

ASIAN DEVELOPMENT BANK

**COUNTRY ASSISTANCE PLAN
(2001-2003)**

MYANMAR

December 2000

CURRENCY EQUIVALENTS

(as of 30 November 2000)

| | | |
|---------------|---|-----------|
| Currency Unit | - | Kyat (MK) |
| MK1.00 | - | \$0.149 |
| \$1.00 | - | MK6.7035 |

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 |
| FY | - | fiscal year |
| GDP | - | gross domestic product |
| SEE | - | State Economic Enterprise |

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 2001-2003 as ADB does not have any operations in Myanmar at present.

FOREWORD

For further information, please visit the Asian Development Bank's website at: <http://www.adb.org> or contact the following:

1. Programs Manager, [Division 3](#)
[Programs Department \(West\)](#)
Asian Development Bank
6 ADB Avenue
Mandaluyong City, Metro Manila

Mailing address:
P.O. Box 789
0980 Manila, Philippines

Telephone (632) 632-5897 or 632-5893 or 632-5894
Fax (632) 636-2648
E-mail adbpub@adb.org

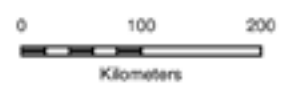
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MYANMAR



- National Capital
 - Division/State Capital
 - City/Town
 - National Road
 - Provincial Road
 - +—+— Railway
 - River
 - Division/State Boundary
 - International Boundary
- Boundaries are not necessarily authoritative.

25°00'N

26°00'N

20°00'N

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MYANMAR

I. Country Performance Assessment

A. Economic Performance Assessment

1. According to official estimates, real gross domestic product (GDP) growth had declined between FY1995/96 and FY1997/98, largely attributable to the adverse impact of bad weather on agricultural production. Another factor is the shortage of agricultural inputs such as fertilizer and pesticides caused by foreign exchange constraints. GDP grew by 5.8 percent in FY1998/99 and is now reported to have grown by about 10 percent in FY1999/2000. Real growth in the agriculture sector declined from 5.0 percent in FY1996/97 to 3.7 percent in FY1997/98, but it recovered to 4.5 percent in FY1998/99 and is estimated to have exceeded 10 percent in FY1999/2000 owing to good weather and an increase in cultivated areas. The economy remains largely an agrarian economy with the agriculture sector accounting for more than 40 percent of GDP including related activities such as livestock, fishing, and forestry. Therefore, agriculture performance is the most important factor in GDP growth and socioeconomic development.

2. Trade and services, which account for 21 percent and 19 percent at 1985/86 constant prices, respectively, have been growing steadily in recent years: trade at about 6 percent on average and services at about 8 percent. The industrial sector, including energy, mining and manufacturing, accounts for only 12-13 percent of GDP. Real growth in manufacturing accelerated from 5.0 percent in FY1997/98 to 6.2 percent in FY1998/99, and is reported to have registered even a much higher rate in FY1999/2000. However, the share of manufacturing in GDP has remained relatively low and the structure of the economy has not changed much since the introduction of market-oriented reforms in 1988. This is largely attributable to inadequate investment in manufacturing. In terms of expenditures on GDP, the share of consumption in GDP at current prices has been high and accounted for 88.2 percent in FY1998/99. The share of investment has remained relatively low, and gross investment accounted for 12.4 percent of GDP in FY1998/99. The saving-investment gap is relatively small. Gross capital formation is 12-13 percent of GDP. This is mostly financed by domestic savings, which stand at about the same level as gross capital investment, implying that there is very little net transfer of resources from abroad.

3. Inflation has been high in mid-1990's, largely because of increasing food prices and excess liquidity caused by financing Government deficits through Central Bank credit. Consumer price index inflation in Yangon increased from 20 percent in FY1996/97 to 34 percent in FY1997/98, and to 49 percent in FY1998/99. However, inflation has subsided since the end of 1999. It stood at 11.4 percent in FY1999/2000 and is estimated to have declined further in FY2000/2001.

4. Official data indicate that there are about 22.5 million persons in the labor force, and 14.2 million persons employed, out of a total population of 47.2 million in FY1997/98. This means that the official unemployment rate in FY1997/98 is 4.1 percent. The extent of underemployment is not clear from the data. Agriculture is by far the largest employer, accounting for 56.5 percent of the labor force. This is followed by trade, hotel and restaurants, and manufacturing, employing 15.8 percent and 11.4 percent of the labor force, respectively.

