

REGIONAL COOPERATION AND INTEGRATION SUMMARY

A. Regional Cooperation and Integration Potential: Current Situation

1. The project is located in Qingshuihe town (in Mengding Township, Gengma County), and the urban areas of Zhenkang County and Cangyuan County, situated along the People's Republic of China (PRC)–Myanmar border in Lincang Prefecture in the southwest of Yunnan Province. The project area is mountainous and comparatively underdeveloped, with inadequate urban infrastructure and municipal services, and higher than average poverty rates. The majority of the population are ethnic minorities, including Wa, Dai, Yi, Miao, and Bai, and the urban residents include a relatively large number of Myanmar immigrants who live and work in the area. The area shares a long, porous inland border with Myanmar, with many border ports and border paths, including a national level Tier I port, the Qingshuihe Port in Mengding Township, and two national level Tier II ports, Yonghe Port in Cangyuan County and Nansan Port in Zhenkang County. Many local border residents from both countries are from the same ethnic groups with similar living styles and habits, and share a similar culture, language, and economic activities. Regular cross-border interactions, exchange of goods, and trade have existed throughout the area's long history. The area is one of the gateways from China to Southeast Asia, and an important part of the Greater Mekong Subregion (GMS) proposed by ADB in 1992. It is currently the second most important land port for trade between China and Myanmar, and is situated along a planned strategic trade route for China to access Myanmar's seaports on the Indian Ocean. As such, the project area has the potential to play a significant role in regional cooperation and development, led by the strong economic growth in the PRC.

2. Border trade in Lincang City has surged in recent years, spurred by the upgrading of Qingshuihe Port to a national level Tier I port, and the completion in 2014 of a secondary highway in Myanmar linking Qingshuihe Port to Myanmar's main north-south highway (Highway 3, serving Mandalay and Yangon); the latter made Qingshuihe Port a viable alternative to Yunnan's Ruili land port¹. As a result Lincang is capturing a larger share of the growing trade between China and Myanmar. By 2015, the total trade value between Yunnan and Myanmar had risen to \$9.7 billion, up from \$3.6 billion in 2010, growing at an average annual rate of 22%. By 2016, the trade value for Mengding had reached CNY 4.27 billion, growing by an average of 36% annually since 2013. The Border Resident Trade Market accounted for 70% of the total value.

3. In line with this rapid growth of trade and cooperation, heavy truck traffic and people crossings in the Lincang border area also have increased dramatically. By 2016, the total vehicle volume passing through the three ports of Mengding, Nansan and Cangyuan reached 751,000, an average annual growth rate of 38%; the total people traffic volume reached 3.37 million, an average annual growth rate of 22%. This fast pace of trade development together with increased vehicle and people traffic is placing tremendous pressure on the border cities of Mengding, Zhenkang and Cangyuan.

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¹ Ruili, in Dehong City of Yunnan Province, is currently the top land border port by value for trade between China and Myanmar, accounting for approximately 60% of the total.

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B. Key RCI Issues and Opportunities

6. However, Lincang Prefecture's poor infrastructure and low competitiveness of its second- and third-tier cities have become a bottleneck for enhancing cross-border trade and achieving sustainable economic and social development. This situation is evident in Qingshuihe, the town supporting the main land port in the prefecture. Limited customs and logistical facilities inhibit the activity of local enterprises and traders and slow the flow of goods across the border. Insufficient production space hinders new investment, resulting in a weak and underdeveloped industrial sector. The urban road network in Qingshuihe is inadequate to accommodate increased traffic flows and population, causing congestion, economic losses and safety concerns for road users and pedestrians. Access to basic utilities is also low—26% of households do not have access to clean piped water, 29% are not connected to the sewerage system, and municipal solid waste collection and treatment capacity is limited – resulting in worsening environmental pollution. The pollution impacts the wider region, since much of the untreated sewage and uncollected waste enters Nanpa and Nanting River, which flows from Qingshuihe Town into Myanmar.

