Chapter: II

Theory and Review of Literature

2.1 The Concept of Economic Development

Economic development is principally characterized by increasing gross domestic product GDP in countries and GDP per capita (Rautakivi, 2012) and it mean the distribution of income (Coleman& Nixon, 1985). Moreover, the idea and process of economic development contains the deliberate manipulation of forces within the control of humans to alter economic outcomes instead of accepting what nature provides by way of sustenance as inevitable (Saylor Foundation, 2015).

Economic development ideally refers to the sustained, concerted actions of policymakers and communities that promote the standard of living and economic health of specific area and also economic development involves the process and policies by which a nation improves the economic, and political, development of human capital, increasing the literacy ratio, improve important infrastructure, improvement of health and safety and others areas that aims at increasing the general welfare of the citizens. Economic development can also be referred to as the quantitative and qualitative change in an existing economy (Todaro, 2011).

The terms of Economic development and economic growth are used interchangeably but there is a very big difference between then. Economic growth has traditionally been attributed to the accumulation of human and physical capital, and increased productivity arising from technological innovation (R.E Lucas, 1988). In transaction, economic growth also can be viewed as such category of economic development (strange & Bayley, 2008). On the other hand, economic development is a policy intervention endeavor with aims of economic and social well-being of people.

In the traditional point of view, "Economic Development is a branch of economics which deals with causes and cures of mass poverty", and it mean the continuous increase in real income of a country over a long period of time and requires political leadership and the control, integration and, coordination of financial and personnel management at a national level with conventional development efforts (Cochrane, 1986).

2.2 Theories of Economic Growth

Growth theory traditionally assumed the existence of an aggregate production function, whose existence and properties are closely tied to the assumption of optimal resource allocation within each economy (Abhijit V. Banerjee and Esther Duflo, 2004). Interest in the study of economic growth has experienced remarkable ups and downs in the history of economic. Economic growth is the increase in a nation's standard of living over time and it is typically measured as the change in per capital Gross Domestic Product (GDP).

First, the theory of classical in economic growth directly derived from a philosophical concern with the possibilities of progress, explained this phenomenon through a theory based upon the class structure of capitalist economy, and developed by Thomas Mun (1571-1641), William Petty (1623-1687), David Hume (1711-1776), Adam Smith (1723- 1790), David Ricardo (1772 - 1823) Jean Baptiste Say (1767-1832), William Nassau Senior (1790-1864), and John Stuart Mill (1806-1873). They identify three classes, workers, capitalist and landowners, which have their own specific role in the economic process. In this theory, workers own labor and sell it on the labor market for a subsistence wage. Landowner rent their land to capitalists in order to obtain rent. Then, capitalists own the produced means of production and organize production by employing labor and renting land.

The principle of the classical theory is generally self-regulating and maintain that the economy is always capable of achieving the natural level of real GDP or output, which is the level of real GDP that is obtained when the economy's resources are fully employed. In contrast to classical economics, Keynesian economics supports policies such as deficit spending, control of the money supply, and a graduated income tax to counter recession and income inequality. Most classical economists reject these ideas.

In this classical economic, there are two kinds of models namely the Ricardian model and the Smithian and Marxian tradition. First, the model of Ricardian emphasizes the tendency towards the stationary state due to existence of scare natural resource and second, the models of Smithian and Marxian emphasize the progressive nature of economic growth. Both of them are commonly interpreted as being characterized by the assumptions that capital and labor are employed in fixed proportions, capitalists anticipate wages that are entirely consumed by labors landowner and capitalists invest all profits.

Second, Neoclassical Economics, the word neo meaning “new” is the name given to an economic theory and the term classical refers to work done by a group of economists developed at the end of the 19^{th} and the beginning of the 20^{th} Century in Europe. The main contributors to this theory were Leon Walras (1834-1910), Alfred Marshall (1842-1924 and Vilfredo Pareto (1848-1923). The theory tries to explain origins of growth employing a production function that expresses relationship between increases in output and in factor inputs (capital, labor, natural resources and technology).

