ASIAN DEVELOPMENT BANK

COUNTRY ASSISTANCE PLAN
(2000-2002)

MYANMAR

<u>December 1999</u>

FOREWORD

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CURRENCY EQUIVALENTS
(as of 30 November 1999)

Currency Unit	-	Kyat (MK)
MK1.00	-	$0.160
$1.00	-	MK6.2517

Since 1977, the official exchange rate of the kyat has been pegged to the SDR at the rate of MK8.5 per SDR, which is equivalent to about MK6 per dollar. However, in 1993, the Government introduced the Foreign Exchange Certificate (FEC) which is trading in the market at about MK335.

ABBREVIATIONS

ADB	-	Asian Development Bank
CPI	-	consumer price index
DMC	-	developing member country
FEC	-	Foreign Exchange Certificate
GDP	-	gross domestic product
GMS	-	Greater Mekong Subregion
NGO	-	nongovernment organization
OPEC	-	Organization of Petroleum Exporting Countries
SEE	-	State Economic Enterprise
TA	-	technical assistance

NOTES

(i) The fiscal year (FY) of the Government ends on 31 March.
(ii) In this report, $ refers to US dollars.
(iii) No Country Programming Mission was scheduled for Myanmar and there is no pipeline of loans and TAs for 2000-2002 as ADB does not have any operations in Myanmar at present.

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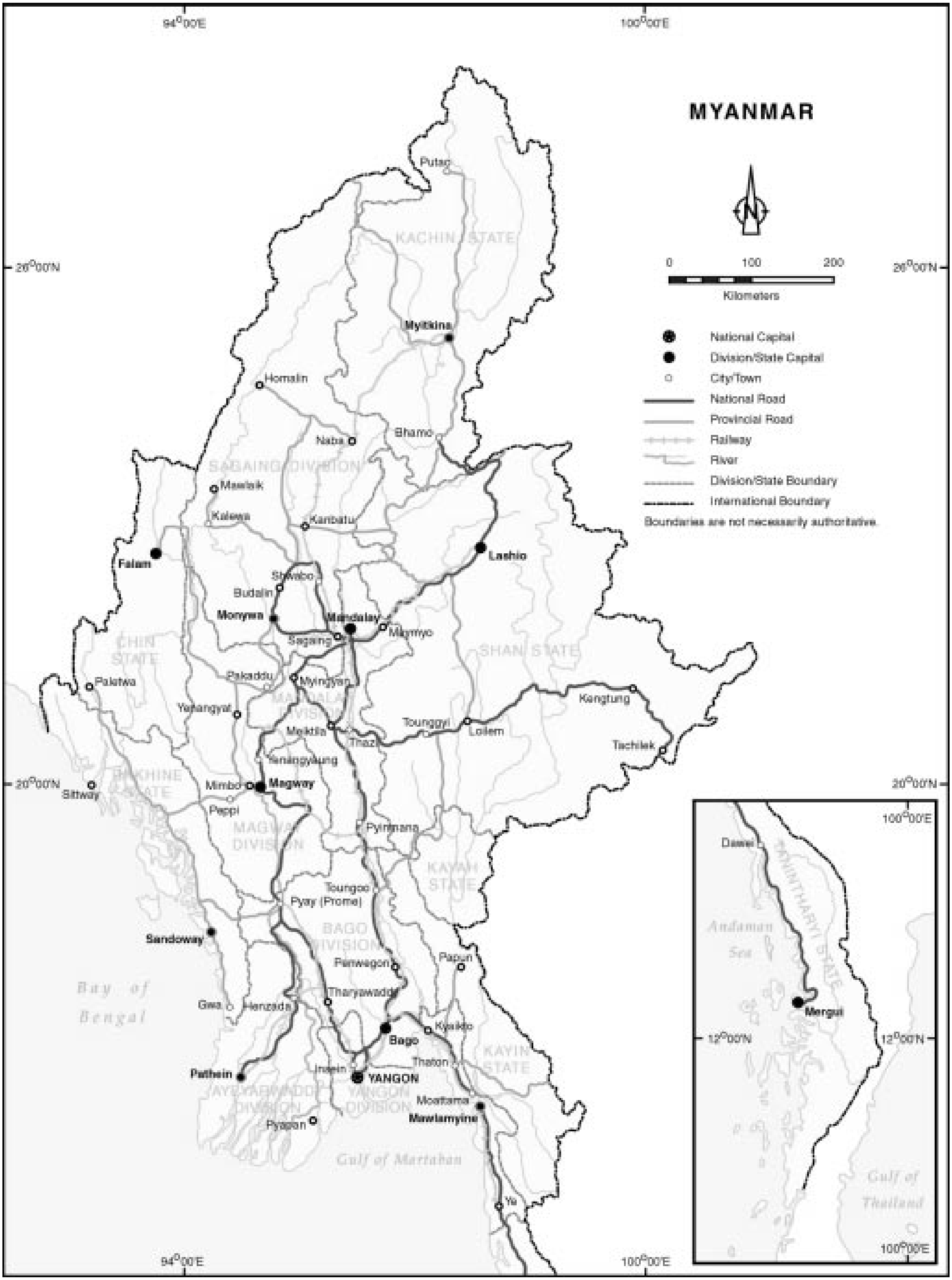
MYANMAR
0
100
200
Kilometers
National Capital
Division/State Capital
City/Town
National Road
Provincial Road
Railway
River
Division/State Boundary
International Boundary
Boundaries are not necessarily authoritative.
KACHIN STATE
SAGAING DIVISION
CHIN STATE
MANDALAY DIVISION
SHAN STATE
RAKHINE STATE
MAGWAY DIVISION
KAYAH STATE
BAGO DIVISION
KAYIN STATE
AYEYARWADDY DIVISION
YANGON DIVISION
TANINTHARYI STATE
Putao
Myitkina
Homalin
Naba
Bhamo
Mawlaik
Kalewa
Kanbalu
Lashio
Falam
Shwebo
Budalin
Monywa
Mandalay
Maymyo
Sagaing
Pakaddu
Myingyan
Paletwa
Yenangyat
Meiktila
Thazi
Taunggyi
Loilem
Kengtung
Tachilek
Yenangyaung
Sittway
Mimbo
Magway
Peppi
Pyinmana
Toungoo
Pyay (Prome)
Sandoway
Penwegon
Papun
Tharyawaddy
Gwa
Henzada
Bago
Kyaikto
Thaton
Pathein
Insein
YANGON
Moattama
Mawlamyine
Pyapon
Ye
Dawei
Mergui
Bay of Bengal
Gulf of Martaban
Andaman Sea
Gulf of Thailand
94°00'E
100°00'E
26°00'N
20°00'N
12°00'N

