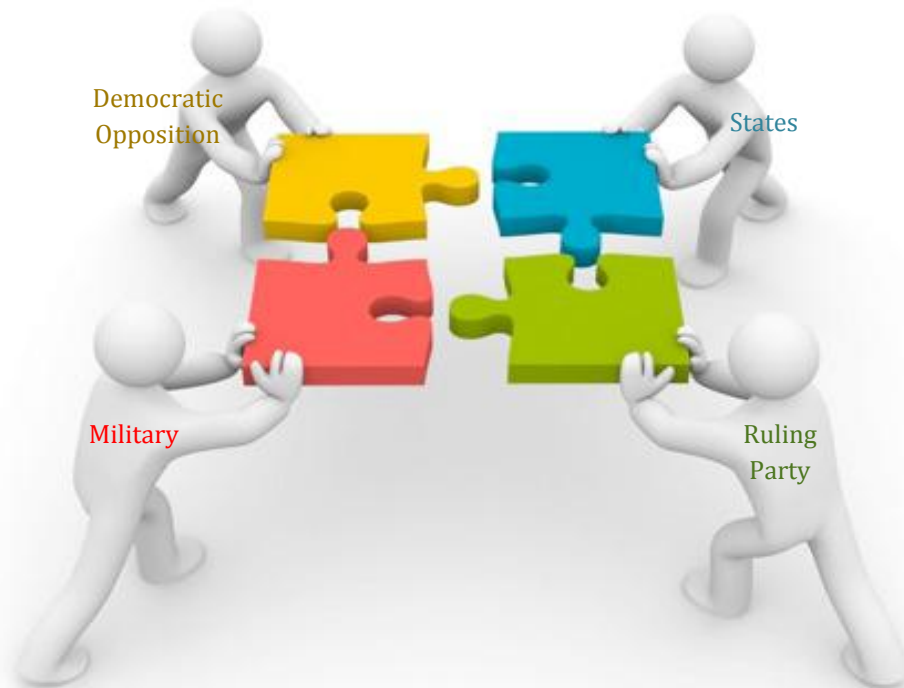




AGAINST THE ODDS: BUILDING A COALITION **Using a New Federalism for Unity and Progress in Myanmar**



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Introduction

A number of people in and out of the government have asked for ideas on promoting reform and ethnic peace. This short paper outlines an approach which builds upon field trips to the Kachin, Karen, Mon and Shan states and conversations with representatives of the UNFC¹ in Chiang Mai, Thailand. In January 2013, an initial draft was discussed with political figures in Yangon and Nay Pyi Taw. The paper uses the framework developed in “Why Nations Fail”, a recent book on economic and political development and also refers to the idea of “illiberal democracy” articulated by Fareed Zakaria². The basic idea is that a broad coalition of the incumbent party, the democratic opposition, ethnic groups and the military is needed to fundamentally change Myanmar’s past failed orientation. This broad coalition should work for a new federalism in which states (at a minimum) have fairly elected governors and meaningful revenue sources so they can run many of their own affairs. This idea for this approach grew out of work on Kachin hydropower resource-sharing. The concept of relying on broad coalitions can be extended to the stewardship of other natural resources and to questions of governance as well.

Some readers of this paper will object that the proposals go too far and are unrealistic. However, few experts foresaw the political opening between the President and Daw Aung San Suu Kyi, or the successful by-elections, or the important role of the NLD in the Parliament. This paper suggests steps we believe are needed for Myanmar to be successful. These are, we recognize, giant steps and may not be realized, but they are just possible. If all important groups agree, the constitution can be amended in the manner proposed here in order to set a new course. Without these changes, we do not see a democratic and united nation enjoying the benefits of economic growth. This is an approach for those looking for a way forward. It is a suggestion of outsiders and is meant to be thought provoking and constructive. It presents a picture of a new direction for Myanmar, one that is possible, even if very challenging to realize.

The Past

It is hard for many of the elite in Myanmar to realize just where their nation is relative to others. Fifty years of military rule, poor policies and sporadic conflict have left Myanmar in the bottom half of the bottom billion people in the world. The IMF published estimates of

¹ United Nationalities Federal Council (Union of Burma)

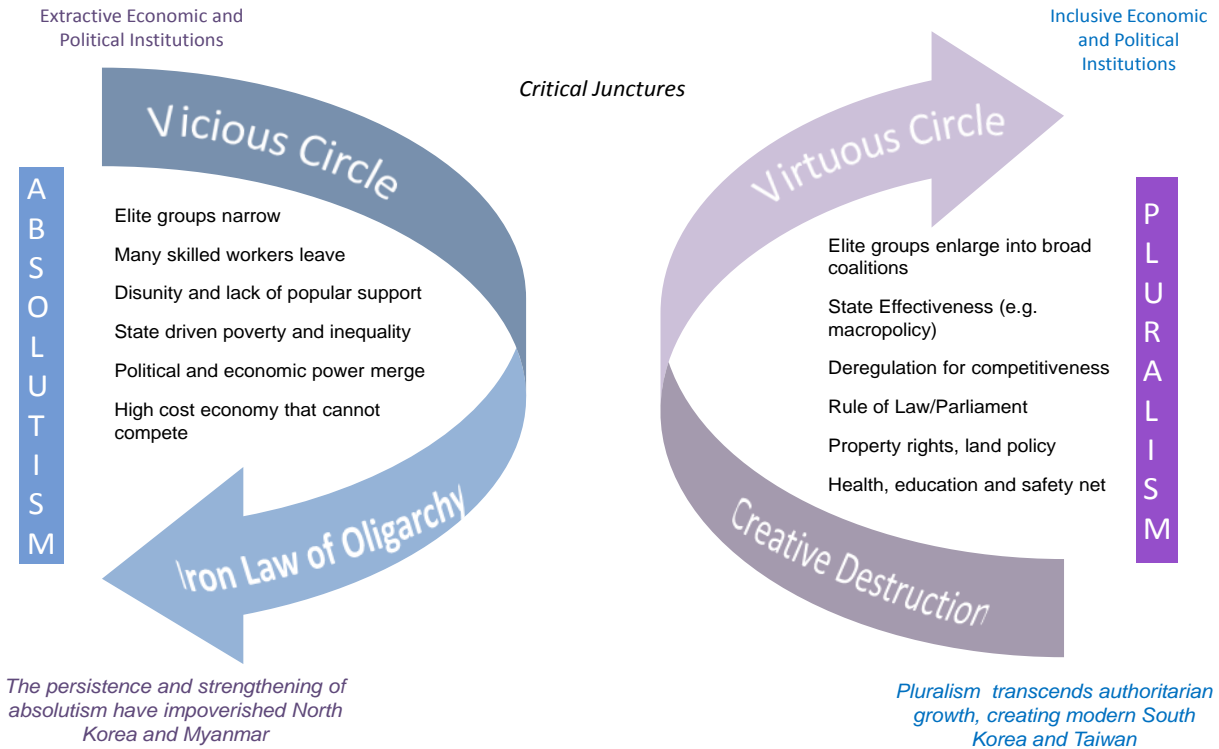
² “Why Nations Fail” by Daron Acemoglu and James Robinson argues that elite politics determine the political and economic direction of poor nations. It is the basis for the graphic on page six. The idea of illiberal democracy is developed by Fareed Zakaria in his book “The Future of Freedom: Illiberal Democracy at Home and Abroad.” that elections alone, while necessary, are not sufficient to ensure positive outcomes. The rule of law and democratic institutions are also needed.