7. In addition, the prefectures' border counties of Cangyuan Wa, Gengma Dai and Wa, and Zhenkang have outdated social services, such as schools and hospitals, that are operating at full or over capacity, unable to accommodate the growing populations. Teacher to student population, and hospital beds to population ratios in the project area are below national standards, and do not take into account the many local Myanmar migrants and Myanmar border residents who, due to the poor municipal services in their country, use the PRC facilities, and can account for up to 20-40% of the population served. Of particular concern, the shortage of hospital beds and staff limits the local capacity to address regional infectious diseases, such as dengue, malaria and HIV/AIDS, which is prevalent in the border area – the number of cases and outbreaks in the project area has risen in tandem with greater cross-border integration

8. Despite the recent economic growth, Lincang Prefecture still has high levels of poverty – the annual disposable income for urban residents was CNY 19,893 per capita, well below the average in the PRC. The border counties of Cangyuan, Gengma, and Zhenkang are officially designated as national poverty counties. The border economy is dominated by agriculture and agricultural processing, and local small and medium enterprises (SMEs), with no business development support. Much of the work is seasonal. Across the border, the Wa and Shan Autonomous Region of Myanmar also have high poverty levels. Due to the border location, the project area attracts many Myanmar nationals, who increasingly find manual jobs in factories established near the land ports and border cities of Lincang. As a result, the strengthening of the Lincang border economy has positive economic spill-over effects on the Myanmar side of the border.

C. Lincang Border Economic Cooperation Zone

9. In order to address these shortcomings, and promote cross-border trade and economic development, the Lincang Prefectural Government established the Lincang Border Economic Cooperation Zone (LBECZ) in 2011, with a total planned area of 33.7 square kilometers (km²), centered on the national Tier I port (Qingshuihe) in Mengding, and national Tier II ports (Nansan port) in Zhenkang and Yonghe port in Cangyuan. The first phase, to be completed by 2020, is a 3.47 km² area adjacent to Qingshuihe Port, which will be built into an important border economic platform that integrates trade and logistics, comprehensive bonded service, cross-border finance, cross-border tourism, international productivity and equipment manufacturing, import and export processing. Construction of the new country gate including a new custom building, goods inspection yard, and warehouses is already underway. The project will construct a number of urgently needed components within the LBECZ master plan, including within the Qingshuihe Port economic cooperation area.

D. Support and Complementarity with Local, National, and Regional Plans

10. The development of the LBECZ is supported by the PRC Government, and fits into the China's wider RCI framework as laid out in the Belt and Road Initiative (BRI). The BRI vision and plan, issued in 2015, lays out China's international development and cooperation strategy to develop inland economic development zones along China's ancient trade routes from Western China to Central Asia, Russia and Europe, and from China's coastal seaports to the Pacific and Indian Oceans to reach South Asia, Middle East and Europe.² The BRI strategy was incorporated into China's national development strategy, the 13th Five-Year Plan (2016-2020), which was approved by the People's Congress in 2015.³ Both BRI and the 13th FYP identify Yunnan's pivotal role in realizing the BRI vision, both as a transportation corridor to South and Southeast Asia, and as the gateway and platform for regional cooperation and economic development. Towards this goal, the State Council approved the LBECZ as one of 16 national border economic development zones in September 2013, and in December 2015 designated LBECZ and the Mengding Border Port as one of the key open ports along the PRC border, and one of five major export gateways in Yunnan Province.

11. Yunnan has fully embraced its RCI role. The Yunnan Provincial 13th FYP calls for the development of several border economic and cooperation zones and corridors in support of its role in GMS and BRI. The Yunnan Provincial Government has identified the Mengding Border Port as one of the key border trade construction projects in Yunnan Province,⁴ and in May 2014, issued the *Notice on Supporting the Construction of Lincang Border Economic Cooperation Zone* with 25 supporting policies for the construction of the cooperation zone.

