Agricultural Trade within the GMS: A Perspective on Agricultural Development in Cambodia

Thun Vathana, Sok Sina and Chhay Pidor discuss the current situation of regional trade in agricultural goods and linkages to agricultural development in Cambodia, investigate the future prospects of regional agricultural trade and make policy recommendations to promote agricultural trade in the GMS.*

Introduction to Socio-Economic Background of the GMS Countries

The Greater Mekong Sub-region (GMS) covers an area of about 2.3 million sq km with a population of 262 million. The GMS consists of six member economies: Cambodia, Lao PDR, Myanmar, Thailand, Vietnam and Yunan province of China. The six countries share the 4200-km Mekong River, the world's 10th longest river. The GMS is rich in natural resources, with a wide variety of minerals, the potential for hydropower, forest and fish resources and fertile soil.

Agriculture's contribution to the economy ranges from 11 percent in Thailand to almost half of production in Myanmar (Table 1). Although agriculture still represents a significant share in the GDP of the GMS countries, each country has sought to shift its economic structure into manufacturing and services. With the exception of Thailand, which has had a free-market economy for decades, the GMS economies were previously centrally planned and characterised by state-owned means of production. Five of the six GMS economies are now undergoing a transition to a market base and opening their economies to foreign participation, but the process is slow in Myanmar for political reasons.

With a large labour force and increasing income per capita, the GMS is both an attractive production base and a potential market. Companies in east Asia are increasingly shifting labour-intensive manufacturing operations to the GMS to make use of its competitive wages, surplus of employable people and increasingly skilled labour force.

In international trade, the GMS as a whole has a slight deficit in trade balances, import values exceeding export values. The three non-Indochinese countries, however, have positive balances. The GMS countries export a range of products, but most are concentrated in a few areas. Textiles are a common export for Indochina, with export shares ranging from 13.3 percent in Vietnam to 76.9 percent in Cambodia. To increase trade, the GMS countries are committed to open their economies and undergo structural reforms under the ASEAN Free Trade Agreement (AFTA) and the Early Harvest Programme. Except for Myanmar and Laos, the GMS countries are full members of the World Trade Organisation (WTO).

The purpose of this article is to discuss the current situation of regional trade in agricultural goods and linkages to agricultural development in Cambodia. It also investigates the future prospects of regional agricultural trade and makes policy recommendations to promote agricultural trade in the GMS. The scope of this study is limited to Cambodia; information on other GMS countries serves only for comparison. The article is divided into four sections. Section 1 provides an introduction and the socio-economic background of the GMS. Section 2 discusses the linkages between trade and agricultural development. Section 3 discusses reasons that developing countries should focus on regional trade. Section 4 concludes the article and presents policy recommendations.

Trade and Development

A Historical Background

The role of international trade in economic development has received the attention of economists, policy makers, politicians and large multinational corporations for centuries. International trade has existed for hundreds of years, but trade infrastructure was poor most of that time. Money, goods and credit markets had developed to facilitate trade and colonial expansion by the 16th and 17th centuries. At that time, the economic doctrine known as mercantilism encouraged exports but discouraged imports. As a result, there was a wide rage of restrictive trade policies, including import tariffs, licences and export subsidies.

However, when the Industrial Revolution spread in the late 1700s, mercantilist ideas were increasingly questioned because raw materials for expanding outputs to be exported could not be supplied by domestic production, and therefore the country needed to relax its trade policy towards imports of raw materials. In the early 1800s a strong movement toward economic liberalisation began, with the unilateral removal of trade restrictions in the United Kingdom (the world's leading economic power at the time) starting with the repeal of its Corn Laws in 1846, ending the world's first major price-support programme for agricultural commodities. Britain then sought worldwide trade liberalisation, with some

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Table 1: Socio-Economic Situation of the GMS Countries

