

# THE LANCANG-MEKONG COOPERATION MECHANISM (LMCM) AND ITS IMPLICATIONS FOR THE MEKONG SUB-REGION

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A WORKING PAPER ON THE LANCANG-  
MEKONG COOPERATION MECHANISM

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## ISSUES & INSIGHTS

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## **Executive Summary**

The Lancang – Mekong Cooperation Mechanism (LMCM) was officially launched at the first LMCM Leaders' meeting in Sanya, China in March 2016 with the participation of leaders from Cambodia, China, Laos, Myanmar, Thailand, and Vietnam. The LMCM includes cooperation in political and security issues, sustainable economic development, and social, cultural, and people-to-people exchanges. The scope of cooperation covered under the mechanism is much broader than other existing mechanisms in Mekong sub-region.

This paper will examine how the LMCM fits into the national development strategies of Mekong riparian countries and identify possible associated risks for downstream countries. As the initiator and its strongest supporter, China is the only country that has articulated a clear vision for the LMCM, which serves China's strategy to expand its influence in the region through building and promoting China-led cooperation mechanisms. The LMCM also serves China's domestic development needs by addressing excess production capacity and economic development of its western region. For other Mekong riparian states, the LMCM mostly fits into their interest in poverty reduction, agricultural development, and improving connectivity. It also fits some other specific political interests for these countries.

Although this initiative does contribute to overall cooperation in the Mekong basin, it also poses some possible risks for downstream states such as economic dependence due to Chinese economic dominance, reduced ability in adopting monetary policy, and the probability of indebtedness to China. Other risks might occur due to the increased unemployment rate, the introduction of Chinese laborers, and negative environmental impacts. Based on the potential risks, this paper recommends strategies for Mekong states to minimize risks while taking advantage of the LMCM for their national development and regional cooperation.



## **The Lancang–Mekong Cooperation Mechanism (LMCM) and its implications for the Mekong sub-region**

By Nguyen Dinh Sach

The Lancang–Mekong Cooperation Mechanism (LMCM) was officially launched at the first LMCM Leaders’ meeting in Sanya, China in March 2016 with the participation of leaders from Cambodia, China, Laos, Myanmar, Thailand, and Vietnam. The idea of creating a new cooperation framework for China and other Mekong countries was initiated by Thailand; it was then called the Initiative on Sustainable Development of the Lancang–Mekong sub-region. The Thai initiative included cooperation in water-related disaster management, tourism, safety of navigation, agriculture, and fisheries, all related to water use on the Mekong. By contrast, the LMCM has a much broader range of cooperation activities including political and security issues, sustainable economic development and social, cultural, and people-to-people exchanges.<sup>1</sup> In the first stage, LMCM prioritizes cooperation in five areas: connectivity, production capacity, cross-border economic cooperation, water resources and agriculture, and poverty reduction. This suggests that China’s strategy toward the Mekong sub-region goes beyond sustainable economic development to include political and security issues in downstream countries.

Since formation of the LMCM, China and the other Mekong countries have been accelerating engagement in the five priority areas. However, China’s strategy to use the LMCM to address its own economic development and increase its influence in the region has made Southeast Asian partners wary that LMCM could have adverse impacts and make them more dependent on China. Meanwhile, major problems related to Mekong water management remain unaddressed.

This paper is divided into five parts. First, I lay out the regional context in which the LMCM was created. Second, I examine China’s strategy behind the LMCM and how Beijing’s underlying ambition shapes LMCM cooperation. The third section examines how the LMCM fits into the interests of other Mekong countries and how they are responding to the initiative. Section four identifies risks associated with cooperation projects for the downstream states. In the final section, I recommend strategies for downstream Mekong countries to reduce the risk associated with the LMCM. Specifically, I recommend that the Mekong riparian states should take advantage of LMCM to promote national development, but should be very active in proposing their own cooperation agenda instead of being led by China’s proposals, and should be cautious in negotiating conditions for loans and investment from China. Mekong countries should also insist on prioritizing water management issue as this is the most enduring problem with largely negative impacts.

### **Regional context**

The Lancang–Mekong Cooperation Mechanism (LMCM) is one of many cooperation mechanisms in the Mekong basin. The mechanisms can be categorized into those that are internally focused and those that involve external partners. Internally focused

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<sup>1</sup> These are the three pillars of cooperation identified in the Sanya Declaration.

mechanisms emphasize coordination of water exploitation among lower basin members. They include the Mekong River Commission (MRC), which includes Cambodia, Laos, Thailand and Vietnam and the Ayeyawady-Chao Phraya-Mekong Economic Cooperation Strategy, which includes the MRC countries plus Myanmar. Externally focused groups include the Greater Mekong Sub-region (GMS) Economic Cooperation Program (mainly funded by the Asian Development Bank), Mekong–Japan Cooperation, Mekong–Ganga Cooperation (Lower Mekong countries and India), the Mekong– Republic of Korea Partnership, the Lower Mekong Initiative (initiated and funded by the US), and the ASEAN Mekong Basin Development Cooperation (AMBDC). The common theme among these mechanisms is that the areas of cooperation, including infrastructure improvement, poverty reduction, and capacity building, are inter-related. The external partners that have engaged the lower Mekong countries through these mechanisms have tried to exclude China and expand their influence in the sub-region to counter China, which has made the Mekong River sub-region an arena for power competition.

Among these mechanisms, the Mekong River Commission (MRC), established in 1995, is the major body. The MRC has not been effective in preventing dam building on the Mekong because it has been used as a technical advisory agency that only governs projects on the mainstream Mekong and not those on tributaries. Moreover, MRC regulations are not binding: they only require prior consultation for any project before the construction begins. Together with its lack of funding, the diverse interests of MRC members in water exploitation make it difficult for the MRC to coordinate activities in the Mekong basin. For example, Laos sees the MRC as a political bully as it has consistently condemned Laos for its dam-building projects on the river.<sup>2</sup> Meanwhile, Thailand did not notify the MRC of its water diversion project. It is against this backdrop that China proposed the establishment of LMCM.

Despite the existence of these cooperation mechanisms, several other factors influence relationships in the region. First, riparian countries continue water exploitation projects on both mainstream and tributaries of the Mekong without due attention to the adverse impacts on other Mekong countries. The projects are undertaken within the individual capacity of each country without any or with very loose consultation with other Mekong countries.