MYANMAR

I. Country Performance Assessment

1. According to official estimates, real GDP growth has been declining in recent years, from 6.4 percent in FY1996/97 to 5.7 percent in FY1997/98, and further to 5.6 percent in FY1998/99. The decline is mainly attributable to the adverse impact of floods in FY1997/98 and droughts in FY1998/99 on agricultural production. Another factor is the shortage of agricultural inputs such as fertilizer and pesticides caused by foreign exchange constraints. Real growth in agriculture has declined from 5.0 percent in FY1996/97 to 3.7 percent in FY1997/98, and to 2.8 percent in FY1998/99. The slowdown in agriculture may also have been exacerbated by a distorted incentive structure. The large impact of poor agricultural performance on overall growth reflects the predominant role of the sector, which accounts for 42.7 percent of GDP in FY1998/99, including related activities such as livestock, fishing, and forestry. Trade and other services, which account for 21.1 percent and 19.3 percent, respectively, have been growing steadily in recent years: trade at about 5 percent and other services at about 8 percent. The industrial sector, including energy, mining and manufacturing, accounts for only 16.9 percent of GDP. Real growth in the industrial sector has been declining from 10.7 percent in FY1996/97 to 8.9 percent in FY1997/98 and to 6.6 percent in FY1998/99. The structure of the economy has not changed since the introduction of market-oriented reforms in 1988 and remains a largely agrarian economy. In terms of expenditure, the share of consumption in GDP at F19985/86 constant prices has been declining in recent years, and stood at 68.8 percent in FY1998/99. The share of investment has increased, and gross investment accounted for 28.9 percent of GDP in FY1998/99. The saving-investment gap is relatively small. Gross capital formation in FY1998/99 is about 11.1 percent of GDP. This is mostly financed by domestic savings, which amount to 10.7 percent of GDP, implying there is very little net transfer of resources from abroad.

2. Inflation has been high in recent years, largely because of increasing food prices and excess liquidity caused by financing Government deficits through Central Bank credit. CPI inflation in Yangon increased from 20 percent in FY1996/97 to 34 percent in FY1997/98, and to 49 percent in FY1998/99. On a monthly basis, inflation has slightly subsided since mid-1998. With the new base of 1997, annualized inflation came to 32.7 percent in FY1998/99.

3. Official data indicate that there are about 19.7 million persons in the labor force, and 18.4 million persons in employment excluding unpaid family workers, out of a total population of 46.4 million, in FY1997/98. This means that the official unemployment rate in FY1997/98 is 7 percent. Agriculture is by far the largest employer, accounting for 64 percent of the labor force. This is followed by trade and industry, each employing another 9-10 percent of the labor force. The private sector and cooperatives employ 92 percent of the labor force while the public sector accounts for less than 8 percent of employment.