Aggregate Production Faction:

$$Y = A\ K^{a}\ L\ (^{1-a})$$

Where Y = Gross Domestic Product,

K = Stock of Capital (Human Capital and Physical Capital),

L = Labor,

A = Represents the Productivity of Labor

Growth Accounting Formula:

$$\frac{\Delta y}{y} = \frac{\Delta A}{yA} + a\frac{\Delta K}{K} + (1 - a)\frac{\Delta L}{yL} +$$

Neoclassical economists point out that other factors besides the ones in the production function may exist in the producing process. Each factor has a certain effect on growth of output and these factors correlate. Of these factors, capital is considered as the most important because it is associated with technical and scientific advances while labor is seen as the most essential resource for economic growth.

Basically, neoclassical economists focused on the market to find a way out for the developing countries. Policies of liberalization, stabilization and privatization therefore become the central elements of the national development agenda. Foreign trade, private international investments and foreign aid flowing into the developing countries are expected to accelerate economic efficiency and economic growth of these countries.

Third, in the mid-1980s, endogenous or new growth theory was to explain the poor performance of many less developed nations, which have implemented policies as prescribed in neoclassical theories and it is developed by Paul Romer (1986) and Robert

Lucas (1988). The growth of endogenous theory linked the technological change to the production of knowledge and the new growth theory emphasizes that economic growth results from increasing returns to the use of knowledge rather than labor and capital. Therefore, overall there are constant returns to capital, and economies never reach a steady state. Growth does not slow as capital accumulates, but the rate of growth depends on the types of capital a country invests in. Research done in this area has focused on what increases human capital or technological change.

Four, Roy Harrod in England and Evsay Domar in the U.S. developed a new economic growth in the 1940s that considered increases in savings and decreases in ICOR are preconditions for economic growth. In fact, however, economic growth does not necessarily comes from increases in investment; and ineffective investment produces no growth. When investment is effective, increases in savings can only create a short -term economic growth.

These arguments help Robert Solow develop a new model of his name in 1956 based on the neoclassical economic theory. While Harrod-Domar model pays attention to the role of capital in form of savings and investment in economic growth, the Solow model includes labor and technical advances in the function of economic growth. The latter is considered by Solow as decisive factor of both long- and short-term economic growth.

Five, Modern economists emphasize economic equilibrium in Keynesian model. The equilibrium does not necessarily exist in the level of potential output but at a point lower than this level. Under normal conditions, unemployment and inflation may exist. Natural unemployment rate and acceptable inflation rate should be identified. The economic equilibrium is determined by balance between aggregate supply and demand.

Usually modern of economic growth pay less and less attention to natural resources or land as variables of the function of economic growth. They consider land as a fixed factor while the role of natural resources becomes less important. Such factors as land or natural resources could be included in capital (K).

Thus, three factors that affect directly the economic growth are capital, labor and Total Factor Productivity. In this modern of economic growth, Capital and labor are considered as physical or extensive factors whose effects on economic growth can be quantified. Total Factor Productivity reflects efficiency of technical, institutional, or cultural factors and is considered as quality of economic growth, or an intensive factor of growth.

Concisely economic growth is driven by four primary factor what are physical capital that is needed to produce and goods and services include plant and machinery for manufactures and computer equipment in many offices, human capital which is an economist's term for the knowledge and skills that workers acquire through education, training and work experience, natural resources included energy source such as coal, oil and gas as well as renewable resource such as tree but also sun, wind and waves, and improvements in technology (knowledge) that is most important to create innovation and help us become efficient at producing goods and services. Other economists have highlighted the importance of strong institutions and the rule of law as an ingredient for growth.