China has already completed the construction of six dams and is planning to build another 21. There have been cases where China discharges water from its reservoirs in the wet season and stores water in the dry season, which have severe impact on the downstream basin.

Laos has finished the construction of 29 dams, 26 more are under construction, and another 33 are being planned. Among them, the Xayaburi, the biggest dam on the Mekong mainstream in Lao territory, is under construction despite serious criticism from other downstream countries and nongovernmental organizations for the significant negative economic and environmental impacts on the downstream basin.

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<sup>2</sup>Shannon Tiezzi, “Facing Mekong drought, China to release water from Yunnan dam,” *The Diplomat*, <https://thediplomat.com/2016/03/facing-mekong-drought-china-to-release-water-from-yunnan-dam/> (accessed Dec. 11, 2017).

Thailand is also eager to move ahead with its project to divert water from the Mekong into the waterway to its northern area for agriculture production.

Cambodia and Vietnam also have dam projects planned, although they are smaller than those upstream in China and Laos. Vietnam has not constructed any dams on the mainstream but has finished building dams on tributaries that flow into the Mekong through Cambodia territory. Cambodia has no dams in place yet, but is conducting feasibility assessments for two dam projects on the Mekong mainstream.

The major impact of all these water exploitation projects is the change of the water flow pattern, which is associated with many problems. The cascade of six completed dams in China only can store over 23 billion cubic meters of water, which is equal to 28 percent of the annual river flow at the border of China and Thailand.<sup>3</sup> As water is stored, the dams usually trap most of the sediment that fertilizes rice fields. The impact becomes more severe in the dry season because a lack of water flow causes salinization of land, making agricultural production almost impossible. This threatens food security of around 60 million people in the Mekong basin and has further implications on the region as most rice exports to Southeast Asia are produced in downstream countries, including Thailand, Cambodia, and Vietnam.<sup>4</sup>

The building of dams also blocks the migration of hundreds of fish species, which are the main source of living and provide 40-80 percent of the protein for local communities with an annual catch of 2.6 million tons and annual revenue estimated to be \$3.9 to \$7 billion a year.<sup>5</sup> Agricultural and fishery sectors combined employ up to 75 percent of local residents.<sup>6</sup>

Second, with its rapid economic growth, China is expanding its influence in Southeast Asia and other parts of the world. As its economic power has increased, China has gradually become not only the leading trade partner but also a major foreign investor in the region, especially in Laos and Cambodia. However, China's economic presence in the region is still far behind countries such as Japan and South Korea. Currently, most major infrastructure projects in the Mekong riparian countries are funded and implemented by Japan, while foreign investment comes from sources such as Japan, South Korea, Taiwan, and Malaysia. To expand its economic and political influence, China needs to increase its presence and build its own China-led international cooperation mechanisms. To do that, China is speeding up the implementation of China-led initiatives such as the Belt and Road

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<sup>3</sup>Timo Räsänen, "New study shows significant impact of Chinese dams on Mekong," *The third pole*, <https://www.thethirdpole.net/2017/02/06/new-study-shows-significant-impact-of-chinese-dams-on-mekong/> (accessed Dec. 11, 2017).

<sup>4</sup> Richard Cronin and Timothy Hamlin, *Mekong turning point: shared river for a shared future*, (Washington DC: The Henry L. Stimson Center, 2012), <https://www.stimson.org/content/mekong-turning-point-shared-river-shared-future> (accessed Dec. 11, 2017).

<sup>5</sup>Timo Räsänen, "New study shows significant impact of Chinese dams on Mekong," *The third pole*, <https://www.thethirdpole.net/2017/02/06/new-study-shows-significant-impact-of-chinese-dams-on-mekong/> (accessed Dec. 11, 2017).

<sup>6</sup>Schmeier, Susanne, "Regional cooperation efforts in the Mekong river basin: mitigating river-related security threats and promoting regional development," *Austrian Journal for Southeast Asian Studies*, Vol. 2, No. 2, pp. 28-52, (2009), <https://ssrn.com/abstract=1531374>.

Initiative and the Asian Infrastructure and Investment Bank. Under those initiatives, China is offering billions of dollars in loans to finance infrastructure projects along its imagined Silk Road, which runs from China through South and Southeast Asia to Europe and Africa. Those initiatives, together with the LMCM, contribute to China's rising influence in the region.

Third, despite the effort to promote cooperation, there are still sources of tension between countries in the Mekong sub-region (China and Vietnam over the South China Sea, Thailand and Cambodia over land border disputes, Vietnam and Cambodia over land border disputes, Thailand and Laos over border issues, Myanmar and China over border areas). Those border issues lead to suspicion toward each other, especially toward China, and may escalate tensions if they are not well managed.

Fourth, China seems to have sufficient hydropower from the Mekong at least in the short- and medium-term. The energy market is changing rapidly with a remarkable decrease in renewable energy prices, such as solar and wind power, in the past two years, making this energy more viable while hydropower is becoming less attractive due to rising tradeoffs regarding the environment, loss of revenue from fish catch and agriculture production. At the same time, hydropower plants usually have high construction costs and take a long time to recover the investment, which can pose financial risks. In 2015–2016, solar and wind energy prices dropped by 13 percent and 10.75 percent, respectively. In this context, China is diversifying its energy sources, especially with increased capacity of renewable energy production. China has been installing numerous solar panels and has become the biggest solar energy producer in the world. Currently, China has overcapacity in electricity production and Yunnan province is now losing \$15 million per day due to overcapacity. This, together with China's slower economic growth reduces pressure to exploit the Mekong River to generate more energy to meet demand. Therefore, China has more room to compromise on water use with downstream states to expand its influence and promote itself as a responsible power.

### **China's strategy and efforts to institutionalize the Lancang-Mekong Cooperation Mechanism**

China's strategy is the most important factor shaping the scope and implementation of LMCM. Other Mekong riparian countries are responding to China's initiative without a specific and coordinated strategy. Therefore, *it is necessary to understand China's motives for establishing the LMCM to identify the risks associated with LMCM and to recommend a strategy for other riparian states to respond to China's proposals.* This section will examine how the LMCM complements China's broader economic engagement strategy and how China is implementing the LMCM.