4. The consolidated budget is composed of the Union Government budget and state enterprises budget, and Cantonment Development Committee budget. On the revenue side, tax revenues and transfers from State Economic Enterprises (SEE) each account for about 40 percent of the Union Government revenues in FY1998/99. The share of tax revenues decreased from more than 50 percent in FY1997/98 to 39.2 percent in FY1998/99. In terms of GDP ratio, the Union Government's revenues declined from 7.9 percent in FY1997/98 to 7.3 percent of GDP in FY1998/99. The decline is attributable to decreased tax receipts. On the expenditure side, current expenditures and capital expenditures accounted for 47 percent and 53 percent, respectively, of the Union Government expenditures in FY1998/99. In terms of functional

classification, economic services accounted for 8.5 percent of total expenditure, followed by 8.2 percent for defense. Expenditures declined more substantially than revenues, from 8.8 percent in FY1997/98 to 7.3 percent of GDP in FY1998/99. Consequently, the Union Government deficit decreased from MK10.0 billion (-0.9 percent of GDP) in FY1997/98 to MK0.1 billion (0.0 percent of GDP) in FY1998/99. On the other hand, the State enterprises deficit increased from MK47.4 billion in FY1997/98 to MK69.4 billion in FY1998/99. The SEE's deficit was mainly resulted from the valuation of exports at the official exchange rate. The deficit incurred by exporting SEEs amounted to MK26.5 billion in FY1998/99. Subsidized rice procurement for state sector employees was also one of the factors leading to the SEE's deficit, the deficit on this account amounting to MK10.5 billion. Combining the Union Government and SEE deficits, the consolidated budget deficit for 1998/99 amounted to MK69.5 billion, 4.5 percent of GDP. The deficit has been mostly financed by Central Bank credit. It has become an annual practice to formulate a supplementary budget in the second half of the fiscal year. In the case of FY1998/99, the initial target for the consolidated deficit was 3 percent of GDP, and the gap of 1.5 percent between the deficit target and the actual deficit was filled by the supplementary budget. In FY1999/2000, the consolidated budget deficit is targeted at 2.4 percent of GDP. However, the Government already foresees a larger deficit of 4 percent of GDP.

5. SEE operations are generally inefficient. One of the indicators to show the inefficiency is SEEs' capacity utilization. The average capacity utilization ratio of SEEs under Ministry of Industry [2] (heavy industry) has been around 30-40 percent in FY1997/98. The ratio of SEEs under Ministry of Industry [1] (light industry) is higher, at 77 percent in FY1997/98. Another example of inefficient SEE management is rice subsidy for state sector employees. The subsidized sales price is estimated to be only about 15 percent of the Government procurement price paid to producers. The state entities monopolize energy, power, and communication sectors. The state sector accounts for about 50 percent of sectoral GDP in forestry, construction, and financial institutions. However, these sectors have small shares in GDP, and their growth rates are relatively low except for construction, communication, and financial institutions. In addition, the state sector employs only less than 10 percent of the total labor force. Despite their small contribution to economic activities and growth, the state sector has been given greater importance and support from the Government. This has contributed to inefficiency in economic management and undermined incentives in the private sector. One of the most serious problems facing SEEs is the adverse effect of the present exchange rate system. Because of the enormous difference between the official exchange rate of about MK6 to the dollar and the parallel market rate of MK350, exporting SEEs are making losses. Their domestic costs are largely based on the parallel market rate while export earnings are recorded at the official rate. Import businesses are making profits because they import at the overvalued official exchange rate and sell domestically at market prices.

6. On the monetary front, monetization of the economy had progressed with velocity declining until FY1996/97. Money supply has been increasing by 30-40 percent in recent years. Domestic credit has also been increasing by 30-40 percent. The share of currency in broad money has decreased. Credit to the private sector has been increasing at more than 50 percent since FY1995/96, which resulted in an increase in the share of the private sector, standing at 34 percent at end-1998. Business people in the private sector indicated that they had an easier access to bank credit when the economy was booming in FY1996/97. However, it has become difficult for them to borrow from commercial banks because of the recent economic slowdown. Real interest rates have been negative. However, the Central Bank recently lowered its discount rate from 15 to 12 percent, to encourage investment and to minimize adverse social impact of high interest rates on inflation via higher production costs. Also the Central Bank fixed the maximum deposits and lending rates at 12 percent and 17 percent, respectively. The lower

interest rates have helped commercial banks reduce interest payments to depositors while securing a 5 percent spread. The interest rate reduction has not had much impact on the amount of deposits. Meanwhile, the share of foreign currency deposits in the total deposits has increased to a little over 20 percent, twice the level of two years ago. This has weakened the Central Bank's control of domestic money supply.