12. The Myanmar government also welcomes the PRC's Belt and Road Initiative. Trade and economic cooperation between the PRC and Myanmar has been strengthened in recent years. On 14 November 2014, the PRC and Myanmar governments issued a joint announcement to further strengthen their strategic cooperation and partnership,⁵ including further strengthening cooperation on economic and trade development, and the construction of a China-Myanmar-India

² NDRC, MOF and MOC, *Vision and Action Plan Promoting the Establishment of Silk Road Economic Belt and 21st Century Ocean Silk Road* March 28, 2015

³ The Thirteenth Five Year Planning (2016 – 2020), 12th People's Congress, March 16, 2016

⁴ Yunnan Provincial Government. *Suggestions on Expediting the Construction of Border Economic Cooperation Zone*. May 2012.

⁵ PRC State Council, November 14, 2014, PRC and Myanmar Joint Announcement to Further Strengthen the Overall Strategic Cooperation Partnership between the Two Countries.

corridor. As part of the implementation of the China-Myanmar Corridor, the PRC and Myanmar governments are cooperating on several major construction projects in Myanmar, including: (i) the recently completed secondary highway from Qingshuihe Port to Hseni in Myanmar, connecting Qingshuihe Port to Highway 3, Myanmar's main North-South transportation corridor; (ii) a new bridge at Kunlong, located along the Qingshuihe Port-Hseni highway, which upon completion next year, will allow wider and heavier trucks to use the route; (iii) the upgrading of the Kyaukpyu Seaport, already underway; and (iv) planned upgrades to sections of the highway linking the PRC to the Kyaukpyu seaport. On May 16, 2017, the Ministries of Commerce of the PRC and Myanmar signed a memorandum for the joint development of border economic cooperation zones⁶ to promote and encourage the business and trade along the border area between the two countries. This includes a plan to jointly develop a 200 km² corresponding border economic development and corporation zone at Chin Shwe Haw, on the Myanmar side of the Qingshuihe Port crossing.

13. The project fits with ADB's strategic focus on strengthening RCI, with its emphasis on improving regional transportation corridors, building closer trade integration and intraregional supply chains, raising the competitiveness of border region economic corridors, and supporting the delivery of regional public goods, such as improved public health, as laid out in ADB's Midterm Review of Strategy 2020, ADB's Operational Plan for RCI, 2016–2020, and ADB's country partnership strategy for the PRC, 2016–2020. It is included in ADB's country operations business plan for the PRC, 2018–2020, which references inclusive development of small-sized cities. It will also directly support ADB's Greater Mekong Subregion (GMS) initiative. Yunnan Province and Guangxi Zhuang Autonomous Region of the PRC are members of the GMS, together with Myanmar, Lao People's Democratic Republic (PDR), Thailand, Cambodia and Viet Nam, with the shared goals of encouraging regional cooperation and integration, strengthening economic connection and promoting regional economic development. Since its establishment, commercial relations among the six Mekong countries have been increasing, notably in terms of cross-border trade, investment, and labor mobility. The Yunnan – Lincang Border Economic Cooperation Zone Infrastructure Development project has been identified as a key project to be completed under the GMS Regional Investment Framework 2022, as part of a 5-year push to achieve greater economic cooperation, as agreed under the March 2018 Ha Noi Action Plan. Finally, this project falls within the cooperation zone of the Lancang–Mekong River (LMR) Cooperation, another regional cooperation initiative between the PRC, Thailand, Cambodia, Lao PDR, Myanmar, and Viet Nam, established in March 2016. The LMR Cooperation initiative promotes the coordination and cooperation among the participating countries to achieve sustainable economic development with a focus on communication and connection, trade and production, financial cooperation, environmental protection, and poverty reduction. This project will play a critical role in developing greater regional cooperation across many of these themes.