President Xi Jinping has articulated China's overall economic strategy as making China a moderately affluent society by about 2020 and transforming China into a fully developed nation by about 2049. At the recent 19<sup>th</sup> Party Congress, Xi emphasized that the new era will see China move closer to the center stage and making greater contributions to

mankind.<sup>7</sup> In other words, China will continue to seek to influence the shape of global developments through China-led mechanisms such as Belt and Road Initiative and the Asian Infrastructure Investment Bank.

In the Mekong sub-region, accelerated implementation of LMCM is part of China's strategy to develop the nation and expand its influence. Specifically, the LMCM serves to (i) promote the development of China's western territory, (ii) expand the market for Chinese products to address China's excess capacity and promote internationalization of the yuan, (iii) to complement the Belt and Road Initiative and (iv) to repair China's image in the region after rising criticism of China's aggressiveness.

**Promote the development of China's western territory.** In 2000, the China State Council launched the Western Development Strategy to boost economic development in its western provinces as this region was lagging the coastal part of the country. The western region of China accounts for 77 percent of the country's total land area but makes up only 28.6 percent of total population and 17.7 percent of GDP. Data from Chinese government shows that the average income in western provinces was approximately 77 percent of the national average in 1999 and had only risen to 80 percent in 2008.<sup>8</sup>

As part of the Western Development Strategy, China has built and is planning to build more dams and their related infrastructure in a bid to generate income for residents, lifting them out of poverty. Much of the hydropower is to be sold to coastal provinces. From 2001 to 2005, the central government even banned hydropower projects in Guangdong to increase demand for projects in the southwest, notably in Sichuan and Yunnan.<sup>9</sup>

The five-year action plan for 2016–2020, announced by Premier Li Keqiang, sees the period as a critical time for the western region to realize its development goals through innovation, reform, and opening-up.<sup>10</sup> As part of its opening-up strategy for its western region, China sees Yunnan province as critical to efforts to connect to Southeast Asia and South Asia.<sup>11</sup> Its shared borders with Myanmar, Laos and Vietnam make it a gateway<sup>12</sup>. The LMCM, with its connectivity, production capacity, cross-border economic cooperation initiatives, connects Yunnan to Southeast and South Asia and promotes cross-border

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<sup>7</sup>Tom Phillips, "Xi Jinping heralds 'new era' of Chinese power at Communist party congress," *The Guardian*, <https://www.theguardian.com/world/2017/oct/18/xi-jinping-speech-new-era-chinese-power-party-congress> (accessed Dec. 11, 2017).

<sup>8</sup>Nancy Huang, Joie Ma and Kyle Sullivan, "Economic Development Policy for Central and Western China," *China Business Review*, <https://www.chinabusinessreview.com/economic-development-policies-for-central-and-western-china/> (accessed Dec. 11, 2017).

<sup>9</sup>Andrew C. Mertha, *China's water warriors: citizen action and policy change*, (Cornell University Press, 2008), pp. 29-30.

<sup>10</sup>"New five-year plan brings hope to China's west," *Xinhua*, [http://english.gov.cn/premier/news/2016/12/27/content\\_281475526349906.htm](http://english.gov.cn/premier/news/2016/12/27/content_281475526349906.htm) (accessed Dec. 11, 2017).

<sup>11</sup>Naina Singh, "Yunnan: China's Bridge to South and Southeast Asia," *The Diplomat*, <https://thediplomat.com/2016/08/yunnan-chinas-bridge-to-south-and-southeast-asia/> (accessed Dec. 11, 2017).

<sup>12</sup>Tibet province has similar geographic importance to that of Yunnan but there are more political sensitivities to connecting with the outside world.

economic activities.<sup>13</sup> China has also proposed a giant railway project that would run from Yunnan province through Laos, Thailand, and Malaysia to Singapore.<sup>14</sup>

**Expand the market for Chinese products to absorb China's excess capacity and promote internationalization of the yuan.** China's factories have been producing more steel, solar panels, and other products to sustain its high economic growth and keep laborers employed. However, the quantity of those China-made goods has exceeded the demand of its domestic market. According to the China State Council's Guiding Opinion on Eliminating Severe Excess Capacities published in 2012, the country was experiencing severe excess capacity in the steel, cement, aluminum, flat glass, and shipbuilding sectors. Sustained overproduction capacity also exists in more than 10 other industries such as ferro-alloy, iron, copper smelting, and zinc smelting.<sup>15</sup>

To address its excess capacity problem, by the end of 2016, China had signed several production capacity cooperation documents with 27 other countries in Central Asia, Southeast Asia, Africa, Latin America, and Europe.<sup>16</sup> China also signed a joint statement with ASEAN on industrial capacity cooperation. Within the framework of the LMCM, China and five other Mekong riparian states issued a joint statement on production capacity cooperation while releasing no similar documents on the other four sectors of connectivity, cross-border economic cooperation, water resources and agriculture and poverty reduction. In speeding up the implementation, China announced \$5 billion in loans specifically for industrial capacity cooperation,<sup>17</sup> proof that China is eager to prioritize industrial capacity. Concluding the agreement with other Mekong riparian countries could help China maintain production capacity, especially in areas such as steel, cement, and other sectors necessary for infrastructure improvement, which is much needed by other less developed riparian nations. As stated in the Sanya declaration, production capacity cooperation within the LMCM will be implemented in the industries of building materials, supporting industries, machinery and equipment, power, and renewable energy, which are also areas where China is experiencing excess capacity.

Together with production capacity cooperation, LMCM countries agree to develop key infrastructure projects to build a comprehensive network of highway, railway, waterway, port, and air linkages in the Lancang-Mekong region; expedite construction of a network of power grids, telecommunication, and the Internet; implement trade facilitation measures;

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<sup>13</sup>"Sanya Declaration," [http://www.fmprc.gov.cn/mfa\\_eng/wjdt\\_665385/2649\\_665393/t1350039.shtml](http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/2649_665393/t1350039.shtml), (accessed Dec. 11, 2017)

<sup>14</sup>David Eimer and Oudomxai, "China's 120mph railway arriving in Laos," *The Telegraph*, <http://www.telegraph.co.uk/news/worldnews/asia/laos/10572583/Chinas-120mph-railway-arriving-in-Laos.html> (accessed Dec. 11, 2017)

<sup>15</sup>Rui Fan, "China's Excess Capacity: Drivers and Implications," *Stewart Law*, <http://www.stewartlaw.com/Content/Documents/China%27s%20Excess%20Capacity%20-%20Drivers%20and%20Implications.pdf> (accessed Dec. 11, 2017)

<sup>16</sup>Zhang Mei, "The Present and the Future of China's Production-Capacity Cooperation with Foreign Countries," *CIIS*, [http://www.ciis.org.cn/english/2016-08/19/content\\_8975283.htm](http://www.ciis.org.cn/english/2016-08/19/content_8975283.htm) (accessed Dec. 11, 2017)

<sup>17</sup>Li Tao, "China Focus: Leaders of Lancang-Mekong countries convene, China plans loans for infrastructure," *Xinhuanet*, [http://news.xinhuanet.com/english/2016-03/23/c\\_135216798.htm](http://news.xinhuanet.com/english/2016-03/23/c_135216798.htm) (accessed Dec. 11, 2017)

promote trade and investment; and facilitate business travel.<sup>18</sup> Those projects promote both hardware and software connectivity between Mekong riparian countries and lay a strong foundation for the promotion of regional trade where China has an advantage with its diverse and cheap products.