comparable per capita income in 2011 and Myanmar at \$1325 is #164 out of 185 listed nations. Those nations below it account for only about 5% of global population. Appendix 1 discusses the reasoning for putting Myanmar in such a low position. This paper will assume that the IMF is correct and the official data inaccurate. Real GDP did not grow at 12% a year in the decade after 2000 nor is rice production after losses close to twenty million tons annually. It is also not possible that food poverty dropped in half during a period of declining food production per capita and a rising share of food in total spending.³ Myanmar is a very poor country with governance indicators and many other reliable indicators (such as electricity use) among the lowest in the world.

Once this reality is accepted, the question is how to move forward – not only with faster economic growth but also with better quality growth and political change that will unify the nation and create broad progress. Central to an answer to this question is a transition from a repressive, extractive and exclusive political system with crony businesses to a broadly inclusive political system that spreads economic opportunity. The choice to begin this transition is a “critical juncture” as shown in the diagram below. At critical junctures, bold and decisive moves are needed. Incremental or step-by-step reform approaches will be insufficient to break with the past. The present juncture was created after the 2010 elections when the President, Speaker of the Lower House and several ministers decided to push for a rapid political opening, surprising most observers. *However only moving in the political sphere will not be sufficient, broad political and economic change need to go hand in hand.* This argument applies to all nations, not only Myanmar.

³ Food poverty levels in Vietnam and Thailand are several times **higher** than those reported in Myanmar in 2010, even though both countries are significantly richer and have better safety nets compared to Myanmar. Food poverty is an income level just sufficient to buy enough calories to meet requirements.

Why Nations Fail — or Succeed Acemoglu and Robinson Paradigm



In spite of several significant political steps towards the virtuous circle on the right, on balance policies in Myanmar – especially economic policies – are still leaning in a crony- extractive-exclusive direction. Well-connected businesses still predominate. State effectiveness is low and costs are high. Property rights are weak. Health and education lag behind regional norms. Renewed ethnic conflict has contributed to slower growth. This failure to move forward on economic reform is reflected in pressure on agricultural profitability and shows up in slowing growth. The *only* plausible path to a virtuous circle **requires building a broad coalition** of reformist elements in the government, the Parliament, the military, ethnic parties, opposition parties and supportive business leaders who will work together. This will be very difficult because elements within each group may prefer the unsustainable present to a better future.

Each part of the coalition is important. The military, which still has the power to intervene at will, has to be persuaded that any changes will ensure national unity and not harm the Tatmadaw as an institution. The incumbent party, represented both in the executive and Parliament, will make major decisions for the next few years (at least) and have a decisive voice

in the political direction taken. The ethnic groups also have a key role – if they remain a suppressed minority who feel their resources are being taken, tension and conflict will prevent a shifting of resources from military uses to economic development. The democratic opposition, mainly the NLD and in particular Aung San Suu Kyi, represents popular sentiment and has to decide which allies to unite with as it pushes for dominance in the next elections. Of all these, the key group will be the democratic opposition, for they have the ability to persuade large parts of the public that a coalition is legitimate and working in their interests. They are the likely winners of any fair national elections, at least as things stand now.

Why should these disparate groups cooperate with each other? And what should they work for? They need to cooperate to get Myanmar out of its history of failure and current downward spiral towards conflict and eventual foreign domination. Myanmar's elite needs to stop relying on the plunder and extraction of natural resources as their main source of wealth, for this does not create an economy or society that is successful by any definition. The elite needs to work for political inclusion through the coalition for economic opportunity and progress; the two are dependent on each other⁴.

Move to a New Federalism

New federalism sets the stage to unwind the past and to create real peace. In the past, the terms of cease fires served to divide up revenues from timber, mineral and drug sales among the military and the ethnic militias. These paid-for cease fires reinforced a kind of feudalism, in which those with guns extracted what they wanted from the land and the people. *Cease fires of that kind are part of the problem, not part of the solution.* What is needed is a fundamental change to a rule of law, including democratic selection of local governors with all political groups represented in fair elections, and sharing of mineral and other revenues so that the state governments can effectively function. This fundamentally different approach can be called the “**New Federalism**”⁵. New Federalism is new because it does not call for separatism or national disintegration at all. Indeed, New Federalism is perhaps the only way to create a stable

⁴ Starting nation-building with a democratic framework is somewhat unique. Most fast-growing Asian economies had fairly authoritarian regimes to start and some switched to democracies after building up a middle class. However, many slow growing or failed economies also had authoritarian regimes, and Myanmar is one. The Acemoglu-Robinson argument works well for middle income countries needing to sustain growth that have “outgrown” the authoritarian regimes that got them started. It also may work for poorer nations that have found authoritarian regimes to be failures. Because of Myanmar's specific historical experiences, we believe that this paradigm applies to their current situation. Ironically, this historical approach runs counter to the claims of universality of Acemoglu and Robinson.

⁵ The idea grew out of requests to visit ethnic areas and identify policies that would hasten development and a permanent peace. In particular, the study of Kachin hydropower pushed thinking about new initiatives. The proposal shares revenues among the Kachin state, other states, and the central government.

and growing union in which all regions will want to belong. New Federalism uses peace to build a unified nation based on consent. Key to successful New Federalism are significant and meaningful regional self-government within a national framework, as well as a sharing of resource revenue with the Center. New Federalism requires real democracy and accountability in the states. The diagram depicting several elements of this new federalism is shown below:



There are economic policies needed to support this New Federalism. First, there has to be rapid economic growth, for without growth there will be little prospect of sustaining a coalition. Monopolies that drive up prices will need to be dismantled and avoided, especially in key service sectors like banking, construction, telecommunications and construction. Land for small holders will need to become more secure, while natural resources extractors will need to pay taxes to both central and state/division governments. Natural resource extractors must also control harmful emissions and curtail investments harmful to the environment. Finally, a decision needs to be made about how to treat much of the wealth gained during the past two decades – something that will likely require some degree of amnesty if those who have benefitted agree to stop or limit future extraction.

