energy potential of Central Asia—especially the hydrocarbon reserves in the Caspian Sea basin—generated much excitement in the West. In 1994 former US Secretary of State James Baker famously proclaimed that ‘Caspian oil may eventually be as important to the industrialised world as Middle East oil is today’.

However, the fanciful predictions of 200 or even 720 billion barrels (bb) of crude oil eventually gave way to more realistic estimates. The 2013 BP Statistical Review of World Energy sets the figure at around 38 bb in proved reserves, which is a far cry from the Persian Gulf’s 798 bb. Kazakhstan has the region’s greatest oil endowment, with reserves of 30 bb.

Central Asia’s share of the world’s reserves of natural gas is somewhat higher at 11 per cent; still, it falls short of the Middle East’s share, 43 per cent. Turkmenistan possesses 17.5 trillion cubic metres (tcm) of this commodity, followed by Kazakhstan and Uzbekistan with 1.3 and 1.1 tcm respectively.

While Kazakhstan and Turkmenistan will not and could not become swing producers on a par with Saudi Arabia and Qatar, with a global outreach and significant influence on international energy security, they are rich countries craving the role of reliable providers of hydrocarbons to the market. Maximising the benefits from resource politics requires creative and balanced engagement by Central Asian leaders with internal and external stakeholders.

The energy sectors in Kazakhstan and Turkmenistan have played a critical role in attaining high rates of economic growth after 2000. Hydrocarbon rents have also enabled the authoritarian regimes in Central Asia to provide the welfare services that ensure their populations’ acquiescence in their government.

In 2013 the oil sector in Kazakhstan generated a quarter of GDP, 65 per cent of the total exports, and 40 per cent of budget revenues. Natural gas constituted 90 per cent of Turkmenistan’s exports, and the petrochemical industry as a whole accounted for half of the country’s GDP. The sustainability of this model of development may be eroded by the common problems of effective investment, resource depletion and social dislocation.

Kazakhstan appears to be better prepared to tackle these challenges. Its long-serving president, Nursultan Nazarbaev, has consistently pursued an open-door policy towards foreign energy companies. Kazakhstan has attracted more foreign investment per capita than any other Commonwealth of Independent States country since 1991, with 89 per cent of the funds going to the oil and gas sector. Western, Russian, Middle Eastern, Chinese and Indian corporations are all present in Kazakhstan; they balance each other out so that no one foreign actor has too much influence over the Kazakh oil sector.

The flow of money did not dry up even after the authorities engaged in resource nationalism and tightened control and regulation of the energy sector in 2007. In 2012, the government launched an unprecedented ‘People’s IPO’ program, selling stakes in energy assets to domestic investors. The expectation is that half a million of Kazakhstan’s 16.7 million citizens will acquire equity in the oil and gas sector over the next five years.

Diversification away from oil and gas dependency is already a high priority for Kazakhstan’s government. In January 2014, Nazarbaev outlined an ambitious program, ‘Kazakhstan-2050’, which set the objective of moving the country into the top-30 most-developed nations in the world. The hydrocarbon sector, and particularly the national sovereign wealth fund, are to act as the source of financing to modernise and radically improve the quality of life.

Labour unrest has been gaining momentum in Kazakhstan’s oil and gas industry since the 2000s, fuelled by poor working conditions and...
inequality in pay between local and expatriate staff. In December 2011, a strike in Zhanaozen culminated in a riot and substantial loss of life. The incident led to two major welfare initiatives in 2012, yet according to many observers at home and abroad, industrial relations in the sector remain ripe for reform.

Unlike Kazakhstan, Turkmenistan has not undergone a fundamental market transition after independence. It has remained a paternalist state that provides the population with basic consumer goods and utilities on a free or highly subsidised basis. The hydrocarbon sector is tightly controlled by the government and remains non-transparent; the investment climate is difficult.

The change of guard from the first president, Saparmurat Niyazov, who died in 2006, to Gurbanguly Berdymuhammedov did not bring any liberalisation. The regime continued to pour petrodollars into extravagant high-visibility projects at the expense to pour petrodollars into extravagant liberalisation. The regime continued to build elite, frequent purges, and a constant rotation of the executive personnel in the energy sector.

Diversifying export routes and obtaining the best purchase price in the international market have been top priorities in Kazakhstan’s and Turkmenistan’s foreign policies.

Kazakhstan has multiple pipelines delivering its oil to end users in Europe, Russia and China. Italy, The Netherlands, France and Austria bought 56 per cent of Kazakhstani oil in 2012, while China accounted for 16 per cent. The existing transport infrastructure has enough flexibility and spare capacity to accommodate the input from new oil fields and absorb market shocks.

Turkmenistan suffered for many years from dependency on the old Soviet gas distribution network, which put it at the mercy of the Russian gas monopoly, Gazprom. After a number of price disputes and an explosion at a Gazprom-controlled pipeline in April 2009 which paralysed Turkmenistan’s gas industry for months, it finally got a break in the form of a pipeline to China, commissioned in December 2009. In 2012, Turkmenistan delivered 43 billion cubic metres (bcm) to the market, 52 per cent of which went to China, while Russia’s import fell by three quarters to 24 per cent, due to Russia’s increased domestic production. Iran soaked up 22 per cent. A raft of energy agreements signed between Berdymuhammedov and Xi in 2013 locked Turkmenistan’s growing production and export capacity into an eastern direction. By 2020, China is projected to import 65 bcm of Turkmen gas each year. This may leave precious little to other potential customers.

It seems that the Russian near-monopoly on Turkmen gas exports is being replaced by a Chinese one. Already in 2010 China was paying 36 per cent less per cubic metre than Russia, and 11 per cent less than Iran. Nabucco and TAPI—two pipeline alternatives mulled over since the 1990s that could have helped Turkmenistan break into the lucrative EU and South Asian markets—have never materialised. The reasons for their failure are complex, but Russian and Chinese intransigence did play a role.

At the current rate of production, Kazakhstan’s oil may run out in 30 years, but the country is reasonably well positioned to benefit in full from its energy wealth and eventually overcome its over-reliance on the oil sector. Turkmenistan may enjoy 70 to 100 years of robust gas exports yet its current trajectory is likely to turn it into a mere resource appendage of China.

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