2.3 Experiences of ASEAN Countries

2.3.1 Vietnam

Viet Nam's political and economic system reform (Doi Moi) launched in 1986 have transformed the country from one of the poorest countries in the world to a lower middle-income country and it's one of Asia's success stories and has also transforming from a centrally planned economy into a more market-oriented economy through gradual integration into the global trading and investment system. Moreover, liberalization of trade and foreign direct investment has been an integral part of the structural reforms that contributed to improved competitiveness and thus export-led growth.

Before the reform of political and economic (Doi Moi) policy, foreign trade in Vietnam was subject to central decision by planning authorities and could be carried out only by small number of state trading monopolies and Vietnam maintained system of multiple exchange rates with difference rates, for trade transactions within central plan, for invisible transactions, and for trade transaction outside the plan.

In 1987, the government of Vietnam has adopted the foreign investment law which was the first legal document that helped form the legal framework for the Vietnamese marked economy and the private Enterprise law and corporate law were introduced in 1991. The amended 1992 Constitution affirmed the existence and development of multi-sector economy under a market mechanism, including the foreign invested sector.

This was followed by the promulgation of a number of laws essential for the formation of the marked economy, including land law, tax law, Bankruptcy law, Environment law, and labor code which were designed to raise sufficient fiscal revenues to support critical infrastructure and human capital development while introducing elements of a modern tax system for a marked economy. As a result of these reforms, fiscal revenue increased from 13% of GDP in 1988 to 24% in 1994 and more than 80% of total domestic revenues by tax collection.

Since the establish of Doi Moi and until its WTO accession Viet Nam's growth rates were high owing principally to rising investment and vigorous exports. Viet Nam grew at an annual average rate of 6.3% (2007-12), albeit trending slowly downward for the last 5-6 years. The growth of economic for Viet Nam has been driven equally by the expansion of the export sector and strong domestic investment. It was supported by a generous economic stimulus package in 2009, while the recent slowdown has been the outcome of the slow pace of structural reforms that impeded TFP growth, the global financial crisis, and tighter macroeconomic policies adopted in 2011. Notwithstanding recent macroeconomic instability involving, a sharp rise and subsequent drop in inflation whose latest bouts were in 2008 (23%) and 2011 (18.6%), official unemployment remains low.

On the other hand, a key to success of Vietnam’s export-led growth strategy has highly depended on the adoption of a more flexible marked-oriented exchange system and a marked-oriented rate policy, which enable it to avoid the overvaluation of its currency and maintain it external competitiveness. Usually in transition economies, the Socio-Economic Development Strategy (SEDS) 2011-2020 gives attention to structural reforms, environmental sustainability, social equity, and emerging issues of macroeconomic stability. It defines three "breakthrough areas": (i) promoting human resources/skills development (particularly skills for modern industry and innovation), (ii) improving market institutions, and (iii) infrastructure development.

The Doi Moi process helped Vietnam rapidly escape hunger and poverty and lay the initial foundation for an industrialized economy, as well as maintaining a high growth rate and a relatively equal society and development of health care and education. Therefore, the Vietnam’s economy will develop continuously with encourage by government.

2.3.2 Cambodia

The Economy of Cambodia, one of the least developing countries, at present followings as open market system (Market Economy) and has seen rapid economic progress in the last decade. Cambodia's growth has driven by garments, construction, agriculture, and tourism since 2004. GDP climbed more than 7% per year between 2010 and 2013.

Cambodia has an open and liberal foreign investment regime with a relatively pro-investor legal and policy framework. Investment incentives available to foreign investors include 100% foreign ownership of companies, corporate tax holidays of up to eight years, 20 % corporate tax rate after the incentive period ends, duty-free import of capital goods, and no restrictions on capital repatriation.

In 1995, the government transformed the country’s economic system from a Planned Economy to its present market-driven system. Following those changes, growth was estimated at a value of 7% while inflation dropped from 26% in 1994 to only 6% in 1995. Imports increased due to the influx of foreign aid, and exports, particularly from the country’s garment industry, also increased.