There also needs to be political and legal changes including negotiated changes to the constitution. Changing the constitution, as President Thein Sein declared in his inaugural address, is a vested right – so long as it is done in line with procedures. If negotiations with all groups lead to sufficient agreement, what modifications would promote a new federalism? The changes needed include a rebalancing of military and civilian power (i.e., no “right to intervene” by the military); a law redefining citizenship⁶; and a provision for local election of chief governors of states and rebalancing of political authority and accountability between the states and the central government; and a move to proportional representation in the Parliament to encourage healthy competition and development of viable political parties⁷. These are substantial changes but they do not require a new constitution, only amendments. These will at least have to be negotiated and agreed to by substantial parts of the military.

Issues with the Idea of New Federalism

Several issues complicate the general idea of a New Federalism.

The major one is that the current political situation is in transition from the old authoritarian system to another as yet undetermined political equilibrium. The 2010 elections were flawed. The government and Parliament are not yet fully in control of policies. The military not only has a blocking faction in the Parliament but also has influence on appointments and control of army activities. The military also has control over a special fund outside of normal budgetary oversight. Consequently, notwithstanding a democratic façade, the military effectively dictates some policies and has the flexibility to pursue policies it believes are in its own interests.

A second issue is the ongoing violence in Rakhine State. Elections in the midst of sectarian violence will not deliver acceptable outcomes. Central control will be needed until the situation improves. Indeed, a military presence is needed.

A third issue is how semi-autonomous areas are to be treated within the new states. One approach would be to allow votes by citizens in these areas on their status. If incentives for “regular” status were created by directing greater state spending to “regular” areas, it is likely that eventually these semi-autonomous areas would be willing to become normal regions within their states. (The regularized taxation of resource revenues, with some going to the state, would also reduce the incentive to remain semi-autonomous.) The main point is to negotiate and provide choices, not force unwanted changes upon these areas.

⁶ Amending citizenship has at least two elements. One would revert back to the definition adopted at Independence rather than the Ne Win / SLORC definition now used, which is more restrictive. The second element would allow Myanmar citizens to run for office, even if they were or are married to foreign nationals.

⁷ For a thoughtful view, see “Shifting to a Proportional Representation Electoral System in Myanmar?” by Richard Horsey, SSRC Conflict Prevention and Peace Forum, January 31, 2013.

A fourth problem is that many states and ethnic political parties have not given much thought to the precise institutional arrangements regarding limited autonomy. This should be discussed and negotiated prior to any transfer. Elections alone do not ensure good government or outcomes. It is therefore important for the states to have control of and responsibility for many local issues. They would not have to “negotiate with the king” over language, their form of government, local laws, etc. However, mapping out the exact set of issues that the states would control and where they would have to harmonize with national laws (in issues of land ownership, for example) is important to negotiate prior to any state elections. The parties must know what is under their control (if elected) and what is not.

A fifth area of concern is how to have free and fair state elections without armed gangs bullying and taking over. For this, some external election monitors may be needed, probably the United Nations. Since real revenues will be available to the new state governments, one can expect there will be intense political competition for offices. Keeping such competition honest and nonviolent is crucial to giving the new states a chance to function.

There are many other complexities and details that will need to be worked out, but the broad direction is for significant and meaningful regional self-government within a national framework, and for sharing of resource revenues with the center. The New Federalism we envision requires real democracy in the states. This New Federalism must be part of larger economic and political reform to move to a functioning – not illiberal – democracy.

New Federalism Helps to Avoid Illiberal Democracy

This suggestion to move towards a New Federalism is ambitious and may seem unrealistic. However, the huge support for Aung San Suu Kyi⁸ and her willingness, along with the NLD, to consider entering a coalition brings the idea within reach. Recent history provides cautionary examples and support for an approach relying on a broad coalition. If a single party is able to dominate government with few effective checks and balances, the results are often poor. The ANC (African National Congress) in South Africa, which came to power during a transitional period, had essentially complete control of politics. Notwithstanding its favorable position, the ANC failed to move the nation forward⁹. Had there been more political competition, it is likely that voter discipline of poor governance would have been more effective. In the context of Myanmar, vibrant ethnic parties are likely if the New Federalism moves forward. These parties

⁸ The NLD won almost all of the contested seats in the by-election and Aung San Suu Kyi is by far the most popular politician – her picture is in most homes we have visited throughout the country.

⁹ See “Cry, the beloved country,” in [The Economist](#), October 20, 2012. The article describes economic and political failure, a disgraceful educational system, corruption and ineffective government in spite of a peaceful transfer of power and a Nobel Prize winning political giant, Nelson Mandela, who first took office.

could improve the governance for the entire nation while seeking to protect their own rights and interests. This natural competition is why a new federalism is not just for placating the ethnic states, but is a key element of creating a well-functioning democracy in Myanmar.

It is true that the 25% military bloc in Parliament offers one kind of check and an independent Supreme Court could form another. Of course, the military bloc is likely to be more interested in protecting military prerogatives than improving governance, and may prove temporary, even if their preferred position is likely to be extended past this decade. A new Supreme Court would be untested. International experience is mixed. Courts are often subjugated to strong political forces, as was the case in Malaysia under Mahathir.¹⁰ South Africa, where the Supreme Court's decisions were generally honored during Apartheid and through the transition, fared better¹¹.

If the incumbent party moved to disassociate itself from past, unpopular policies, it too could become politically competitive over time. Establishing political vibrancy of the incumbent party would be a more durable and desirable way of ensuring effective political competition. Examples of how the incumbent party could move away from past policies include revisiting past land takings with an eye to restitution or compensation when appropriate, and trying to find a negotiated settlement on the Monywa copper mine. In any case, the emergence of a broad political coalition would diminish the chances of one-party abuse of power and an illiberal democracy.