In terms of finance, China can promote the use of its currency in LMCM projects. China has promised \$1.54 billion in concessional loans and \$10 billion in credit lines for infrastructure project.<sup>19</sup> Chinese Premier Li Keqiang also called for the use of Chinese yuan in promoting sustainable development, production capacity cooperation, and poverty reduction.<sup>20</sup> As the major provider of financing for LMCM infrastructure and cross-border economic cooperation, China will have huge influence over the terms of loans and may request the use of Chinese yuan in those projects. In fact, China has been implementing steps since June 2009 to promote the international use of its renminbi. In July 2009, China started a pilot program using RMB for cross-border trade settlement in five domestic cities and for trade with Hong Kong, Macao, and ASEAN; the program expanded to 20 provinces and trade with other countries in 2010.<sup>21</sup>

In addition to Premier Li's call for the use of RMB, the Sanya Declaration also asks LMCM countries to support the operations of the AIIB and take advantage of AIIB loans.

**Complement implementation of the Belt and Road Initiative.** China sees Southeast Asia as part of its Belt and Road Initiative connecting China with Africa and Europe through Southeast Asia and South Asia. As stated in the Sanya Declaration, the LMCM encourages synergy between China's Belt and Road initiative and LMCM activities and projects.

Successful implementation of the LMCM could be used by China to show the world China's goodwill and capacity in addressing global issues. Through its initiatives, China is showing leadership in the region with new rules being set by China. In its effort to establish the LMCM, China is proposing 45 early harvest projects in all five areas of cooperation within LMCM to be completed by the end of 2017. This allows China to highlight key features of the LMCM with its project-oriented approach. By working with high-ranking government officials, projects are expected to be implemented quicker than if they were being pushed up from the grassroots. More importantly, the LMCM could impose China's cooperation platform in the Mekong sub-region to compete with existing ones dominated by China's rivals, such as Japan's Greater Mekong Sub-region Economic Cooperation Program, the United States' Lower Mekong Initiative, or the Mekong River Commission.

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<sup>18</sup>"Sanya Declaration," [http://www.fmprc.gov.cn/mfa\\_eng/wjdt\\_665385/2649\\_665393/t1350039.shtml](http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/2649_665393/t1350039.shtml), (accessed Dec. 11, 2017).

<sup>19</sup>"Lancang-Mekong cooperation enriches countries along the river," *Xinhuanet*, [http://www.chinadaily.com.cn/china/2016-03/26/content\\_24114124.htm](http://www.chinadaily.com.cn/china/2016-03/26/content_24114124.htm) (accessed Dec. 11, 2017).

<sup>20</sup>Li Tao, "China Focus: Leaders of Lancang-Mekong countries convene, China plans loans for infrastructure," *Xinhuanet*, [http://news.xinhuanet.com/english/2016-03/23/c\\_135216798.htm](http://news.xinhuanet.com/english/2016-03/23/c_135216798.htm) (accessed Dec. 11, 2017).

<sup>21</sup>Zhai Fan, "RMB Internationalization and China's Financial Liberalization," *OECD*, <https://www.oecd.org/finance/financial-markets/49700722.pdf> (accessed Dec. 11, 2017).

**Repair China's image in the region.** China and some Southeast Asian countries have disputes over territorial claims in the South China Sea. Tensions have escalated in recent years mostly due to China's aggressive actions in the disputed areas. Some key moments in the disputes were the standoff between China and the Philippines over Scarborough Shoal in 2012 and China's moving a giant oil rig into a disputed area in Vietnam's exclusive economic zone in 2014. A more general feature of the tension has been China's aggressive program to build artificial islands in disputed regions of the South China Sea. ASEAN has consistently expressed its concern over the disputes and land reclamation in the South China Sea though it does not directly refer to China. Other international forums such as the G7 have also criticized China over this matter.

In continental Southeast Asia, China's insistence that it has the right to exploit water resources from the Mekong river without consulting with downstream states has also created tension with lower Mekong countries. Those projects are blamed for adverse impacts on other states, especially in dry season.

These disputes undermine China's good neighbor policy, especially as China has tried to expand its influence with its Belt and Road Initiative (BRI) and the AIIB. China has engaged in benign actions such as agreeing to begin negotiations on a Code of Conduct with ASEAN on the South China Sea, releasing water from its dam on the Mekong to ease drought conditions in downstream areas, and committing to cooperate and provide loans for less-developed downstream countries on the Mekong.

The effort to use the LMCM to repair China's image is reflected in the statement of China's Ministry of Foreign Affairs' spokesperson that the "LMCM sends a strong signal to the world community demonstrating China's desire to maintain a constructive dialogue and create mechanisms of cooperation with Mekong River countries and to facilitate the alleviation of tension between the People's Republic of China and Vietnam."<sup>22</sup>

China has sought to institutionalize the LMCM, making it the most comprehensive among cooperation mechanisms in the region. China has set up its LMCM secretariat, which is based at China's Ministry of Foreign Affairs and reached an agreement with other LMCM members that they should set up similar coordinating institutions in the first half of 2017.<sup>23</sup>

China's desire to quickly institutionalize the LMCM is also reflected in the draft five-year plan of action for 2018-2022, under which China proposes establishment of the international Lancang-Mekong secretariat, which will coordinate overall cooperation within LMCM. Although China and other riparian countries have not finished setting up all the working groups in the initial five areas of cooperation, the plan of action proposes new sectors of cooperation and upgrading the working groups in place for the five initial sectors to senior official or ministerial levels.

