



MYANMAR

UNLOCKING THE POTENTIAL

COUNTRY DIAGNOSTIC STUDY

EXECUTIVE SUMMARY

© 2014 Asian Development Bank

All rights reserved. Published in 2014.
Printed in the Philippines.

Publication Stock No. ARM146783-2

The views expressed in this publication are those of the authors and do not necessarily reflect the views and policies of the Asian Development Bank (ADB) or its Board of Governors or the governments they represent.

Note:

In this publication, “\$” refers to US dollars.

6 ADB Avenue, Mandaluyong City
1550 Metro Manila, Philippines
Tel +63 2 632 4444
Fax +63 2 636 2444
www.adb.org

For orders, please contact:
Public Information Center
Fax +63 2 636 2584
adbpub@adb.org

EXECUTIVE SUMMARY

After a series of bold social and economic reforms since its return to civilian rule in 2011, Myanmar has made a strong start on its journey toward peace, democracy, and prosperity, one that could put its troubled postwar history behind it. To secure its course, however, it will have to navigate a complex set of long- and short-term measures that are potentially fraught with difficulty.

Much has been achieved in the 3 years since the government, led by President U Thein Sein, came to office in the first general election in 20 years. While initial reforms focused on the political system and national unity, major macroeconomic reforms are well under way. The exchange rate has been unified under a managed float and the country now has an independent central bank. Details have also been released on increasing transparency in the national budget. Authorities have begun establishing basic regulatory structures and removing unnecessary hurdles to business and trade, providing legal foundation for foreign investment, improving essential public services, and addressing governance and corruption issues.

In response, the economy has sustained gross domestic product (GDP) growth of more than 7% for 2 years running, a remarkable performance helped by foreign governments lifting long-standing trade sanctions. Foreign investment is flowing in, foreign exchange earnings rising, and tourists returning to enjoy the country's outstanding areas of natural beauty and cultural attractions.

These achievements, with visible improvements in most economic and some social and political indicators, illustrate the government's strong commitment to economic development and the scope for further rapid deployment of innovative policies.

Few will be surprised, nonetheless, to hear of the pitfalls ahead. Modernizing an economy is a huge and complex task. And the government needs to prioritize and sequence reform measures and identify and address

constraints to sustained rapid economic growth. Observers widely acknowledge the huge opportunity, yet the country is facing difficult challenges in almost all aspects of economic and social policy.

A successfully integrated development policy framework will need to consider comprehensive development and reform planning and phasing. It is in this context that the Asian Development Bank's (ADB) Economics and Research Department presents this report, *Myanmar: Unlocking the Potential*, which is based on an in-depth country study undertaken in 2013. The report examines the most important and immediate issues that need to be tackled to unlock the potential. These include weak infrastructure, creating modern market and government institutions, human development, stronger regional integration, a clear focus on inclusive growth, and environmental protection.

More than just economic growth

Economic growth is imperative if Myanmar is to alleviate poverty and improve living standards. Once a very rich country that commanded the world's largest rice exports in the early 1940s, Myanmar was in decline for decades, with its per capita income of \$876 in 2012, the lowest in the Association of Southeast Asian Nations (ASEAN). It is one of the poorest countries in Asia, with estimates from the United Nations and others indicating a poverty rate of 25%, higher than Cambodia (21%) and Viet Nam (21%). But growth alone is not sufficient for a successful transformation, and its contribution to poverty reduction depends on specific circumstances and policies.

Myanmar is unique—and uniquely challenged—in a cultural complexity that reflects its geographical position between India to the west, the People's Republic of China to the northeast, and Southeast Asia to the east. Its 61 million people are among the world's most diverse, with more than 135 different ethnic groups.

The country's ability to ensure that participation in the growth process and the sharing of its benefits is as broad as possible will be crucial for a successful program of reforms. It can achieve this by making social inclusion, environmentally sustainable growth, and balanced regional development central to that agenda. In particular, this means promoting

greater participation in the economy of ethnic minorities through, for one thing, equitable sharing of natural resource revenues.