An important component of the New Federalism is the development of a political culture accepting of the rule of the law. Our proposal recommends the reinvigoration of the Supreme Court's power to make binding decisions on the constitutionality of acts by the executive and the legislature and to protect the human rights of the Myanmar people. There are many examples – both successful and unsuccessful – of functional high courts around the world. At this point, we take no position on which of those is appropriate for Myanmar. However, a credible and functioning court that can support the development of the rule of law and the protection of individual rights will be critical for the success of the New Federalism we propose. In part, a credible Supreme Court will be critical to providing guarantees that the terms upon which the military agrees to begin to remove itself from public life in Myanmar are respected. As the military moves from a position of control to one of a minority power position, the military and others will look to an effective Supreme Court to enforce the rights negotiated during the transition. This dynamic can be extremely helpful in generating a legal and political culture supportive of the rule of law.

¹⁰ Anwar Ibrahim, the Deputy Prime Minister under Mahatir began to criticize corruption and was convicted on a dubious sodomy charge, which was later overturned. He had insisted on an independent judiciary.

¹¹ In South Africa, Jacob Zuma has tried to rein in the Supreme Court and so far has failed.

Reform the Role and Size of the Military

With respect to the role of the military, the paramount consideration is to refocus its mission so that it protects the nation more and governs less. This will mean first and foremost shrinking the size and influence of the army. The true cost of the army is not just represented in line items in the national budget.¹² There are huge swaths of land that have been taken over by the military. Some of these swaths of land remain within the bounds of military bases, often planted with crops that produce revenues for the battalions occupying the seized land. Other land has been given or cheaply sold to private companies, often with a profit interest shared with the military or the top officers. In other cases, local farmers are allowed to farm their own land, which was taken, if they pay rent back to the military. Reversing some of these land seizures is good economic and political policy.

Many “private” companies are said to be owned by officers and have privileged market positions with the ability to extract high prices. These reportedly include smaller local companies supplying fuel or other commodities, not only the larger ones in the Union of Myanmar Economic Holdings or the Myanmar Economic Corporation. Large businesses with military connections and privileged market positions include businesses in the gem and jade extraction industries and trading, banking, tourism, breweries, property, transportation and construction.¹³ Inefficiency, poor service quality, and high prices in these sectors will act as a drag on the economy, preventing rapid or equitable growth. This strangle hold on the economy needs to loosen. Reducing military control over economic sectors would reduce the flow of off-budget funds to the military, which are likely substantial but of unknown size. However, some resource extraction may remain for a transitional period.

In addition, there has been massive extraction of natural resources. Billions of dollars in timber and natural gas sales, which were largely taken over by the military leaders in the last decade, are unaccounted for. Jade sales in 2011 were quite possibly around \$10 billion or more, but little of that made it to the national budget. It would take a considerable effort to discover the true level of resources spent on the military, or the amount of cash or other investments held offshore. For example, there is a “special fund” that bypasses the Parliament (but needs presidential approval) that can be accessed by the military for unspecified expenses.¹⁴ **Reform**

¹² The [2010 Statistical Yearbook](#) (p.358) gives defense spending at 11% of total government spending in 2009-10. This includes both capital and current spending. This understates the real resources going to the military. A separate report puts military spending in the budget at 14% of \$15.3 billion government spending, or 4.3% of GDP. Other Asian nations such as Indonesia, Thailand, China and Bangladesh spend 1-2% of GDP on their militaries. Other revenues not in the budget make total military spending more than 4-5% of GDP.

¹³ “Myanmar Military: The Next Campaign – Cementing Power” by Andrew Marshall and Jason Szep, November 2012, p. 6. Telecommunication costs are also among the highest in Asia and need to come down as well.

¹⁴ Marshall and Szep, [Op. Cit.](#), p. 7

would mean directing these revenues into a unified budget and using them for investment and health and education.

If ethnic peace were really achieved, the size of the military would logically shrink, as there would be no combat role for most of the battalions. How big an army is big enough in a peaceful Myanmar? Indonesia, with some restive provinces, has 582,000 soldiers in a widely spread nation of 240 million, or 2400 soldiers per million people. Bangladesh has fewer than 1500 soldiers per million. China has 2200 per million. If Myanmar's population is 60 million, this would suggest a military sized between 90000 and 140000, including ethnic soldiers added into the national forces. Of course, it is clear that a smaller, but still competent, military will be needed for situations like Rakhine state or where local violence threatens public safety. It is not clear how many active Tatmadaw soldiers there are now, with estimates running from 200 to 400 thousand men. (Not all battalions are up to their rated strength – the “official” estimates of about ½ million military personnel assume that all battalions are at their full strength.) In any case, many currently active personnel, including ethnic militias, would have to find new vocations, but many soldiers could continue in the military. Still, those demobilizing will need special help to be sure of having the means to earn a decent living outside of the army or militia.

The ability of the military to intervene at will to “correct” the policies of an elected civilian government by taking over power is not in line with democracy or the rule of law. While the 25% appointed delegates in the Parliament may be held for a period (this is a matter for negotiation), the supremacy of the constitution and elected leaders is required for an accountable government. *This is the fundamental shift needed in the legal status of the military.* This shift would reinforce the smaller size and resources (on and off-budget) used, and support the shrinking economic role of the military in the overall economy. *A reinvigorated Supreme Court is a logical replacement of military oversight of the executive and legislative branches.* A well designed court would encourage a predictable and fair review of laws and policies and support the development of a rule of law. A vibrant Supreme Court can also play an important role in guaranteeing individual and group rights to the military who will have to exchange preferential positions in politics and the economy for credible promises of equal treatment before the law.

The other important element in this transition is a decision about amnesty for military and militia officers. There was no effective rule of law under the previous military commanders – their word was law. Commanders were told to support their units and they often did so by taking land and other resources and exacting arbitrary taxes or monopolizing trade. (Ethnic militias did the same thing.) In the process, many of the officers also became wealthy. If a decision were made to bring to trial anyone judged guilty of economic crimes, many military

and militia officers might be charged. In China, these anti-corruption drives often become ways to persecute a particular faction rather than to truly reform the system. This adds to instability and a lack of accountability, as officials try to team up with the winning side and avoid charges. This raises the question as to whether it might be wise to envision limited taking back of wealth. It may be worth considering permitting officers to retain some considerable minimum in property or other wealth as a mechanism for buying peace and coalition building. Large amounts of wealth beyond a designated maximum would be captured or taken back by the state. Imposing such a take-back is essentially a political question but it also depends on the technical difficulty of tracking wealth. In general, forgiving economic crimes, with or without take-backs, given the past murky legal environment, is probably necessary to ensure continued political and economic reform. However, huge wealth can create political power which may make it hard to govern well in the future and stricter rules can certainly be applied going forward.

