Myanmar

Myanmar is continuing to implement market reforms. Its integration with the region's economies will improve following its recent membership in the Association of Southeast Asian Nations (ASEAN). However, the existence of a dual exchange rate system continues to undermine the efficient functioning of the economy. Long-term growth prospects depend on the extent to which Myanmar can improve its openness and competitiveness and overcome infrastructural bottlenecks.

RECENT TRENDS AND PROSPECTS

Myanmar is continuing the slow process of implementing a market economy. While the government has already partially liberalized foreign direct investment (FDI), trade, and agricultural prices, the legacy of central planning continues to hamper development. In 1997 GDP grew by 5 percent. Nevertheless, Myanmar continues to suffer from structural problems, such as inefficient state enterprises that continue to require budget subsidies and an underdeveloped financial system. These are preventing the economy from growing more rapidly. With the recent financial crisis in the region, a realignment of the fixed exchange rate has become imperative. Myanmar has yet to implement the measures needed to achieve greater openness and competitiveness, such as providing more infrastructure in areas like transportation, shipping, ports, and utilities. The country's political status and international relations have yet to be resolved, and information about Myanmar remains limited.

Despite being to a large extent a closed economy, Myanmar felt the impact of the financial crisis in East and Southeast Asia. In the last few years, despite its economic and political problems, Myanmar has managed to achieve fairly respectable growth rates. However, the mini-boom has begun to fade, and the financial crisis has highlighted both the country's economic frailty and policy shortcomings.

Inflation has generally remained in the 20 to 30 percent range in recent years. However, in mid-1997 serious flooding in the south and in the Irrawaddy delta region destroyed 1.2 million hectares of rice. This drove up food prices and increased inflation from 30 to 35 percent in April 1997 to more than 40 percent by the end of the year. In early September the situation forced the government to appeal to the United Nations for emergency food relief.

Gross investment stood at 16.8 percent of GDP in 1997, while national savings amounted to 8.3 percent. Total foreign investment rose to $6 billion by April 1997, up from $5.3 billion in December 1996. The United Kingdom was the largest investor, with around $1.3 billion, followed by Singapore with $1.2 billion and Thailand with $1 billion. Despite a highly publicized pullout by Western investors, investment continues to flow in from Asia.

Growth is expected to remain at 5 percent in 1998 and 1999. This is lower than in previous years

1997 refers to fiscal year 1997/98, ending 31 March.

because of adverse factors that will affect agricultural production, such as a lack of inputs and continued government intervention in production decisions. Gross investment is expected to decline slightly to 16 percent of GDP, and national savings to a little under 8 percent of GDP. Fiscal deficits and lax monetary policy will keep inflation high. Although financing problems will moderate import growth, weak export growth will keep the current account in a substantial deficit.

CRITICAL ISSUES IN SHORT-TERM ECONOMIC MANAGEMENT

The single most critical problem Myanmar faces relates to the management of the exchange rate system. Myanmar's dual system of an official exchange rate and one determined in a parallel market was cause for concern well before the recent regional currency depreciations. In the last few months, the influence of the fixed official exchange rate in restricting the country's ability to maintain growth, investment, and trade and to hold inflation at bay has become even more apparent. The official exchange rate continues to be fixed at MK6 to the dollar. However, at the beginning of the region's financial crisis, the kyat's rate of exchange in the parallel market fell by nearly 100 percent. At one point it traded at more than MK300 to the dollar.

In June and July 1997, as foreign exchange became scarcer, confidence collapsed. The government then resorted to printing kyat to buy dollars at the parallel rate, but this generated inflation. These events reflect the fragility of Myanmar's economy and its lack of resources to react to current events in the region. While the authorities are well aware of the exchange rate problem, they consider that a devaluation will not only increase inflation, but will also increase the amount of kyat necessary to repay foreign debt that is denominated in foreign currency. While the authorities have made some attempts to depreciate the kyat by shifting transactions from the fixed official rate to the parallel exchange market, about a third of external transactions, all related to the public sector, still use the official rate. Most private sector external transactions are now conducted in the parallel market. However, the complex set of foreign exchange and trade regulations still needed to maintain the dual exchange system has reduced transparency and undermined the efficiency of other measures taken to orient Myanmar toward a market economy.

The second important problem that Myanmar needs to resolve is the recurrent large fiscal deficits, which result from a small revenue base. Budget revenues declined from about 8.4 percent of GDP in the early 1990s to 5.1 percent in 1996. Despite a significant reduction in government expenditures from about 10 percent of GDP to 6.6 percent during the same period, the nonfinancial public sector deficit (that of the central government and state enterprises) remains at some 5 to 6 percent of GDP. These deficits are routinely financed with credit from the Central Bank and contribute to inflationary pressures. During the first six months of 1997 the amount of net credit to the public sector increased sharply. At the same time, credit to the private sector also began to expand rapidly, growing by 45 percent (albeit from a small base).

POLICY AND DEVELOPMENT ISSUES

Myanmar's long-term growth prospects depend on the extent to which it succeeds in introducing greater openness and competitiveness, improving infrastructure, accelerating market reforms, liberalizing trade, and increasing its capacity to attract FDI. Myanmar must encourage FDI as a way to obtain foreign technology, but this will be difficult as long as current distortions persist.

As concerns integration into the world economy, probably the most important event in 1997 was Myanmar's entry into ASEAN. This is expected to lead to substantial inflows of investment from neighboring countries. Myanmar is a resource-rich nation and possesses a large, low-cost workforce, which makes it potentially attractive as a production base for industrializing ASEAN members, such as Malaysia, Singapore, and Thailand. Myanmar will also join the ASEAN Free Trade Area and has been given until 2008 to complete the tariff reduction process.