	Cambodia	Laos	Myanmar	Thailand	Vietnam	Yunan	GMS
	2006	2006	2006	2006	2006	2005	2005/6
Area, '000 Km2	181.04	236.80	678.50	514.00	329.56	394.10	2334.00
Population, Mn	14.10	6.52	47.37	65.23	84.16	44.50	261.89
GDP/capita, US$	419.00	425.18	202.64	3161.85	723.45	982.00	1251.85
GDP, Mn US$	5931.00	2773.00	9600.00	206,259.24	60,883.56	42,395.20	327,842.00
Agriculture, %	28.10	43.40	50.00	10.70	20.40	18.90	15.30
Industry, %	28.70	30.60	15.00	44.60	41.50	41.76	42.38
Services, %	43.20	26.00	35.00	44.70	38.10	39.34	42.31
Exports, Mn US$	3693.00	982.20	3560.00	130,583.42	39,826.00	2641.58	81,286.20
Imports, Mn US$	4749.00	1376.00	1980.00	128,606.12	44,891.00	2096.64	183,698.77

Source: compiled and calculated by authors based on various sources, 2007

success. World trade was relatively free until World War I, with selective protectionist policies (Norton and Alwang 1993). Trade was further stimulated by advances in transportation and communications.

Industries, including agriculture, that had expanded during the war suffered slack demand and falling prices after the war. Governments during the 1920s and 1930s attempted to protect these industries by introducing protectionist policies that the world is still struggling to remove today. The cost of protectionism can be high, and developing countries are concerned about it because they need to increase their exports in order to earn foreign currency to repay debts (Riddell et al. 2002). Persistent protectionist policies for agricultural commodities are especially evident in the failure of the negotiations at the WTO. Each country claims that foreign commodities compete unfairly and that their own particular product is essential for the domestic economy and farmers' well-being. Thus it is argued that government, as protector of the public interest, should provide safeguards against imports, even though it claims to support free trade.

Effects of Trade

In neither the media nor academia is there a common view on the effects of free trade. Discussions about trade often involve two opposing positions: one is that exports from more developed countries in particular cause problems for developing countries, and the second is that open trade is necessary for economic development. Proponents of the negative view of trade argue that as developing countries become more integrated into the world economy, they open themselves to increased exploitation by the more developed countries and by wealthy elites within their own countries. Proponents of the more positive view of trade argue that it facilitates development because it permits more efficient use of resources. A country can benefit if it exports what it can produce more cheaply than others and imports items that others can produce more cheaply. Some scholars argue that free trade provides prosperity to both importing and exporting countries only if both countries are at the same stage of economic development; otherwise it creates winners and losers. Losers are mainly importing countries that are less efficient and therefore less competitive. Winners are exporting countries that have efficient production methods.

The traditional model of free trade, which was based on assumptions of constant returns and perfect competition, has lost its original importance due to the empirical fact that increasing returns (economies of scale) and imperfect competition explain most of today's movement of goods. Paul Krugman (2003), the founder of the new trade theory, and others argue that trade is not necessarily a result of comparative advantage. Instead, it can be a result of increasing returns or economies of scale, that is, of a tendency to lower unit costs with large output. Economies of scale encourage countries to specialise their production and trade even in the absence of differences in their resources or technology. In the real world, economies of scale are more likely a result of imperfect rather than perfect competition. The government can play a role in creating economies of scale by supporting domestic firms' research and development. A large expenditure for research and development is regarded by the new trade theory as well as by the new growth theory (endogenous growth theory) as a reliable source of external economies (external effects).[1] In some circumstances, economies of scale are a result of strategic trade policies that governments use to support firms in international competition. Subsidies for research and development, dumping and tariffs are well-known measures used in today's strategic trade policies.