Redefining National Security

The change in size and function of the military should be combined with a modernization of their doctrine. Previously, the threats to national security were from Burmese Communists and separatism from ethnic states. This era may be past, as even the Kachin are speaking of terms for remaining in Myanmar with a degree of self-government. Other groups are much less aggressive. So what issues are of concern for Myanmar's national security? The core issues are backwardness and extraction, as these cause national disunity and weakness. The military has to work to create a better government and resilient state by reducing extraction, not maintaining or intensifying it. They need to work to create a strong nation, not just a strong army.

One example of the current weakness is high transport costs. Research undertaken for Proximity found that trucking costs per ton-mile within Myanmar were five to twenty times higher than in Thailand or China. This has the effect of directing economic activity in the states to Myanmar's neighbors rather than to demand within the country. Given capital flows, migration to and from neighboring countries, and these trade flows, the states are effectively becoming absorbed economically by other nations rather than integrating within Myanmar's economy. Over time, this will draw the border-states and central Myanmar further apart, reducing national integrity. The solution is to improve roads and reduce road blocks and excessive tolls so that trade flows naturally within Myanmar rather than outside of it.

Another threat is that of adult illiteracy. While official data suggest high levels of literacy, the definition of literacy appears to be too easy and limited evidence (to be confirmed by surveys) suggest that functional literacy is much lower. That is, a farmer may not be able to read

instructions on a pesticide can or a mother may have trouble deciphering the message on a bottle of medicine for her children. This not only slows economic growth but also impedes the development of a healthy democracy. If voters cannot read, they will have difficulty making informed decisions. Fortunately, the army has literacy programs for soldiers which may prove useful as models for remedial programs. Other nations, such as India, have good adult literacy curricula. Improving the quality of literacy will make the nation more equal, more governable and promote faster growth. Improved literacy is also one way to reduce the chances of an “illiberal democracy” that combines elections with poor governance.

Additionally, many natural resource extractors now pay little in official taxes and often nothing to the local government. A rational taxation policy needs to be negotiated with owners and producers so they get a reasonable return on their assets while both central and state governments get revenue with which to invest and provide services. The magnitude of natural resource exports is much greater than indicated in the official data. For example, jade emporium sales in 2011/12 fetched \$126 per kg and official output was 43 million kg, so the calculated value was \$5.4 billion.¹⁵ However, a great deal of output is not reported, and a total jade value of more than \$10 billion is quite possible. Yet jade payments of any kind to the national government were only \$557 million in 2011/12. (See Appendix 3 for a deeper discussion.)

An important step in the direction of reversing extraction was taken when the official exchange rate to the dollar (used to convert export revenues to kyat) was moved from six kyat per dollar to 850, closer to its realistic market value. This increased the value of natural gas taxes and royalties to the Treasury. Similar adjustments, with revenue sharing among central and state governments, are needed for other minerals, timber and hydroelectricity.¹⁶ Because resources are unevenly distributed, richer states will have to share some revenues with poorer regions. If this is not done, there will be inadequate public investment, poor health and education, and a perception of state failure.

Generate Faster Economic Growth

The slowdown or even reversal in economic growth for much of 2012 suggests that policies need to be improved. First, ethnic peace would allow mining in Kachin state to be restarted.

¹⁵ Valuable jade is easy to smuggle and this avoids taxation, so assuming a price for all output equal to the Nay Pyi Taw emporium price is conservative, even though some lower value jade goes direct to Mandalay.

¹⁶ The issue of drugs remains a difficult one. Past international experience with drug substitution programs may help, especially if transport costs are reduced. Now, poppy growing and amphetamines are significant problems. However, the “opium substitution program” of China has resulted in land grabs and displacement – a small holder based model is needed, not one relying on foreign investment in large plantations.

Jade and other mining is a major source of revenue, and conflict has greatly reduced such production. Second, serious work on providing electricity in the short and medium term is needed. Current plans are mired in red tape and are inadequate to provide power except at very high prices. (Diesel generators cost 30-40 cents per kWh)¹⁷ Extensive work on improving the electrical grid is also needed. Third, the exchange rate needs to be set at a realistic level so as to encourage agriculture and labor-intensive exports, not to encourage the import of used cars. Fourth, the rapid development of a real banking sector that makes loans to small and medium businesses is needed. This will involve the entry of foreign banks, not only the growth of domestic ones. Fifth, a plan to reduce transport costs is needed – this would include improving roads and ports, and reducing formal and informal tolls. Myanmar needs to create a national economy and cannot do it without reasonable ways for different parts of the nation to trade with each other. If the economy starts to grow rapidly and in a way that rewards broad groups of people throughout the country, the chances for a successful coalition and reform program will be much higher.

Explain and Push for a New Deal

The people of Myanmar know that the past decades have not been good ones. They have seen their land taken and millions of their young people leave. They know that their country lags behind its neighbors – even Bangladesh. They want a new deal. The new deal will include the changes described in this note. If a strategy to move towards a New Federalism, including the rule of law, more self government, less military spending and more investment, better economic policies and secure land holdings is offered, the people will support it. Those who manage such policies would win popular support. The challenge is persuading existing beneficiaries of the past system to support or allow these changes. Some will be reluctant and only a broad coalition of different groups will be sufficient to insist on the needed changes. That is why a broad coalition is needed to move reform ahead.

Constructing and holding together these groups will be hard. Each group has elements that either like the present situation or prefer going it alone. The military has officers (including retired officers) more concerned with enrichment than national well-being. The ethnic parties and militias have sometimes benefited from “cease fire” arrangements and might not welcome autonomy if this meant having to compete politically and giving up their share of mineral and other revenues, unless they can be elected to run state governments. The incumbent party has various interests, and many of them benefit from current conditions. The NLD is

¹⁷ Apparently the gas pipeline, largely over land, that travels north through the Mon state to Yangon was poorly built and leaks, greatly reducing its effective capacity. A larger pipeline with better steel could replace the current one. This would allow the building of combined cycle plants of several hundred megawatts and allow Yangon manufacturing to grow. Use of aid funds and international contractors would ensure this new effort is durable.

understandably confident of its popularity and may decide that some of these other groups can be excluded in any coalition it builds.