E. Project Rationale and Justification from Viewpoint of RCI

14. The proposed project aims to promote sustainable regional economic development and regional cooperation and integration through improvements in border trade capacity, region-serving social services and environmental protection, and poverty alleviation in the border cities and towns. The proposed project will build new facilities and infrastructure in three border port cities and towns, including new trade, logistics and production facilities and road connections in and around the border economic cooperation zone to accommodate the fast growing border trade activities and trade-related production; new hospitals and new/upgraded schools to accommodate

⁶ Ministries of Commerce of PRC and Myanmar, May 16, 2017, Memorandum of the establishment of the border economic cooperation zone.

the growing population; new water supply, wastewater treatment, and solid waste management systems to accommodate current and planned economic and population growth near the main port; and support capacity development of project EA and IA staff, and the management and planning staff of key components to strengthen organizations, management, services and programs for optimal development outcomes. The project will have positive social and environmental impacts for the border region with positive implications for longer term economic development and cooperation. The project rationale and justifications include.

- (i) **Improved trade and logistic facilities.** Border trade is an important business activity for residents from both sides of the border, helping local border residents to establish their own businesses and earn money.⁷ However, a lack of adequate trade facilities at Qingshuihe border limits the types of products that are traded and increases processing times, hindering growth. The project's new, larger Border Resident and General Trade Market will reduce congestion, speed up processing times by integrating sales and distribution, and improve the quality of logistics and goods handling capacity at the border port, which will remove a major bottleneck along this important trade corridor. The second facility, the Qingshuihe International Cooperation Area, will address the lack of facilities for product processing and assembly, staging, and storage (including cold and bonded storage), expanding the range of products that can be traded and attracting more trade and production activity to the region. Together, these two facilities will help to strengthen regional integration and economic development by: (i) expanding border trade with Myanmar; (ii) improving the quality of logistic services and trade capacity in the border region; (iii) strengthening the local economy and promote export-oriented development stemming from the growth of trade and logistic sectors, the improvement of business development opportunities and enhanced cross-border supply-chain linkages; (iv) increasing employment and income earning opportunities in the region for border residents and migrant labor; and (v) expanding areas for economic and technical cooperation between the two countries.

- (ii) **Improved border port transportation access.** Qingshuihe Town is designated as a National Tier-I Border Port and is slated for further development in the national regional cooperation development plan, as it is situated along the main Kunming-Kyaukpyu Seaport transportation corridor, a strategic trade route. The Yunnan Department of Transportation has started construction of the Lincang-Qingshuihe expressway, and a high capacity connection road from the Qingshuihe expressway exit to the border port; both are scheduled for completion in 2018. The completion of this segment will complete the Chinese portion of the road transport corridor, and significantly increase the amount of border traffic and local trade and logistic service activities in Qingshuihe Town. To avoid congestion and further stimulate economic investment, an improved urban road network is urgently needed to handle the additional traffic loads. This project will build urban access roads to the expressway connector road to provide good transportation access to the border port, trade market, processing yards, warehouses and other trade and logistic facilities.

⁷ For example, to support the economic development of border areas, the PRC government gives border residents permission to import up to CNY 800 worth of goods duty free each day. Border residents typically join local wholesale trade cooperatives and pool their individual duty-free trade quotas, enabling them to buy and trade on a larger scale and achieve higher returns.