Trade will not take place if the transportation costs are higher than differences between countries' unit costs. Transportation costs pose obstacles to trade and tend to have effects on the size and location of companies. In his centre-periphery model, Krugman (1991) comes to the conclusion that high transportation costs will force producers to choose production locations close to markets, and this leads to a large and concentrated production centre that ends up with increasing returns. High transportation costs will bring trade to a halt and break the relationship between centre and periphery. Low transportation costs will facilitate trade and bring benefit to the trading countries. Prosperity increases with reduced transportation costs.

Trade under imperfect competition, to a large extent, serves to explain most trade disputes. Trade in agriculture, in particular, remains the biggest stumbling block to trade liberalisation in the WTO as well as in the AFTA, even though the economic contribution of agriculture to GDP around the world has sharply declined in the last few decades. In developed countries, agriculture accounts for only 1.8 percent of GDP, but this sector remains the most protected (Martin and Anderson 2006: 3). This section discussed the effects of trade on the development of countries involved in it. The following section focusses on trade policy in the GMS and discusses why the GMS needs to promote regional trade.

Trade Near or Trade Far?
Trade Policy in the GMS

As mentioned earlier, agriculture plays an important economic and social role in the GMS countries. Moreover, all GMS countries realise the need to increase agriculture in order to reduce rural poverty, as agreed in the GMS agriculture ministers' meeting on 10 April 2007 in Beijing.[2] Agricultural trade, especially an export orientation, helps solidify the role of agriculture in development. This is particularly true when a country manages trade with a focus on employment-based growth.

While trade is essential to agricultural development and poverty reduction, there is a variety of agricultural trade strategies depending on resource endowments, history, food security, sources of government revenues, balance of payments, the ability of commodities to penetrate into different markets etc. Nowadays most developing countries encounter impediments to agricultural trade. Major impediments to GMS agricultural trade with developed countries such as Japan, Europe and the United States are in three categories: (1) long distances to markets and poor trade infrastructure, (2) tariffs, non-tariff barriers and safeguard measures and (3) external demand constraints and market instability.

Long distances to markets and poor trade infrastructure: The GMS countries are relatively far from potential markets in developed countries. Long-distance transportation involves high costs and so reduces the competitiveness of traded commodities. Moreover, limited financial and technical support for improving trade infrastructure, together with the small volume of exports from each individual GMS country, makes per-item transaction costs higher than for bulk exports. Furthermore, poor infrastructure and inefficient institutions may increase transportation costs. Under such circumstances, short-distance trade, including trade within the GMS countries, is more beneficial than long-distance trade.

Tariffs, non-tariff barriers and safeguard measures: The simplest trade policy is a tax levied on imported goods, a tariff. Tariffs, one of the oldest trade policies, have traditionally been used as a source of government revenue and a means to raise the cost of imports and thus protect producer prices. High tariffs are still levied on agricultural commodities by developed countries like Japan, Europe and the United States. Not to speak of different subsidies that developed country governments allocate to their farmers, they have also used non-tariff barriers and safeguard measures to limit imports of cheap agricultural commodities from developing countries. Thus promoting local agricultural markets (in the GMS countries) is a reasonable strategy to develop agriculture in these countries.

External demand constraints and market instability: Generally, prices of primary commodities become inelastic when per capita income increases. Additional exports may cause a fall in world prices of commodities with inelastic demand. Therefore developing countries are concerned that their primary products face relatively inelastic demand in developed countries. As well, there is empirical evidence that developed countries are more protective of their primary than of their industrial commodities. Developed countries tend to support farm gate prices above market equilibrium levels in the hope of supporting farm incomes, generally resulting in restriction of imports. Meanwhile developing countries tend to discriminate against agriculture, resulting in high volatility of farm gate prices, which leads to an unstable supply of commodities.

Due to the above constraints and while WTO negotiations on agricultural trade liberalisation are still far from success, GMS countries should consider improving trade within the region, rather than focussing on markets in developed countries. While physical infrastructure in the GMS is being improved, each country should consider and specialise in commodities for which it can have the greatest cost advantage and import others that it cannot produce cheaply. At the same time, all GMS countries should work together as one regional body to make agriculture more competitive and to export to different regions.