5. 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 non-tax revenues accounted for 44.7 percent and 54.8 percent, respectively, of the Union Government revenues in FY1999/2000. The share of tax revenues has declined since

the mid 1990s. In terms of GDP ratio, the Union Government's revenues declined from 7.8 percent in FY1997/98 to 7.2 percent of GDP in FY1998/99, and to 4.9 percent in FY1999/2000. The decline is attributable to relatively slow increase in tax receipts. On the expenditure side, current expenditures and capital expenditures accounted for 46.3 percent and 53.7 percent, respectively, of the Union Government expenditures in FY1999/2000. In terms of functional classification, economic services accounted for 40.8 percent of total expenditure, followed by 16.8 percent for social services. Expenditures as percentage of GDP declined more substantially than revenues, from 7.8 percent in FY1997/98 to 7.2 percent in FY1998/99, and to 4.9 percent in FY1999/2000. The Union Government balance turned from a deficit of MK2.3 billion in FY1997/98 to a surplus of MK4.5 billion in FY1998/99, but turned to a substantial deficit of MK20.2 billion in FY1999/2000. On the other hand, the SEEs' deficit almost doubled from MK47.5 billion in FY1997/98 to MK85.9 billion in FY1998/99, but declined to MK71.4 billion in FY1999/2000. The SEEs' deficit was partly resulted from the valuation of exports at the official exchange rate.

6. Combining the Union Government and SEE deficits, the consolidated budget deficit for FY1999/2000 amounted to MK110.5 billion or 5.0 percent of GDP. A major source of the deficit has been financing for loss-making SEEs, which is done through the State Fund Account System. Subsidies on some commodities including rice and fuel and services such as transportation for state sector employees have been another source of the large deficit. For example, the subsidized sales price of rice is estimated to be only about 15 percent of the Government procurement price paid to producers. The public sector deficit has been mostly financed by issuance of Treasury bills and bonds. It has become an annual practice to formulate a supplementary budget in the second half of the fiscal year.

7. 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. The ratio of SEEs under Ministry of Industry [1] (light industry) is higher, at around 70 to 80 percent in FY1997/98. The share of the state sector in GDP is only about 22 percent, and 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.

8. On the monetary front, monetization of the economy is still relatively low with total liquidity around 30-40 percent of GDP. Money supply has been increasing by 30-40 percent in recent years. The share of currency in broad money has been decreasing. Domestic credit has also been increasing by 20-30 percent. Local business people 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. Since the Central Bank of Myanmar started granting banking licenses to the private sector in 1995, private banks have grown rapidly and now play a leading role both in terms of lending and deposit taking. Credit outstanding to the private sector also grew significantly throughout the 1990's and now accounts for more than 30 percent of total domestic credit. SEEs ceased borrowing from commercial banks in 1989. Real interest rates have been negative. The Central Bank lowered its discount rate from 15 to 12 percent in April 1999 and further to 10 percent in

April 2000, to encourage investment and to minimize adverse social impact of high interest rates on inflation via higher production costs. Despite the interest rate reduction, deposits continued to increase in FY1999/2000. Foreign currency deposits have increased in recent years, and if converted at the parallel market rate, account for almost 30 percent of total liquidity. This may weaken the Central Bank's control of domestic money supply.

9. According to official figures, total imports amounted to \$2,539 million in FY1999/2000. Of this, about 40 percent was capital goods, about 17 percent intermediate goods, and the remaining consumer goods. Total exports amounted to only \$1,132 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 but only about 10 percent of total imports. While the trade deficit amounted to \$1,408 million in FY1999/2000, the current account registered a smaller deficit of \$671 million because of surpluses in services account and transfers. After adjusting for capital account transfers, Myanmar posted a net balance of payments deficit of about \$54 million in FY1999/2000. Gross foreign exchange reserves are reported to be about \$240 million or 1.6 months of imports. The foreign exchange market remains highly distorted, with the parallel market rate of MK350 per Foreign Exchange Certificate and MK350-380 per US dollar cash, as compared to the official rate of about MK6 per dollar. Trade in the state sector is still recorded at the official exchange rate, which is reported to account for about 30 percent of the total trade.

10. Trade is controlled by quantitative restrictions on imports and exports, and foreign exchange control, rather than through high import duties or export levies. Private traders are normally not allowed to export items such as rice, sugar, rubber, and minerals and gems. 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. Myanmar has been complying with the tariff reduction program based on the CEPT (Common Effective Preferential Tariffs) scheme agreed with Association of Southeast Asian Nation (ASEAN) countries. In addition, preparatory work has been started for implementing the World Trade Organization (WTO) valuation agreement by 2002. 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.