- (iii) **Improved environmental conditions and sustainable development in border towns.** The project town of Qingshuihe is located in a subtropical climate area with a well-developed natural ecological environment. The forest and vegetation coverage in the area is very high and the natural environment is in fairly good natural condition. However, due to limited access to municipal services and outdated systems, there is uncontrolled pollution discharge and random dumping of solid waste. In Qingshuihe town, there is no systematic wastewater collection and treatment system, and all domestic wastewater is discharged directly to the river system, which flows into Myanmar affecting both sides of the border. Most drinking water is from individual wells and water treatment units, so its safety cannot be assured. Growing trade activity and population is adding to the strains on municipal services and to environmental pollution from the lack of waste treatment. The project will effectively address these needs with the construction of a new water supply system, a new wastewater treatment system, and improved MSW collection and management system in Qingshuihe Town. The project will include service/connections to the Qingshuihe Border Economic Cooperation Zone, including the Trade Market and the International Cooperation Area. The project will also rehabilitate Qingshui River, which runs through the town of Qingshuihe, with many urban sewage discharge outlets, and flows into Nanpa and Nanting Rivers, which are shared with Myanmar. The project will build a new river embankment to meet the flood control standards, stabilize the banks along the new port development area, and build sewage inception pipes along both sides of the river to collect the sewage water and send it for treatment before discharge. Together, these components will help to reduce the environmental pollution and protect the natural environment on both sides of the border, and promote sustainable development in Qingshuihe Town. They will also create a better urban environment and improve living standards, which are important conditions to promote border town economic development.
- (iv) **Improved social services and integration for border residents.** The increase in regional cooperation and trade has led to rapid population growth along the Lincang border area, a trend which is expected to accelerate after the completion of the Lincang-Qingshuihe expressway. The rapid growth of the economy on the Chinese side of the border has attracted many immigrated workers from Myanmar, and business connections between both countries have grown steadily. This has contributed to greater regional integration not only economically, but across a much broader range of activities, including education, medical services, cultural exchange, etc. Many children of immigrant workers or Myanmar residents living in China are attending Chinese schools, and many Myanmar citizens come to Chinese hospitals and schools to access better quality services. As a result, there is a need to increase the capacity of these social service facilities to accommodate the local population growth and increasing numbers of Myanmar residents using these facilities. Currently there are acute shortages, with some elementary schools operating at 150% of capacity, and hospitals with no available beds treating patients who ought be admitted as out-patients. The project will help to construct two hospitals and one new elementary school, and expand one existing elementary school to address current shortages and meet future needs. In addition to increased access to hospital care, the regional health benefits of the new hospitals are: (i) a wider range of services available to border residents, such as MRI scans; and (ii) increased capacity to detect and treat infectious disease

outbreaks (e.g., Dengue, Malaria and HIV/AIDS), which have risen in tandem with cross-border migration, with the establishment of dedicated infectious disease wards. The latter will also help to strengthen the local institutions involved in the early detection and reporting system for infectious disease outbreaks along the border region. An additional regional benefit of new school construction is enhanced language and cultural familiarity between China and Myanmar as more Myanmar students are accommodated, which will help to promote spatial mobility across the border and cross-border business and economic investment in the future.

- (v) **Poverty alleviation and ethnic minority development.** All eight counties and district under the jurisdiction of Lincang Prefecture are national level poverty counties/district according to the PRC poverty standard poverty line. The average per capita GDP in Lincang Prefecture (CNY 18,710 in 2015) is less than half of the national average (CNY 49,351 in 2015). Furthermore, the ethnic minorities are concentrated in the project cities and towns: Minorities account for 93.9% of the population in Cangyuan County, 55.2% in Gengma County, where Qingshuihe Town is located, and 31.5% in Zhenkang County. A similar situation exists on the Myanmar side of the border, with high concentrations of poverty and minority population. The project will help to create new job and business opportunities for local border residents and Myanmar migrants, which will help to alleviate poverty. It will also develop and implement an ethnic minority development action plan to help address the development needs of the minority population and help them to improve their living standards.
- (vi) **Increased organizational and development capacity for RCI.** Many infrastructure projects are built with a “build it and the will come” mentality that has resulted in their underperformance and reduced their developmental impacts. Building on learning from successful border development projects elsewhere, this project will complement the physical investments in facilities and infrastructure with capacity building initiatives to strengthen project management and facilities management, and provide development support. Specific to RCI, training workshops, study tours, and technical assistance will be provided to strengthen the management, development and promotion of the border resident market and international cooperation area; to support small- and medium-sized enterprise (SME) development; to develop educational programming; and to help position and strengthen the competitiveness of the LBECZ in order to maximize its regional economic and trade development impact.
- (vii) **Improved regional coordination and communication.** The project is adopting innovative approaches to strengthen communication and coordination between China and Myanmar. The regular meetings between the Director of LBECZ and the Director of the Commercial Bureau, Ministry of Commerce, in Chin Shwe Haw, Myanmar is one example of the mechanisms being used. The development of an ICT trade platform in the Border Trade Market is another, which will help to improve communication between sellers in Myanmar and traders in China; currently sellers bring their agricultural products to the border purely on spec, aggravating over supply and shortage problems. These innovative mechanisms are being piloted and can serve as a reference for other border areas in China and Asian countries.