In 1989, the State of Cambodia implemented reform policies that transformed the Cambodian economic system from a Command Economy to an open market one, with economic reform, private property rights were introduced and state-owned enterprises were privatized. Cambodia’s foreign policy focuses on establishing friendly borders with its neighbors (such as Thailand and Vietnam), as well as integrating itself into regional Association of South East Asian Nations (ASEAN) and global World Trade Organization (WTO) trading systems.

These policies triggered a growth in the economy, with its national Gross Domestic Product growing at an average of 6.1%, and since 1999. As a result, the Cambodian economy has continued to grow. The Cambodian Government is working with bilateral and multilateral donors, including the Asian Development Bank, the World Bank and International Monetary Fund, to address the country's many pressing needs; more than 50% of the government budget comes from donor assistance.

Currently, despite facing various challenges, Cambodia continues to attract investors because of its low wages, plentiful labor, proximity to Asian raw materials, and favorable tax treatment. Frequently, Cambodia has one of the most open economies in what is a generally very open economic region. Reported by Heritage Foundation's Index of Economic Freedom which is compiled annually Cambodia ranked 57.5 among 110 countries in 2015 in terms of economic freedom for doing business.

2.4 Relevant Researches

Myanmar country reported by Bertelsmann Stiftung's Transformation Index (2014), after two decades of direct military rule, six decades of civil war, and alienation from global community, the country has embarked on process of wide-reaching political and economic reform that were supported by liberal members of the parliament, allowing for a liberalization of authoritarian regime to take place .

And then Economically, Myanmar already makes the headlines as "Asia's next tiger" or next "rising star." However, it is doubtful whether the country will experience an investment boom aside from extractive industries. Showing already strong characteristics of a "resource curse," it depends on the willingness of the president to reinvest these incomes into social and health sectors, to rebuild infrastructure, the financial sector, agriculture, manufacturing and the like.

On the other hand, the country lacks much stipulation for investment (an educated workforce, infrastructure, energy, etc.). President U Thein Sein should address these issues, and spending on education should increase considerably. And then the government could also attempt to increase the incentives for exiles to return. The most challenging issue in Myanmar is strengthening human rights and the rule of the law, because there are preventing for reformist politicians and ethnic groups, and the economic recovery.

Myanmar: overview (2015) reported by The World Bank, Myanmar is going through important political transformation in its development path- from isolation and fragmentation to openness and integration to region and global. As the largest country in mainland Southeast Asia, Myanmar has one of the significant untapped agricultural potential and rich endowments of natural resource. Started in 2010, the government of Myanmar has embarked on an ambitious economic, political and governance reform program including to remove of economic distortions, such as floating the currency, new fiscal regulations to rationalize personal income tax and reduce consumption tax, liberalizing the telecommunications sector.

Myanmar's economic continues to grow at a strong pace on the back of reforms that are gradually opening up the space for investment. The economy of Myanmar estimated to grow at 8.5% in real terms in 2014/15, is driven largely by construction, continued rebound in manufacturing output, and the resulting expansion in the service sector under the government. Although growth of economic, Myanmar has various challenge for prospect of economic. Myanmar has the lowest life expectancy and the second-highest rate of infant and child mortality among the regional and Less than one-third of the population has access to the electricity grid, road density remains low, at 219.8 kilometers per 1,000 square kilometers of land area are still underdeveloped recently.

Myanmar: Trade policy review reported by World Trade Organization, Secretariat in 2014, after isolated from a largest part of the global economy for many years, Myanmar is reintegration into the international community reforming political and economic since 2011. Under the new government, Myanmar has embarked on a series of reforms in its macroeconomic policies. On 1 April 2012, the Central Bank of Myanmar restored a pegged exchange rate with a managed floating exchange rate for the national currency. Providing greater operational autonomy to the Central Bank and improving the monetary transmission mechanism, the new Central Bank Law was enacted on 11 July 2013.