7. According to official figures, total imports amounted to $2,573 million in FY1998/99. Of this, about 50 percent was capital goods, about 12 percent was intermediate goods, and about 38 percent consumer goods. Total exports amounted to only $1,258 million, mostly consisting of primary products such as agricultural, forest, and marine products, and minerals and gems. Border trade with neighboring countries accounts for nearly 30 percent of total exports. While the trade deficit amounted to $1,315 million in FY1998/99, the current account registered a smaller deficit of $546 million because of surpluses in services account and transfers. After adjusting for capital account transfers, Myanmar posted a net balance of payments surplus of about $64 million in FY1998/99. Foreign exchange reserves are claimed to be about $400 million, 1.8 months of imports, at present. The foreign exchange market remains highly distorted, with the parallel market rate of MK335 per FEC and MK350 per US dollar cash, as compared to the official rate of about MK6 per dollar. Only the state sector's trade is recorded at the official exchange rate, which accounts for merely 32 percent of the total trade in FY1998/99.

8. Trade is controlled by quantitative restrictions on import and export and foreign exchange control, instead of imposing high import duties or any export levies. Private traders are normally not allowed to export items like rice, sugar, rubber, and minerals and gems. Consequently, SEEs are still the major players in trading activities. Because of foreign exchange constraints, stricter import regulations have been imposed. For example, SEEs are now required to apply for item-by-item import licenses, and an open general import license is more difficult to get. Basically, if a company, either state-owned or private, is a foreign currency earner, it could use the foreign currency proceeds for importation except for restricted items. In the private sector, selling and buying foreign exchange has become a normal practice, and there seem to be no particular restrictions on it. However, an SEE without its own foreign exchange, will have to apply for a foreign currency allocation from the Government. Import duties are relatively low. Tariff rates range from 0 to 40 percent, and 68 percent of tariff lines are within the range of 0 to 5 percent. Residents are allowed to open foreign currency accounts, but withdrawals are only in Kyat. Exporters are allowed to withdraw in foreign currencies. In 1998, the Central Bank revoked private commercial banks' license for foreign currency transactions. Therefore, only two state-owned banks are currently allowed to conduct foreign currency transactions.

9. At the end of March 1998, the total outstanding debt of Myanmar was $5,647 million, of which about 90 percent is medium and long-term debt. At the time Myanmar had arrears totaling about $1,600 million, of which 70 percent was owed to bilateral sources, 28 percent to private creditors (including suppliers' credit), the rest to multilateral sources. By the end of March 1999, arrears to multilateral sources are believed to have more than tripled.

10. The Government growth projection for FY 1999/2000 is now set at 6.6 percent. The economy has potential to grow at a high rate. However, it remains highly controlled, with the state sector given greater support from the Government despite its small contribution to the economy. There is a large transfer of resources from the private sector to the state sector through taxation and levies, subsidies to SEEs, controlled prices for staples and agricultural and industrial inputs, and the highly overvalued currency. In particular the large and growing subsidy on rice consumption by state employees seems unsustainable. The private sector has not been

given adequate support and incentives to explore its full potential to contribute to higher economic growth. Economic liberalization would significantly enhance efficiency, and release the pent-up energies of the private sector, in response to new opportunities. This could shift Myanmar to a higher growth path, with more rapidly rising standards of living.

II. Country Operations

11. Asian Development Bank (ADB) undertook the preparation of an operational strategy study for Myanmar in 1987, but discussions with the Government were not completed. As of December 1998, cumulative lending to Myanmar consists of 28 loan projects for a total of $530.9 million and 38 technical assistance projects for a total of $10.7 million. No loan has been provided to Myanmar since 1986 and no technical assistance since 1987. All 32 loans approved prior to 1986 were closed by end-1998. However, Myanmar is involved in the Program of Economic Cooperation in the Greater Mekong Subregion (GMS Program). In that capacity Myanmar participates in regional meetings and workshops supported by ADB's regional technical assistance. To keep ADB's institutional knowledge up-to-date with regard to socio-economic developments, ADB has continued to review developments in economic policies and programs to the extent possible, based on the limited data available.

III. Donor Activities, Aid Coordination and Cofinancing

12. Since 1988-89, Myanmar has not received any new lending programs from the multilateral institutions. However, it has received loans from People’s Republic of China, Thailand, India, Singapore, and OPEC. In addition, Myanmar has received Debt Relief Grant from Japan, especially since 1988. Japan is also extending grants to the agriculture, forestry, and health sectors, grass root projects, and the Yangon International Airport Project. IMF continues to conduct its Article IV consultations annually with the last one having been held in June 1999. Although ADB's operations have not resumed yet, ADB has maintained aid coordination with other donors to discuss operational strategies and to exchange operational and economic information. ADB will continue to coordinate with other donors and areas for potential cofinancing operations in the future will be reviewed.