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<sup>22</sup>Vladimir Terekhov, "About Lancang-Mekong Cooperation Meeting," *New Eastern Outlook*, <https://journal-neo.org/2016/04/11/about-lancang-mekong-cooperation-meeting/> (accessed Dec. 11, 2017).

<sup>23</sup>Wang Qingyun, "China launches Lancang-Mekong body with five countries," *China Daily*, [http://wap.chinadaily.com.cn/2017-03/10/content\\_28510599.htm](http://wap.chinadaily.com.cn/2017-03/10/content_28510599.htm), accessed 21 Dec. 2017)

In the track II channel, China has pushed for the formation of a think-tank network between LMC countries: the Global Center for Mekong Studies. China also proposed other institutions such as the Lancang–Mekong water resources cooperation center, the Lancang–Mekong environmental cooperation center and the Lancang–Mekong river space information cooperation center.

### **The Lancang–Mekong Cooperation Mechanism and the interests of other Mekong countries**

Though the LMCM was created based on the agreement of all six riparian states, implementation has been pushed by China based on its strategy and resources. Other Mekong countries have participated in the LMCM with no initial strategy, but they all see explicit benefits to be gained from the mechanism's projects. Those benefits mainly lie in opportunities to attract resources for national development based on China's promise of a combined loan and credit package worth \$11.5 billion for Mekong development projects ranging from railways to industrial parks. China has also offered \$200 million to fund poverty alleviation initiatives and another \$300 million for regional cooperation and setting up a water resource center over the next five years.<sup>24</sup>

The LMCM's emphasis on poverty reduction serves the national development strategies of Myanmar, Laos, and Cambodia as they all put poverty reduction as a top priority and are the least developed countries in the region. For Myanmar, improvement in the quality of life of the people was one of four priorities for the newly elected government.<sup>25</sup> In Laos, poverty reduction has been its top national development goal since 1996.<sup>26</sup> Cambodia made poverty reduction a national priority in 2002; since then, it has been implementing a poverty reduction program as part of its national development strategy.<sup>27</sup>

Apart from that common interest, the LMCM also fits some special needs of downstream countries given their different levels of development and alternative political calculations.

**Myanmar.** The newly elected government's economic vision for the country seeks to achieve inclusive and sustainable economic development with national reconciliation, equitable development, protection of natural resources, and job creation as overarching goals.<sup>28</sup> Specific priorities listed in the vision such as improving infrastructure and

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<sup>24</sup>ThitinanPongsudhirak, "China's its own worst enemy in regional relations," *East Asia Forum*, <http://www.eastasiaforum.org/2016/03/31/chinas-its-own-worst-enemy-in-regional-relations/> (accessed Dec. 11, 2017).

<sup>25</sup>"Myanmar 2017–2021: Building the foundations for inclusive growth," ADB, <https://www.adb.org/sites/default/files/institutional-document/237161/cps-mya-2017-2021.pdf> (accessed Dec. 11, 2017).

<sup>26</sup>"Hydropower in Lao PDR," *Powering Progress*, <http://www.poweringprogress.org/new/2-uncategorised/3-hydropower-in-lao-pdr> (accessed December 11 2017).

<sup>27</sup>"Cambodia's National Strategic Development Plan 2014-2018," [http://cdc-crdp.gov.kh/cdc/documents/NSDP\\_2014-2018.pdf](http://cdc-crdp.gov.kh/cdc/documents/NSDP_2014-2018.pdf), (accessed Dec. 11. 2017).

<sup>28</sup>"Myanmar 2017–2021: Building the foundations for inclusive growth," ADB, <https://www.adb.org/sites/default/files/institutional-document/237161/cps-mya-2017-2021.pdf> (accessed Dec. 11, 2017).

developing the agriculture sector are highly compatible with the LMCM as it includes connectivity, agriculture, and poverty reduction as priorities. Moreover, in the transition period from the military-backed regime to a democratically elected one, the Myanmar government needs a peaceful and stable external environment to secure successful nation building. In this process, according to the OECD, the key to realizing Myanmar's potential is its ability to mobilize and allocate financial resources for the implementation of the country's economic development. As estimated, it is necessary for Myanmar to increase capital investment from 21 percent to 28 percent currently and from 30 to 40 percent of its total GDP by 2035.<sup>29</sup>

**Thailand.** Thailand sees the LMCM as an opportunity to promote a just society by strengthening the agricultural sector to ensure food and energy security as set out in its national economic and social development plan released in 2012.<sup>30</sup> The plan notes that Thailand's northeastern region has the lowest average income compared to other regions and the agriculture sector in this region is less productive. The LMCM, which give priority to cooperation in poverty reduction and agricultural development, serves Thailand's strategy in developing its northeastern region.

Moreover, Thailand's national development plan seeks to create regional connectivity for social and economic stability. This strategy aims to sustain the country's competitiveness in the global market by engaging Thailand's neighbors, which are enjoying higher economic growth and attracting the attention of the major powers. For example, the US, China, and Japan are promoting connectivity in the region through strategies such as the Lower Mekong Initiative, railroad connectivity, and the GMS Economic Development Program, respectively. Thailand also sees regional connectivity as means to promote its economic and social security. To implement this strategy, Thailand has decided to be open to newly established cooperation mechanisms; it has joined the Asia-Middle East Dialogue and is considering participation in the Trans-Pacific Partnership (TPP). That vision was also the basis for Thailand's promotion of its own Initiative on Sustainable Development of Lancang-Mekong sub-region, which was used by China as the basis for the LMCM.

The LMCM could also benefit Thailand in that the LMCM, which is based on consensus and voluntarism, would not require Thailand to notify and seek approval for water diversion projects on the Mekong. This is in contrast with the MRC, which condemned Thailand for not notifying other MRC members about its water diversion projects. In response to the criticism, Thailand had to explain that its projects only took a small amount of water that would not impact current water levels.<sup>31</sup>

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<sup>29</sup>OECD Development Center, *Multi-dimensional Review of Myanmar: Volume 2. In-depth Analysis and Recommendations*, (Paris: OECD Publishing, 2015), <http://www.oecd-ilibrary.org/eres.library.manoa.hawaii.edu/docserver/download/4114071ec007.pdf?expires=1509310712&id=id&accname=ocid56019749&checksum=4B1895A4C25DB02850578953F922F73F> (accessed Dec. 11, 2017).