If Myanmar fails to reach a pluralistic and inclusive solution to its current problems, it will likely be a long time before the country gets another chance. It truly is now at a critical juncture. Another few decades of failed policies may see it cede effective control of national resources and economic power to its neighbors. Again, this is the real threat to national security now and it is one that requires new thinking. A failure to grasp the size and nature of the problem would be tragic and perhaps irreversible. Political leadership is needed not only to push for new policies but also to explain to and persuade enough people so these ideas are difficult to resist. It is extremely difficult for a nation like Myanmar with its reliance on raw materials to change political and economic systems – success is truly “against the odds.” Because authoritarian solutions have been tried and worked out poorly¹⁸, the only viable alternative is some form of democratic federalism. National unity, political competition and broadly spread development are the way forward.

¹⁸ The road to Nay Pyi Taw cannot support heavy trucks – it is poorly built without steel rebar to support the concrete. Road transport costs are many times those of Myanmar’s neighbors. The gas pipeline through the Mon state to Yangon is corroded and cannot carry much gas. Electricity supply per capita is much lower than Bangladesh. Crony development has failed and the nation is poorer for it. A real change is needed.

Appendix 1: Economic Growth in Myanmar: Myth and Reality?

The World Bank does not make estimates of Myanmar's GDP except in very recent years. There is a good reason for this. The official data from 2000 to 2010 show real growth of about 12% a year. This would imply a tripling of real GDP in a decade. This clearly has not happened, so the question is if there is some reasonable way to estimate the true growth. One common approximation is to look at electricity consumption. For poor countries, it is not unusual for electricity to grow two to three times as fast as real GDP.¹⁹ From 1987 to 2008, electricity growth was 6% a year and this implies real GDP growth of 2-3% a year, not much above population growth. From 2008 to 2011, annual growth in electricity was nearly 15% and this implies real GDP growth of 5% to 7.5% a year. This is consistent with a marked increase in production of many raw materials and some services. However, 2012 has seen a reversion closer to the older pattern, with electricity growth of only 5% over 2011. This implies GDP growth of 2% or so.²⁰ Comparing 2012 vs. 2011, exports in dollars are lower – exports dropped by 4% and imports grew by only 1%. These trends are consistent with very slow or even negative growth. This is indicative of serious problems in the economy. The economy should be soaring at a time of rising interest and acceptance of Myanmar by the rest of the world.

It matters what the truth was and is concerning growth. The UN Household Surveys found a very rapid decline in food poverty – it reportedly fell in half between 2005 and 2010. It is highly dubious that food poverty declined, given that food production per capita fell over this period according to one reliable series (the U.S. Department of Agriculture, which has in-country experts following major crops in Myanmar). Indeed, the rising share of food expenditures in total household consumption usually occurs when incomes fall in real terms, not when incomes rise. Paddy production per capita in **1990** was 360 kg per capita.²¹ In 2011 according to the U.S. Department of Agriculture, it was about 320 kg. In 1990, food poverty was estimated at 47%, but in 2010 the UN survey found it below 5%! (Vietnam had 11% food poverty in 2004 and Thailand had 16% - and they are far richer than Myanmar.)²² *One more implausible finding in the UN survey is its estimate of caloric intake per capita per day – the median daily intake was estimated about 3400 calories. This is higher than levels of caloric intake in Sweden and far*

¹⁹ Electricity growth in Vietnam was 15% a year when GDP growth was 7-8% from 1990-2008. In Indonesia in the 1970-95 years, the ratio was two to three. These ratios were observed at per capita electricity use higher than Myanmar's.

²⁰ Given the high current demand for electricity, an 8% growth rate in electricity is consistent with about 3-3.5% GDP real growth and 2-2.5% real per capita growth. This growth may be distributed unequally, so living standards may not improve for many.

²¹ Retired Ministry of Agriculture officials indicated that in 1990 there was no interference with data collection and the system worked reasonably well. They said this became less true after 1990. In 2010-11, the official annual paddy production is 32.6 million tons while the U.S. Department of Agriculture implied paddy estimate (at 58% extraction, which is their assumption) is 18.2 million tons based on a rice production figure of 10.8 million tons. The official estimate is nearly 80% above the US Department of Agriculture estimate!

²² "Framework for Economic and Social Reforms: Policy Priorities for 2012-2015" (Draft), p. 8

above daily requirements. If the caloric data are true, obesity should be a major problem in Myanmar. Extensive field trips to villages fail to confirm a large obesity problem.

If the official GDP, UN poverty levels and official rice production data are all incorrect, what data is correct? The two decade decline in paddy production per capita is consistent with rising poverty. Many people still live in rural areas and rely largely on agriculture for their livelihoods. If the 1990 estimate of food poverty of 47% was accurate, it is logical to assume that today's level of food poverty is higher – well over 50%. Unless government and parliamentary leaders understand just how poor Myanmar is, they will fail to develop policies that are bold enough to deal with the actual problem, not the imaginary reality that bad data have created.

For those who still believe that trends are really positive, several other points can be mentioned:

1. In 2000, the authors interviewed an army general in Myanmar familiar with economic data. He said that a very high official “ordered the GDP numbers” and the data were adjusted to reflect his orders. He admitted that the very high growth rates were a fabrication. Notice that in 1990-91, when this distortion was said not to be in force, the GDP growth rate was less than 3% and real GDP per capita growth would then have been 1%.
2. The rate of underweight children rose from 1990 to 2003 (28.8% to 29.6%) during a period when growth was said to result in a doubling to tripling of real GDP each decade.
3. If actual paddy production were 32.6 million tons (official data), rice production should be nearly 19 million tons. An experienced rice miller put rice consumption per capita in Myanmar at 160-180 kg per capita, suggesting 10 million tons needed for domestic consumption. This should imply exports of seven to eight million tons, even allowing for seed and animal feed. Actual rice exports are between ½ and 1 million tons, precisely agreeing with U.S. Department of Agriculture production figures. The official paddy production numbers are incorrect.
4. Extensive village visits by the authors and others have produced a consistent flow of observations about difficult rural conditions that are completely at odds with a rapidly improving situation. A 2010 arm-circumference measurement of under-five year olds in villages getting public works (admittedly a non-random sample) found 95% of children below the median. Further measurements are being undertaken to expand the sample.
5. Millions of acres of land have been taken by military, government and ethnic militias in past years, resulting in significant reductions in the welfare of rural households, even when (inadequate) compensation is paid. Numerous visits confirm significant reductions in welfare from these land takings.

6. Millions of young Myanmar workers, probably at least 10% of the labor force, have left the country to work in Thailand and other nations. Given the relatively poor treatment most of them receive (they are only semi-legal and have few legal protections), this suggests a “push” factor is at work, even if a “pull” factor of better wages is also relevant.