Ensuring economic stability

Good governance backed by an effective institutional, legal, and regulatory framework will be one of the bulwarks of a successful strategy for growth. Priority here should be given to establishing frameworks for the effective delivery of public services. The capacity of core policy-making institutions also needs to be strengthened to make reforms effective and sustainable.

Maintaining a sound and stable macroeconomic environment is another important precondition for a successful economic transformation. This encompasses the functioning of an independent central bank, sound monetary policies to keep inflation in check, stable financial policies to ensure credit availability, adequate government revenues to finance needed budgetary outlays, and a well-managed exchange rate.

Finally, Myanmar should make concerted effort to establish a favorable environment for a thriving private sector. This will require systemic support measures for improving the regulatory environment, investing in physical and social infrastructure, building human capital with a focus on strengthening the skills of the young, improving labor relations, and deepening the banking sector and financial markets. A well-functioning financial sector is an economy's lifeblood and vital for strong and inclusive growth. Myanmar's financial sector remains underdeveloped. Reforms are under way to rectify this, but this momentum needs to strengthen, with the focus on ensuring stability, efficiency, and increasing access to financial services.

Seeking sectoral advantage

The way forward requires a clear idea of sectoral strengths and a multipronged development plan backed by effective development strategies. Tapping key sectors in combination with appropriate policies will help the country unlock its potential. Exactly what will be Myanmar's growth trajectory is still uncertain, but looking at the experience of its neighbors could be useful in helping determine a suitable growth model. Development in Asia has typically involved a transformation from an agriculture-based economy into an industry and service-based one, underpinned by export-oriented manufacturing.

Myanmar's structural transformation will almost certainly involve a large-scale transfer of resources from agriculture to manufacturing and services. Nonetheless, clear opportunities exist for targeted investment in agriculture-related infrastructure, institutions, and innovation to enable rapid growth in productivity and value addition in the agriculture sector that will immediately benefit those reliant on the sector for income and food security and also contribute to sustained high and inclusive growth in the long run. After all, agriculture accounts for 30% of GDP and over 50% of employment. With relatively abundant land, water, and labor resources and proximity to the world's fastest-growing markets for food, the country has comparative advantage in this area. Revitalizing the rural economy requires that constraints from "farm to fork" be addressed through a strategy that considers investment needs comprehensively, in terms of both hard infrastructure and conditioning policies and services.

There is also great scope for Myanmar to implement policies that can unleash the full potential of industrialization. An industrial development strategy could be anchored in promoting labor-intensive manufacturing with the aim of integrating into global value chains, promoting trade-oriented small and medium-sized enterprises, leveraging special economic zones, and attracting foreign direct investment (FDI). A solid manufacturing base would help incubate industrial clusters, which in turn attract foreign firms with technological and managerial capabilities. For dynamic industrial development, the country will need to make long-term commitments to skills development and external investment partnerships. In particular, the government needs to coordinate its policies for incentives, investments, trade, and landownership and use to attract FDI into sectors that can spearhead long-term growth.

Tourism could be another game changer in the country's economic transformation. Myanmar has already taken significant steps to responsibly develop this potential, but there is an urgent need to address how the benefits of tourism can be leveraged without overwhelming the country's capacities. The Myanmar Tourism Master Plan 2013–2020 has outlined an extensive development plan, but there are still substantial gaps and weaknesses in the sector and its supporting infrastructure which may limit effective implementation.

Building human capital and infrastructure

Human capital, or the quality of the labor force, lies at the core of sustainable and equitable economic growth, making investments in education and health essential. A review of Myanmar's education sector points to three major constraints: insufficient funding, inequitable access, and poor quality or lack of relevance. Due in part to the low quality of education, much of the workforce remains largely unskilled. To help address the skills gap, the government initiated the Comprehensive Education Sector Review and created the National Skills Standards Authority, but a significant increase in investments in education and vocational training is needed to ensure that the country has a labor force equipped with the skills required in the transition to a more industry and service-oriented economy.

The crucial role of physical infrastructure in facilitating economic growth and development cannot be overemphasized. Effective transportation, reliable power supply, and state-of-the-art information and communication technology services enable businesses to thrive, people to become more productive and innovative, and growth to accelerate. Myanmar's infrastructure subsectors require integrated planning and appropriate investments to follow up those plans. Sector master plans should be better coordinated and prepared, with explicit linking of infrastructure plans to development objectives.