<sup>30</sup> "Thailand's National Development Strategy 2012 – 2016," [http://www.nesdb.go.th/nesdb\\_en/ewt\\_dl\\_link.php?nid=3786](http://www.nesdb.go.th/nesdb_en/ewt_dl_link.php?nid=3786), (accessed Dec. 11, 2017).

<sup>31</sup>Igor Kossov, "Mekong diversion under way in Thailand," *Phnompenhpost*, <http://www.phnompenhpost.com/national/mekong-diversion-under-way-thailand> (accessed Dec. 11, 2017).

**Laos.** Laos' plan to develop hydropower, which it sees as the major way to quickly get millions of its population out of poverty because all decisions made within LMCM will be by consensus, is consistent with the goals of the LMCM.<sup>32</sup> Laos is expected to receive 70 percent of the total \$2.6 billion per year in energy export revenue if all the mainstream dams are put into operation.<sup>33</sup>

The connectivity cooperation in the LMCM, especially China's strategy to connect Yunnan province with Southeast Asia, could greatly assist Laos in overcoming its limitation as a land-locked country given the Lao government's determination to promote the perception of the country as a land bridge that could provide direct overland transport routes between seaports of neighboring countries.<sup>34</sup> One major connectivity project proposed by China is a rail network, including a high-speed train connecting Yunnan province with Laos, Thailand, Malaysia, and Singapore. The rail line connecting Yunnan to Vientiane is worth \$7.2 billion, equivalent to 75 percent of Laos' GDP. As part of the plan to promote connectivity and economic development, Laos and China signed the Mohan-Boten Cross-border Economic Cooperation Zone Common General Plan in 2015. The two countries also plan to jointly develop the Sayetth Development Zone in Laos' territory.

Income from the hydropower projects for poverty reduction and connectivity with its neighbor support Laos' strategy to graduate from the list of least developed countries by 2020 and to build a foundation for industrialization and modernization.

**Cambodia.** Besides its interest in poverty reduction, participation in the LMCM gives Cambodia the opportunity to strengthen its position vis-a-vis its two neighbors, Thailand and Vietnam. Recently, Cambodian cooperation with China has intensified with China becoming the number one foreign investor and development assistance provider in the country. Between 2011 and 2015, China provided the total amount of \$5 billion in loans and investment for Cambodia, accounting for around 70 percent of total investment in the country.<sup>35</sup>

In addition, close relations with China, through multilateral mechanisms like the LMCM, give Cambodia a hedge against Western criticism of Cambodia's suppression of opposition factions and its poor record on human rights, which has reduced development assistance from the West.

**Vietnam.** Vietnam's national development strategy is laid out in its 2011-2020 Socio-Economic Development Strategy, and highlights the importance of structural reforms, environmental sustainability, and social equity. The strategy identifies promotion of further infrastructure development as one of the breakthrough issues for the country's

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<sup>32</sup>"Hydropower in Lao PDR," *Powering Progress*, <http://www.poweringprogress.org/new/2-uncategorised/3-hydropower-in-lao-pdr> (accessed Dec. 11, 2017).

<sup>33</sup>Nguyen KhacGiang, "New Rule-based Order Needed to Save the Mekong," *East Asia Forum*, <http://www.eastasiaforum.org/2016/03/29/new-rule-based-order-needed-to-save-the-mekong/> Dec. 11, 2017).

<sup>34</sup>Gretchen A. Kunze and V. Bruce J. Tolentino, "In Laos: Land-linked, not Land-locked," *Asia Foundation*, <https://asiafoundation.org/2008/08/27/in-laos-land-linked-not-land-locked/> (accessed Dec. 11, 2017).

<sup>35</sup>"Why Cambodia has cosied up to China," *The Economist*, <https://www.economist.com/news/asia/21715010-and-why-it-worries-cambodias-neighbours-why-cambodia-has-cosied-up-china> (accessed Dec. 11, 2017).

development.<sup>36</sup> In this regard, the LMCM mostly benefits Vietnam in term of connectivity cooperation. However, the country is also concerned about joint infrastructure projects with China as experience indicates huge problems with these projects such as rising cost, delay, labor safety, and project quality.

In political terms, Vietnam sees the LMCM as new channel to cooperate with China to promote mutual trust and mitigate tensions from conflicts in the South China Sea. Vietnam also hopes to use the LMCM to voice its concern over upstream water exploitation projects. The stated purposes and priorities of the LMCM mostly fit the development needs of the sub-region, including connectivity, poverty reduction, and agriculture development. This explains why all these Southeast Asian states have joined the initiative. However, downstream Mekong countries show some reluctance to fully participate in this China-led mechanism. For example, at the end of July 2017, Thailand, Myanmar, and Vietnam had not set up their national LMCM secretariats even though the agreed deadline was the first half of 2017. Also until the end of July 2017, some Mekong downstream countries still disagreed over the concept papers and principles for some working groups. This hesitation is based on concerns over risks associated with LMCM projects.

### **Risks for regional security and development**

With the LMCM still in its early stage, no big projects have started except for the 45 early harvest projects. Those projects are mostly exchange and training programs. Other projects establish new institutions to coordinate cooperation activities between member countries. Based on the analysis of China's strategies and how LMCM is relevant to the development needs of other riparian countries, this section identifies risks associated with the LMCM by looking at what has been proposed and taking into account experience with China's implementation of previous investment projects.

The LMCM has created a sense of cooperation between sub-regional countries as it maps out multi-layer cooperation in areas that meet the development needs of Mekong riparian countries. If fully implemented, the LMCM will greatly promote peace, security and prosperity in the region.

However, by looking at China's strategy behind the creation of LMC, it is clear that the initiative goes beyond promoting cooperation with downstream countries to address China's own development needs and to expand its influence in the region. These factors present other member countries with the risk of economic dependence and could create negative social and environmental impacts. At the same time, the major problem of water exploitation will remain unaddressed.

**Economic dependence.** To address excess capacity, Chinese firms are encouraged to invest in Southeast Asia. This investment is welcome in less developed Mekong countries, such as Laos and Cambodia. However, given the size of Chinese firms and their technical capacity,

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<sup>36</sup>“Vietnam Overview,” *World Bank*, <http://www.worldbank.org/en/country/vietnam/overview> (accessed Dec. 11, 2017).

they could dominate those countries' domestic markets and control important manufacturing sectors.