In the Southeast Asia, Myanmar has large potential for growth, abundant natural resource, a young labor force, and proximity to a fast-growing dynamic economic region. Nevertheless, significant impediments remain to modernizing for economy and meeting the government's goal of "fostering inclusive broad-based growth and poverty reduction". These involve the lack of capacity and infrastructure.

Myanmar: Unlocking the Potential reported by ADB (Asian Development Bank) in 2014, Myanmar has embarked on a historic path of political and economic transformation and reform. Since 2011, the new government led by President U Thein Sein has adopted impressive reforms, focused initially on the political system to restore peace and achieve national unity and moving quickly to an economic and social reform program.

Started establishing basic regulatory structures and removing unnecessary hurdles to business and trade, providing legal foundation for foreign direct investment, improving essential public services, and addressing governance and corruption issues, Led by President U Thein Sein, the government has been announced its commitment to continuing reform, sustainable growth, and poverty reduction in the Framework for Economic and Social Reforms 2012–2015 and in other economic plans.

The reforms are already bearing fruit, with the economy growing 7% a year for the last two years and improvements in some social indicators. Foreign direct investment has begun to flow into the country, foreign exchange earnings are already substantial, and tourism is expanding rapidly.

Myanmar is well-known advantages-its strategic location, a youthful workforce, ample natural resources, and huge tourism potential-hold promise for the country to become one of the region's success stories. In his inaugural address, President U Thein Sein rightfully identified a raft of challenges.

For prospect of Myanmar economy, one of these is an urgent need for investment in physical and social infrastructure. Another is the need for strong, growth oriented development, led initially by agriculture and natural resources, and followed by manufacturing for domestic and export markets. The President also emphasized the importance of transparency, accountability, good governance and the rule of law; resolute action against corruption; and addressing the widening income gap between rich and poor.

A successfully integrated development policy framework for Myanmar will need to consider comprehensive development and reform planning and phasing. These include weak infrastructure, creating modern market and government institutions, human development, stronger regional integration, a clear focus on inclusive growth, and environmental protection.

On the other hand, the economy of Myanmar is forecast to post higher growth of 7.8% in both FY2014 (ending 31 March 2015) and FY2015, benefiting from rising investment and improved business confidence since 2011. Growth of Myanmar economy is supported by rising investment propelled by improved business confidence, commodity exports, rising production of natural gas, buoyant tourism, and by the government's ambitious structural reform program.

From the World Fact Book, CIA of point of view on Myanmar's economy, since 2011, the government has begun an economic overhaul aimed at attracting foreign investment and joining into the international community. In 2012, the government has started to reform of economic included establishing a managed float of Burmese kyat, in

2013, the law of banking operation system and corruption law in 2013. With relaxation of sanction by U.S.A. and Western, the economy accelerated in 2012 and 2013, having abundant natural resources, young labor force, and proximity to Asia’s dynamic economic.

On the other hand, the government should reform the revenue collection system and antiquated banking system. Modernizing and Opening the financial sector the government should maintained the success of economic accelerating agricultural and land reform.

Myanmar’s Economic Reform and Development: Prospects and Challenges (2013) written by Son Qingrun, the future of Myanmar’s economic reform and development seems bright, but the reality is that economic reform has only just begun and the country’s process of reform and development will be an arduous one full of challenges. As a result, many international investors are still hesitant regarding the results of the new round of reform under the government.

Nevertheless, Myanmar should take note of challenges and carefully overcome the difficulties ahead. If Myanmar will have to make maintained and concrete efforts, it is to become Asia’s next economic star in the world quickly. Myanmar is emerging from five decades of isolation – both economically and politically. With its rich natural resources and strategic location, the country shows good potential for growth.

Under the new government led by president U Thein Sein, Myanmar is making brave new moves, as did many of the region’s high growth and transition economies decades earlier. It is opening up to trade, encouraging foreign investment, and deepening making the critical decisions to achieve its medium - and long - term goals.