F. Recommendations and suggestions for project design and development

15. In order to achieve the expected RCI outcomes, several measures to improve project design and development are recommended:

- (i) **Phase the development of trade and logistics facilities.** The planned areas for the new Trade Market and International Cooperation Areas are relatively large in size, with most of the area intended to meet future demand. The FSR demand forecasts support a rapid build out of these facilities, based on optimistic assumptions of sustained rapid growth rates and the expeditious completion of the Kunming-Kyaukpyu Port transportation corridor. However, slower or fluctuating trade growth due to construction delays, political instability, etc. would result in a slower take-up rate, and could pose significant financial risks associated with high vacancy rates and facilities becoming outdated. Given these uncertainties, it is advisable that the build out be phased according to realistic timelines to allow room to expand and flexibly respond to future demand as it emerges.
- (ii) **Conduct a market analysis and competitiveness assessment.** The LBECZ in general, and the International Cooperation Area in particular, would benefit from a more targeted approach to development, based on a market analysis and competitiveness assessment to guide their positioning, development, phasing and promotion. The current approach is based on a comprehensive list of potential trade zone locators that does not adequately take into account: (i) locational preferences of particular industries, (ii) competing trade zones (including several other Myanmar–PRC border port areas, such as Ruili, as well as competing locations along the corridor, such as Kunming, Dali, Lincang City, and the Kyaukpyu Seaport), (iii) the specific strengths and limitations of Lincang border area (e.g., the limited size of the border labor market), (iv) the relationship to various phases of corridor completion, and (v) broader trends in trade and logistics in the region.
- (iii) **Introduce business development support programs for SMEs.** Most local trade, logistics and agricultural processing activity in the Lincang border area is undertaken by SMEs. The success of the project Border Trade Market and International Cooperation Area, and the Lincang border region more generally, will therefore depend on the expansion of existing SMEs, and the attraction and creation of new ones. To facilitate this process, the LBECZ should provide SME development support, including incentives, business development services and financing.
- (iv) **Develop an education curriculum** that supports local cultural learning, and facilitates migrant and foreign student integration, to help achieve the longer term RCI benefits of the new schools.
- (v) **Assess potential transboundary health issues** associated with cross-border movement of goods, people, and migrant workers, and leverage new hospital capacity, especially with respect to infectious disease detection, reporting and treatment, to further strengthen health in the border area. This can be done through ADB's health impact assessment (HIA) using the framework developed for the GMS countries.

G. Capacity development program for RCI development

16. To address the recommendations above and realize the full RCI development impacts, the following set of capacity building initiatives are proposed, and described in detail elsewhere in the report. Market surveys, study tours, training workshops, and technical assistance will be provided to:

- (i) **Strengthen the Management of the Border Resident Market and International Cooperation Area.** The objective of this initiative is to (i) to improve the efficiency and effectiveness of the Border Resident Trade Market operations and management, (ii) to provide a better understanding of the potential market demand for and competitiveness of the facilities of the ICA, (iii) to assist in creating a marketing and business development plan strategy for ICA, (iv) to inform the phasing of the facility construction, and (v) to strengthen overall management capabilities.
- (ii) **Strengthen the Competitiveness and Positioning of LBECZ.** The purpose of this initiative is to undertake a study to gain an enhanced understanding of the strategic role and competitiveness of the LBECZ within the larger Yunnan-Myanmar development area, and to propose a strategic action plan to systematically increase its competitiveness and capacity to deliver on this role.
- (iii) **Strengthen SME Development.** The purpose of this initiative is to advise LBECZ on setting up an SME Development program by (i) providing a clearer picture about the growth and composition of SMEs in the Lincang border area, as well as their issues and constraints, to better understand SME support needs; (ii) providing knowledge and information to LBECZ policymakers about SME development programs; and (iii) formulating a strategy for SME development in the LBECZ border area.