Further, most investment from China is resource-seeking and could negatively impact the economies and further widen the development gap between China and host countries. Because resource-seeking investment projects are mostly funded by China and natural resources will be exported to China at cheap prices, most economic benefits go to China. Meanwhile, economic growth brought about by exploiting natural resources could impose on local economies "the resource curse" where economic growth is dependent on the exploitation of natural resources and other economic sectors lose their comparative advantage due to unbalanced investment and an unfavorable exchange rate created by huge revenues from natural resource exports.<sup>37</sup> The resource curse has negative and long-lasting impacts on an economy. Thus, instead of promoting sustainable economic development, Chinese investment may do more harm than good for local economies, furthering the development gap between Mekong countries and China.

Second, in an effort to internationalize its currency, China is promoting the use of the yuan in transactions with Mekong countries. The more the yuan is used in daily transactions, the higher the possibility of the other Mekong states losing independence in their monetary policies. This scenario has increased now that China is the leading trade and investment partner of Mekong riparian countries. Recall that China proposed the use of its currency within the LMCM in the LMCM's action plan for 2018-2022. To date, only Cambodia has allowed the use of the yuan in cross-border trade and investment.<sup>38</sup>

Third, countries receiving infrastructure projects funded by China could be trapped by debts owed to China. This has happened with previous infrastructure projects funded by China when projects did not meet deadlines and construction costs were higher than planned. In several cases, the host countries could not use the projects to generate income to pay the debt owed to Chinese investors. As a result, the countries could be forced to make compromises for debt relief. For example, Sri Lanka recently had to propose selling its airport and seaport to China after it could not pay back its debt.<sup>39</sup> Cambodia gave Chinese companies new contracts in exchange for the cancellation of \$90 million in debt.<sup>40</sup>

Economic dependence may also lead to political pressure as China has used economic tools to pressure neighbor countries in cases of bilateral tensions. Given their small economic size and dependence on China, Mekong countries would be losers if there is a disruption of trade and other economic activities with China. China has, several times, pressured other countries with such tools as in the cases of restriction on banana imports

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<sup>37</sup>Are natural resources a blessing or a curse for developing countries?, *The Guardian*, <https://www.theguardian.com/global-development/2012/oct/25/natural-resources-blessing-curse-developing-countries> (accessed Dec. 11, 2017).

<sup>38</sup>Sok Chan, "NBC calls for cross-border trade in yuan and riel," *Khmertimeskh*, <http://www.khmertimeskh.com/5087596/nbc-calls-cross-border-trade-yuan-riel/> (accessed Dec. 11, 2017).

<sup>39</sup>Wade Shepard, "China Tells Sri Lanka: We Want Our Money, Not Your Empty Airport," *Forbes*, <https://www.forbes.com/sites/wadeshepard/2016/07/31/china-to-sri-lanka-we-want-our-money-not-your-empty-airport/#16705bb81beb> (accessed Dec. 11, 2017).

<sup>40</sup>Brahma Chellaney, "China's debt-trap Diplomacy," *Khmertimeskh*, <http://www.khmertimeskh.com/news/34692/china---s-debt-trap-diplomacy/> (accessed Dec. 11, 2017).

from the Philippines following the standoff between these two countries over control of Scarborough Shoal or the stoppage of rare earth exports to Japan after rising tensions over ownership of the Senkaku/Diaoyu Islands. The most recent example is that China refused to provide hydrological data on the Brahmaputra Riverto India after India confronted China in the disputed border between China and Nepal.<sup>41</sup>

Economic dependence on China by any Mekong country could indirectly affect the wider Southeast Asian region as all downstream Mekong countries are members of ASEAN and other related ASEAN-driven mechanisms. China could pressure any dependent country to advance Beijing's views on the agenda or decision-making of ASEAN. Given the consensus principle of ASEAN, a single country can block a joint statement, agenda or decision of ASEAN, preventing the organization from addressing regional issues, including current disputes with China in the South China Sea.

**Social-environmental problems.** The socio-environmental impacts are mostly due to China's interest in transferring outdated technology as part of its capacity cooperation. As stated in the Sanya Declaration, Mekong countries see industrial capacity as a priority. Since China is the primary benefactor in this area, it has the biggest say in deciding what technology is being transferred. The problem is that the technology being transferred to other Mekong riparian states could be environmentally unfriendly and could be restricted in China. The social risks associated with improved connectivity between China and other Mekong riparian countries is that Chinese-made products that are more competitive than those locally produced will be easily delivered to Mekong countries, threatening to compete with locally made goods. As a result, local companies may lose in their own market and local workers could lose their jobs. In some investment projects, Chinese investors bring their own workers instead of employing local labor. This could lead to anti-Chinese sentiment in Mekong countries.

**Water use issues remain unaddressed.** Although LMCM covers water resource management but it is just one of five cooperation fields. Since China is the most upstream country and the most influential state in the LMCM, it is likely to control how LMCM countries prioritize the issue of water management. Currently, China does not give top priority to water issue. In fact, China's top priority is industrial capacity cooperation, because China has huge interest and advantages. This prioritization is reflected in a statement by the Chinese foreign minister that the LMCM should discuss easy issues first, implying that water resource management, the most complicated problem, is not going to be addressed in the near- or medium-term.<sup>42</sup>

The inclusion of water resource management in the LMCM appears to be a tactic to involve other Mekong countries in the China-led mechanism and ease criticism of China's unilateral dam building. The LMCM has offered in the Sanya Declaration some important water cooperation issues such as establishing a center on Lancang-Mekong water resources

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<sup>41</sup>Brahma Chellaney, "A new front in Asia's water war," *ASPI Strategist*, <https://www.aspistrategist.org.au/a-new-front-in-asias-water-war/> (accessed Dec. 11, 2017).

<sup>42</sup>Sebastian Biba, "China drives water cooperation with Mekong countries," *The Third Pole*, <https://www.thethirdpole.net/2016/02/01/china-drives-water-cooperation-with-mekong-countries/> (accessed Dec. 11, 2017).

cooperation as a platform for riparian countries to strengthen comprehensive cooperation in technical exchanges, capacity building, drought and flood management, data and information sharing, conducting joint research and analysis related to Mekong river resources.<sup>43</sup> However, the amount of cooperation is not certain since China has avoided mentioning the core problem for the Mekong basin, which is a binding agreement on the notification, consultation and approval of water exploitation projects. Without addressing major issues concerning water exploitation on the Mekong early in the process, it is possible that each Mekong country will proceed with its own water exploitation projects in an uncoordinated way.