None of these observations by themselves is conclusive, but taken together they strongly suggest a story about the past twenty years completely at odds with the official data. Real GDP growth has been mostly slow, not fast. Poverty has probably risen, not been reduced by 90%. Workers are leaving, not staying. Food production per capita is falling, not rising. Rural households who are landless or nearly landless (less than 1 acre) are growing in number and proportion. If this alternative story is accepted, then much of the recent poverty discussion is off-base and simply wrong, based on incorrect assumptions. Confronting reality is not always pleasant but it is necessary to understanding what needs to be done. Rapid improvement is possible and should be recognized when it happens, but real measurement is needed to track progress.

Appendix 2: Land in Myanmar – Time for a Reckoning

Studies of land in Myanmar have established that there has been significant taking of land by government, military, ethnic militias and influential businesses.²³ This land had usually been farmed, sometimes in shifting cultivation, by local people. Many have been on the land for generations, while others “squatted” on the land in the past decade or two. In most cases, little or nothing was paid in compensation when their land was taken. In some cases, the seized land is rented back to the previous owners, who are allowed to continue growing crops if they pay a rent to the new owners. It is uncertain how many acres of land have been taken or exactly how much of the land has been used for the purposes for which it was taken. What is clear is that past and current laws provide influential groups an incentive to take much more land than is needed. For example, the Muse special economic zone in Shan State is supposed to take over 86,000 acres, equivalent to an 11 mile by 12 mile area! The steel plant near Taungyi in southern Shan State took over 8000 acres, though uranium mining may also be going on. However, if land was not virtually free, there is little doubt that much less area would be needed and would be acquired if fair market prices were paid.²⁴

The new land laws recently enacted provide only limited protection against land grabbing. Much land does not have certificates, and some (in shifting cultivation) is not eligible for certificates. Even certificates do not always protect against land taking – many land registration officials may “adjust” lists or provide alternative certificates to those with influence or money. In any case, certificates and land mapping cost money and few farmers want to pay for such uncertain protection. The consensus of experts is that unless the new laws are modified so that fair notice is given of land auctions and land in smaller parcels is sold to the highest bidder; or that valid certificates allow more real protection against land taking without adequate compensation; or that forest land not be given to large companies but rather to smaller farmers willing to use it wisely – unless these kinds of amendments are passed, the laws will favor the wealthy and influential and provide little security for small holders. While there are remedies through a petition to Parliament, this is a long and uncertain process.

²³ Recent studies include “Myanmar at the HLP Crossroads” by Displacement Solutions, October 2012; “Developing Policy Options for Addressing Land Grabbing and Speculation in Myanmar” by Displacement Solutions, July 2012; “Financing Dispossession: China’s Opium Substitution Programme in Northern Burma” by Transnational Institute, February 2012; and “Upland Land Tenure Security in Myanmar: An overview” by the Food Security Working Group, February 2011. These studies suggest at least 1.7 million acres have been taken and tens of millions more are at risk of seizure with limited recourse.

²⁴ We were told that typical upland farm plots in Shan State were worth 600,000 kyats (about \$700) an acre but compensation – if any is paid – is usually a small fraction of that value, typically \$20 an acre or less. Even a year’s rent was 200,000 kyat (\$240) per acre in 2012 and even “high” compensation is rarely a tenth of the real value.

If states are allowed to establish local elected governments, there will have to be a review of past land takings, since there is considerable resentment against past takings – many of which were done in an arbitrary and possibly illegal way. A complete return of all land to previous owners is out of the question. While the history of who used to operate on the land or “own” it is one valid consideration, there are at least two others. A second valid consideration is how productive the taken land is now – if major improvements were made, it would be better to pay compensation at the original value than to try to return it. A third consideration is the power or influence of the present holder. Land held by the Army will not be as easily returned as that held, but not developed, by a foreign company. A special land review board is needed to examine cases and decide what to do.

One step that would help this process is a land tax. It could be levied on all land with a ten or twenty acre per family exemption, depending on the area or type of land. For example, a family holding 20 acres would pay no tax while a family holding 30 acres would pay a tax on only ten acres – the amount exceeding the exempted 20-acre holding. Such a land tax would fall most heavily on agricultural companies and speculators. If the company was getting a reasonable level of value from the land, the tax would not weigh heavily on its profits. If the speculators were simply holding but not investing in the land, the tax would encourage them to sell and reduce their tax burden. Taxes to be collected could pay for compensation of land that was taken, not properly paid for, and will not be given back. The level of the land tax would be no more than 1% of the land’s value. Such a tax would make the job of any land review board much easier since speculators would not resist so much handing back or selling some of the land that they had taken. (Alternatively, they might resist and begin to invest in it.)

Another possible method of compensating a family that had lost land but would not get the same land back would be to give it augmented land – land with tea or rubber on it that would provide income similar to that of a larger upland plot. Small plot experiments with credit, planting material, fertilizer, and fair prices for production are worth exploring. (Now, farmers are often in debt and have to sell their crops for very low prices at harvest.)The idea is to substitute capital (in the form of permanent tea or rubber plants) in place of land in order to give the farmer equivalent earning power.

There are important questions to answer. Who would be appointed to the land review boards? What rules or guidelines would they follow? Would a court have the right to hear appeals? If someone was due compensation for land taken that would not be returned, who would fund the award? How would priorities be set up? What role would the past legality or illegality of the taking play in its current disposition? All of these are important questions, and not the only ones. However, it seems likely that without some readjustment of land, there will be continuing tension, poverty and migration.

Appendix 3: Natural Resources – Time for a New Sharing

Valuable deposits of jade, gems, gold, copper, etc. have been a source of conflict in the past in Myanmar and are even now contested. Control of these deposits (and also of timber or hydroelectricity) is sought after by foreign companies, ethnic militias and the government or military – directly or indirectly. Revenues from these deposits will play an important role in Myanmar. How should they be treated?

The first principle is the need for transparency. The sales, production, costs and pollution associated with any mine should be known by the government and by the public. While the owner of the resource has a right to exploit it and profit from it, they do not have a right to hide their activities. Nor do they have a right to pollute if this violates the law. Taxation of production or profit is normal, and this requires some information about the operations of the mine. Government support of transparency initiatives suggests this is an accepted principle.

The second principle is that the “rents” from production should be shared. “Rent” is a technical term in economics. It refers to the “extra” profit made from a superior deposit, over and above the normal cost of production. In a gold mine, for example, if it cost \$600 an ounce to produce the gold and it sells for \$1600 an ounce, the rent would be \$1000 an ounce. This reflects the quality of the deposit.