11. At the end of March 2000, the total outstanding debt of Myanmar was reported to be over \$5 billion, of which almost all was medium and long-term debt. At that time, Myanmar had arrears totaling about \$2 billion, of which about 70 percent was owed to bilateral sources, about 20 percent to private creditors (including suppliers' credit), the rest to multilateral sources.

12. Given its rich resource base, the economy has potential to grow at a high rate. However, Myanmar's economy remains highly controlled and has yet to adopt sound economic policies to fully utilize its potential and sustain economic growth. After a relatively successful period of economic growth following the initial liberalization of the economy in 1988, progress has slowed because of continuing structural and policy constraints. Unless more comprehensive and consistent structural reforms are undertaken, the economy will continue to depend heavily on

short-term measures responding to external factors such as weather and the regional economic environment.

13. To fully explore the potential of the Myanmar economy, certain critical structural and policy constraints need to be addressed. First, investment and savings ratios as percentage of GDP have been low and declining, now both standing at around 12-13 percent of GDP. Inadequate investment has hampered industrial development. Secondly, the public sector budget continues to run a deficit of around 5-6 percent of GDP, largely contributed by SEEs' losses and subsidies on commodities such as staples and fuels for state sector employees. While the fiscal deficit has been reduced, this is mainly due to reductions in public spending to unsustainably low levels. Tax collection, along with broadening the tax base and reducing the current level of exemptions, must be improved significantly to resume necessary government spending. Financing the public sector deficits through the issuance of treasury bonds and bills is one underlying factor of persistent high inflation. Thirdly, the current account also continues to register deficits. One of the most critical issues is that the agriculture sector, particularly rice production, is not given appropriate incentive for exports in terms of pricing and distribution channels. Fourthly, there remains a substantial, and growing, discrepancy between the official and parallel market exchange rates. The current official exchange rate is heavily biased toward import-using SEEs who import at the overvalued exchange rate and sell domestically at market prices. The amount of foreign currencies circulated in the economy is negligible if converted at the official exchange rate, but takes up nearly 30 percent of total money supply if converted at the parallel market rate. The distorted exchange rate system may also undermine the effectiveness of monetary policy instruments. Lastly, the banking sector needs to be further strengthened. The Central Bank needs to be granted greater authority and autonomy to control money supply to reduce the rate of inflation to manageable levels. Its capacity to supervise and monitor commercial banks should be strengthened. Although private banks have been growing rapidly, they are still new in the country's financial sector.

B. Assessment of Social and Environmental Performance

14. Myanmar currently ranks 125th out of 174 countries in United Nations Development Programme's (UNDP) Human Development Index (HDI) of 2000, slightly above Cambodia and Laos at the lower end of the group of countries considered to have medium human development. To the extent that they exist, Myanmar's social indicators have improved over the last decades and usually reveal better social conditions than expected given the per capita income. Life expectancy stood at around 60 years in 1997/98. Official poverty incidence for the Union as a whole is 23 percent while cases of severer poverty are reported to occur in border regions. According to statistics consolidated by the Department of Labor, the infant mortality rate was about 48 per 1,000 live births and the maternal mortality rate was about 150 per 100,000 live births. These figures are somewhat lower than indicated in reports from major international organizations. In terms of health care, accessibility to health services needs to be improved as only about 50 percent of villages have health centers. In terms of education, adult literacy is high around 90 percent and the gross primary school enrollment ratio is around 90 percent. However, the primary school completion rate is about 50 percent and the gross enrollment ratio at middle school level is lower than 40 percent. Under these circumstances, it is particularly worrisome that public expenditures for education and health as percent of GDP declined in recent years until FY1998/99. This trend should be reversed so as to raise the standards of living and upgrade Myanmar's human capital. In terms of gender balance, the country ranks 102nd out of 143 countries in UNDP's Gender-related Development Index (GDI) of 2000.

II. Country Operations

15. The 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 data available. In this regard, the 1995 Economic Report on Myanmar will be updated in 2000.

III. Donor Activities, Aid Coordination and Cofinancing

16. Since 1988-89, Myanmar has not received any new lending programs from the multilateral institutions. However, it has received loans from the People's Republic of China, Thailand, India, Singapore, and Organization of Petroleum Exporting Countries. 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. The International Monetary Fund (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 yet resumed, ADB has maintained contact with other donors to exchange information on respective activities in Myanmar.