### **Recommendations for Mekong downstream countries**

Given that the LMCM does bring some benefits to Mekong downstream countries but also poses possible risks, this section recommends strategies for Mekong riparian states that would minimize the risks to national and regional development and security. This section proposes that Southeast Asian countries should adopt an active and cautious approach to implementing the LMCM projects. Mekong downstream countries can proactively put forward their own cooperation projects in areas directly related to their national development, implement a pilot program to assess the real impacts of LMCM projects, and insist on the need to address the water management issue.

**Participate proactively in deciding the implementation of LMCM.** The Sanya Declaration states that the LMCM is based on consensus, equality, mutual consultation and coordination, voluntarism, common contribution, and shared benefits, giving equal status for Mekong countries to work together on the implementation of LMCM. Therefore, downstream states should actively put forward their own cooperation proposals.

- Propose an agenda based on national and regional developmental needs. In the context that lower basin countries are still at relatively low levels of development, priorities within LMCM should address downstream countries' internal development issues such as poverty reduction, agricultural development, and infrastructure improvement.
- Proceed with LMCM cooperation while recognizing the need to protect their long-term national interests and independence. In response to China's efforts under the current five-year plan to expand yuan transactions, Mekong countries should insist on limiting use of the yuan on a case-by-case basis to ensure independent monetary policies are maintained. In addition, the planned expansion of cooperation to new sectors and the upgrade of working groups to more senior levels should be implemented gradually, after determining the efficiency of the current working groups in five priority areas.
- Continue cooperation with other external partners to avoid becoming too dependent on Chinese funds and technology. Other external partners have been engaging with the Mekong's downstream countries for a long time. For example, Japan is a long-time and leading partner that provides significant funding and investment for major

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<sup>43</sup>"Sanya Declaration," [http://www.fmprc.gov.cn/mfa\\_eng/wjdt\\_665385/2649\\_665393/t1350039.shtml](http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/2649_665393/t1350039.shtml), (accessed Dec. 11, 2017).

infrastructure project in the region. In May 2016, Japan announced a new program of \$7 billion to support infrastructure development in lower Mekong sub-region.<sup>44</sup> Cooperation with other partners is also important for dealing with water use issues so that downstream states can plan their actions in dealing with changes in water flow. The US has been sharing its satellite images of the Mekong and geospatial technologies, which help predict changes in water flow throughout the year.

**Adopt a gradual, multi-stakeholder approach to implementing the LMCM projects.**

Mekong countries should adopt a gradual, multi-stakeholder approach to implementing the LMCM. Before approving big programs, Mekong countries should implement pilot projects in all cooperation sectors. The pilot projects should evaluate all environmental, socio-cultural, political-security, and economic aspects of the programs. Multiple stakeholders, including local residents, contractors, technical experts, and other social groups should be involved in all stages of implementation, including the feasibility study, supervision, and post-project assessment. Based on the assessment of the pilot projects, the LMCM could develop specific criteria for approving and implementing future cooperation projects especially in connectivity, cross-border economic cooperation, and production capacity.

- Establish regulations that stipulate requirements for the employment of local laborers and use of local resources.
- Apply strict international standards on environmental issues such as carbon emissions, treatment of industrial waste, soil erosion, etc.
- Establish regulations to prevent contractors from arbitrarily increasing construction costs.
- Develop a planning framework that allows local communities, NGOs, and think-tanks to participate in the feasibility studies to comprehensively assess the impact of investment and infrastructure projects, as other partners have done. For example, Japan's ODA projects in Southeast Asia are usually done in conjunction with think-tanks and NGOs to gain a better understanding of the interests and needs of the local communities.<sup>45</sup>
- Develop effective mechanisms that involve all stakeholders in monitoring the implementation of cooperation projects.

**Promote cooperation in water use.** As the water management issue in the Mekong basin remains a prominent concern for security and development in the sub-region, riparian countries can take advantage of China's involvement in the LMCM to promote cooperation in water management. Promoting coordination between countries in drought and flood management and encouraging China to expand data and information sharing on hydrology to include the whole year should be given top priority in LMCM projects. Currently, China only shares hydrological information in the wet season.

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<sup>44</sup>Amy Sawitta Lefevre, "Japan to support Mekong countries with \$7 billion over three years," *Reuters*, <https://www.reuters.com/article/us-thailand-japan/japan-to-support-mekong-countries-with-7-billion-over-three-years-idUSKCN0XT0MK>, (accessed Dec. 11 2017).

<sup>45</sup>GatraPriyandita and TrissiaWijaya, "China's Southeast Asia Gambit," *The Diplomat*, <https://thediplomat.com/2017/05/chinas-southeast-asia-gambit/> (accessed Dec. 11, 2017).

Smaller countries should use the Sanya Declaration's basic principles of consensus, mutual consultation and coordination, voluntarism, common contribution and shared benefits to ensure water utilization concerns are addressed. They should ask China to compromise on the water issues in exchange for approval of cooperation projects in other sectors.

## **Conclusion**

The Mekong countries are facing development needs such as poverty reduction, agriculture development, and infrastructure improvement. They are also interested in promoting mutual trust and addressing water resource management in the region. Given China's interest in working with the downstream countries, the LMCM is a good opportunity to address these issues in a comprehensive manner. However, to make the LMCM a true platform for mutual trust and prosperity, the Mekong countries must ensure the mechanism produces concrete and sustainable outcomes. This means the LMCM should be implemented through a gradual, multi-stakeholders approach. Southeast Asian countries should insist on promoting cooperation in sectors related to their national development priorities, including the water management issue. Moreover, as there have been many other cooperation mechanisms developed in the region, the LMCM projects should be designed to complement rather than compete with existing projects to avoid overlap, maximize resource utilization, and prevent over-dependence on China.

The successful implementation of LMCM with concrete and sustainable outcomes not only contributes to the prosperity and development of the Mekong basin but also serves China's interest in developing its economy and expanding its influence in the region. An LMCM with debt, dependence, and other negative socio-economic consequences would damage China's image, creating more obstacles to China's goals of moving closer to making greater contributions to mankind, as stated by its president at the recent 19<sup>th</sup> Party Congress.

## About the Author

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