A Development Perspective on Some Agricultural Commodities in Cambodia

Trans-national road corridors are being upgraded under the GMS.[3] GMS countries have taken major steps to open their borders by agreeing to trade facilitation measures, including single-stop inspections at major border crossings.

Cambodia signed a memorandum of understanding (MOU) with Thailand to facilitate cross-border movements starting in 2006 at Poipet-Aranyaprathet. Cambodia and Vietnam signed an MOU to start similar arrangements at Bavet-Moc Bai in mid-2006.

The GMS cross-border transport agreement, which entered into force in November 1999, was originally a trilateral agreement between Laos, Thailand and Vietnam, and was joined by Cambodia in 2001, China in 2002 and Myanmar in 2003. The agreement aims at cross-border facilitation on movements of commodities and people, with focuses on issues such as single-stop inspections and easy provision of visas. Easier cross-border movement is one key to attracting Vietnamese and Thai agribusiness to invest in agriculture in Cambodia. The two commodities which have received attention from investors are rubber and cassava. These two products are produced in Cambodia, exported to both Thailand and Vietnam and then re-exported to China after processing and packaging. Informal movement of cattle from Thailand to Cambodia for local use and for re-export to Vietnam was noticed even before the MOU with the two countries. McNaughton (2004) estimates that the export of live cattle from Cambodia to Vietnam, Thailand and Malaysia in 2002 was 10 times higher than recorded. After 2005, there seem to have been fewer informal movements across international borders, probably the result of trade facilitation.

In the GMS agriculture ministers' meeting on 10 April 2007 in Beijing, all ministers reaffirmed the importance of agriculture for poverty reduction because millions living in rural areas depend on agriculture for their livelihoods. They vowed to continue to support the work of the WGA. The agricultural work being carried out under the umbrella of GMS cooperation seems to be effective, to contribute to increased trade and to induce exchanges of agricultural technology. For example, many Cambodian agricultural technicians were trained by China, Thailand and Vietnam in aquaculture, animal husbandry, cross-border animal disease control and prevention and land use. China, which is more advanced in agricultural technology, has committed to provide practical agricultural training needed by GMS countries. Although Cambodia faces some constraints within the GSM agricultural development programme due to high competition in some commodities from more advanced countries, especially Thailand and Vietnam, agricultural development can be assisted through capacity building and export opportunities. However, a rosy future for some major Cambodian agricultural commodities (e.g. cassava and rubber) is visible and while for some other commodities will depend on improving the export competitiveness of major agricultural commodities.

Conclusion

Trade is not a panacea for development, but without it the development perspective is gloomy. We argue "no trade, no development," but there is a need for Cambodia to improve its international competitiveness through enlarging and specialising its production.

A necessary condition for trade is competitive products. However, this condition is meaningless if transportation costs are higher than differences in prices of goods between trading countries. High transportation costs harm all kinds of trade. Once a country is competitive in production and transportation costs are low, access to foreign markets is required.

For the development of Cambodian agriculture, there are some potential products for export, e.g. cassava, rubber and rice. More export opportunities for those commodities are foreseeable with improvement of productivity and marketing infrastructure. The increasing market in the GMS will be a stimulant for trading these kinds of products. While regional markets are available, Cambodia should consider reducing transaction and transportation costs. This together with improving productivity, this will increase agricultural trade and incomes of people living from agriculture.

Endnotes

1. These effects have long been ignored by classical growth theory.
2. The GMS Tenth Ministerial Conference in November 2001 initiated the Working Group on Agriculture (WGA) to serve as an advisory body to GMS ministerial-level conferences on agricultural issues. An inception workshop was held in July 2002, followed by annual meetings. The WGA's mission is to reduce poverty in the GMS through partnerships with rural communities to promote agricultural trade, food security and sustainable livelihoods.
3. The ADB has assisted the GMS since its inception in 1992.

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