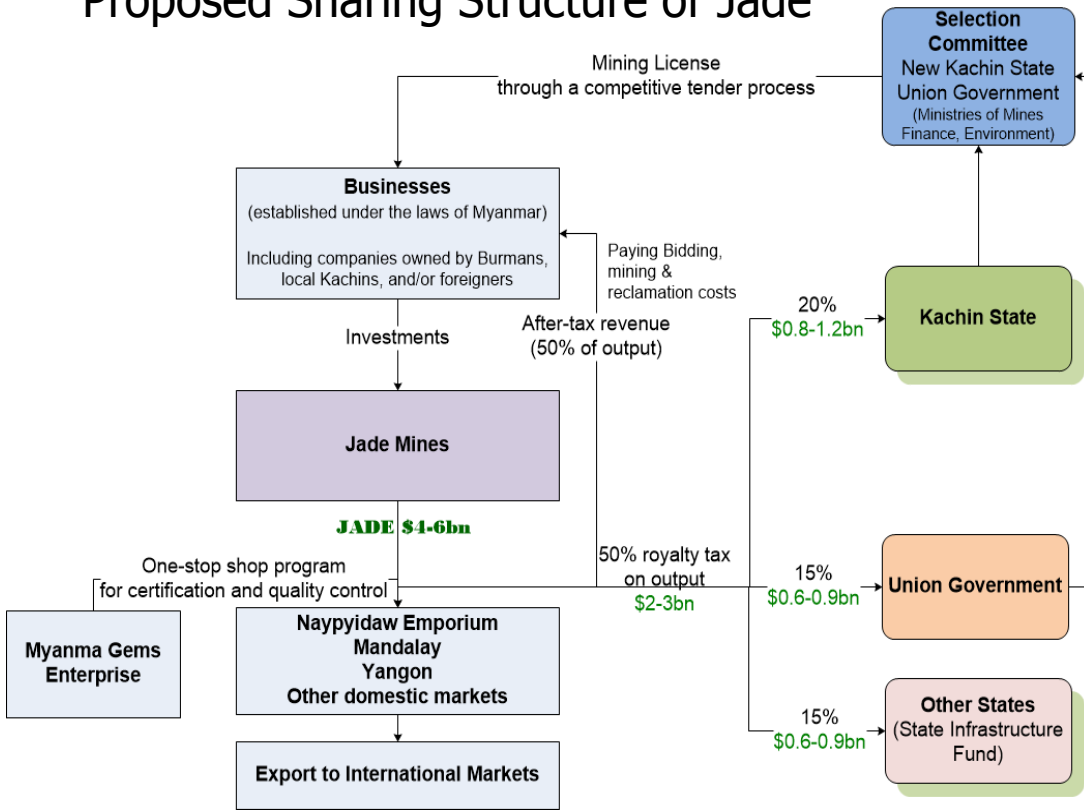
However, it is often the case that the production cost (\$600) does not account for an adequate amount of pollution control. Cyanide is often used in gold mining and if improperly dumped, it can cause many problems downstream, including death of fish and livestock, making water undrinkable or even unusable for irrigation, etc. Suppose that proper treatment of the cyanide waste cost \$60 an ounce. This treatment should be required, but then the “rent” would be only \$940, not \$1000.

The next question is how the rent should be distributed. The claimants are the owner of the deposit, the central government and the state government. All should get some fraction of the rent. This might be recovered through royalty payments (a set amount paid per acre or ton of ore); sales taxes; profit taxes on the financial amount cleared after all legitimate costs; or through production sharing agreements. The exact mix of payments is partly a technical and partly a political matter. The producer must have an incentive to invest and continue production. The state should benefit to some degree from “its” resources in order to fund infrastructure and public services. The central government also has an interest in the resource deposit and should receive some payments, if only to reduce regional inequalities.

We were told that with jade, there is a 10% sales tax and then a split of revenues with 40% to 45% going to the government in joint ventures, which now comprise most producers. There

were also (in 2011) payments to the Kachin Army, amounting to tens of millions of dollars. This arrangement reflects local realities but should be renegotiated to allow more payments to an elected local Kachin state government and a share to the central government as well. We would suggest a 20-25% sales tax on the emporium value of jade for the Kachin state government and additional taxes or production sharing as payment to the central government, to be used to enhance growth in other regions, with some minimum amount earmarked for other state governments. One such proposal is shown below.

Proposed Sharing Structure of Jade



Appendix 4: About the author and the research partners

David Dapice is a professor at Tufts University and a leading expert on the economic development of Southeast Asia and has worked extensively in Indonesia, Thailand, Cambodia and Vietnam. He was principal advisor to the Indonesian Ministry of Finance when this country enjoyed its period of rapid growth. He has studied the Vietnamese economy since the late 1980s, with a particular emphasis on macroeconomic issues, public investment policy, and regional development. Professor Dapice is also the principal economist and researcher associated with the Ash Center's research paper series on Myanmar. **Thomas Vallely** is the director of the Vietnam and Myanmar Programs at the Kennedy School of Government's Ash Center. Vallely leverages the programs' research to engage in a candid and constructively critical dialogue with a broad range of stakeholders about the economic and political challenges confronting each country. Vallely's work extends to other nations that have been isolated from the global economy or have had difficult relations with the United States, such as Mongolia, Ukraine and Cambodia. Mr. Vallely combines applied research and consulting to equip senior policymakers with a nuanced understanding of critical policy challenges they face.



The Ash Center at Harvard Kennedy School is dedicated to studying development and democratic governance in very different situations, including "hard countries" such as Vietnam, Indonesia and Myanmar. The approach taken is to understand the political economy of reform, not just the technical economics, and to explore the connections between politics and institutional development to help address social and economic problems. www.ash.harvard.edu



Proximity Designs is a unique and complex organization. It started as a social entrepreneurial company that designed, manufactured, and sold irrigation and other equipment aimed at poor rural families. After Cyclone Nargis, it grew into an organization that provided relief in emergency situations. As its name suggests, a deep knowledge of the problems it confronts is necessary to solve them. It understands that relief and better machinery do not by themselves reduce poverty sufficiently unless broader policies are also improved. Proximity spearheads a broad policy research effort which combines its local knowledge with Harvard Kennedy School's comparative political and economic insights. This partnership with the Myanmar Program has produced studies noted for their depth, nuance, and practicality. www.proximitydesigns.org