Institutional and human resource capacity in the public sector needs to substantially increase to allow prioritization of key development projects based on high-quality economic assessments across all sectors. Private sector participation should be promoted to mitigate funding constraints and improve the provision of infrastructure and social services.

Social inclusion, regional integration, and environmental sustainability

Poverty is high and there is considerable inequality in access to opportunities and social services across the country's regions. Economic, political, and social inequality among different ethnic groups can also breed ethnic hostility and lead to a conflict. A peaceful resolution of conflicting interests across ethnic and social groups during the transition is therefore critical, as is balancing regional development such that all ethnic groups have more economic opportunity and access to public services.

This calls for a development strategy for inclusive growth based on three policy pillars. The first is to sustain high economic growth to create sufficient economic opportunities for vulnerable groups. The second is to make adequate investments in education, health, and basic social services to enhance human capacity, eliminate market and institutional failures, and reduce social exclusion. And the third is to install social safety nets to enable households to withstand livelihood shocks caused by, for example, natural disasters and economic downturns.

Myanmar's geopolitical position, straddling three major cultural and economic realms, presents a great opportunity to enter regional and global markets, technology, and finance. The FDI–trade nexus will be crucial for the country's economic growth and development, and can be strengthened by promoting export-oriented manufacturing and facilitating integration into regional production networks and global supply chains. To this end, the government should develop special economic zones more strategically to link domestic and regional growth centers, with an emphasis on better connectivity.

Myanmar will continue to depend heavily on its natural resource assets. In 2011, 39% of GDP derived from primary industries, including agriculture, forestry, fisheries, mining, electricity, water, oil, and gas. Exploiting these sustainably requires immediate measures to eliminate the economic incentives that destroy natural habitats and to prevent overextraction of renewable resources. Safeguard procedures and regulations are needed, and monitoring and enforcement capacity for environmental protection should be strengthened. The country is already facing increasing environmental pressure—it has the fastest rate of deforestation in Southeast Asia, and poor regulation on pollution and emissions, to name just a few areas in urgent need of attention.

Strategic pillars and priority actions

Achieving these goals will require a strategic framework that focuses on a set of priorities from the multiple objectives already crowding the policy spectrum, while addressing bottlenecks and challenges. Eight strategic pillars are presented to support the development mission and vision.

1. Accelerating governance and public sector reform
2. Ensuring macroeconomic and financial stability
3. Creating a business-enabling environment
4. Leveraging rich endowments
5. Fostering internationally competitive sectors—manufacturing and services
6. Enhancing regional connectivity and integration
7. Promoting human development and poverty reduction
8. Pursuing environmentally sustainable growth

Realizing this mission and vision requires a great number of concrete actions to be taken in all sectors of the economy. The following are 10 meriting the most immediate attention (the full list of policy recommendations is available in the full report, Appendix 3).

Extractive Industries Transparency Initiative—Appoint a senior government official to lead the early adoption of the initiative, and use it to leverage internal governance reform in the extractive sector and, more broadly, exploit opportunities to anchor broader policy reforms, including anticorruption efforts.

Monetary policy—Develop a monetary policy process based on reserve-money targeting and develop the operational capacity to execute the process. Steps toward this goal include regulations and policies to support the development of private interbank, bond, and repo markets; conversion of the Central Bank of Myanmar auction facility into a lender of last resort able to impose penalty interest rates; and the redefinition of the reserve requirement to be consistent with monetary policy.

Financial sector—Develop market institutions and infrastructure for the banking system. This would include (i) finalizing the legal framework, (ii) completing the automated clearance and payments systems, (iii) developing the money market system, (iv) creating a credit information system, and (v) establishing financial accounting standards.

Fiscal management—Unify the annual budget and move further toward hard budget constraints for state economic enterprises, along with their further corporatization, and give consideration to the privatization of other state economic enterprises.

Education—Increase public spending on education, in particular for primary and secondary schools in the short term, to improve access and quality throughout the country; update school curricula; and enhance the quality and relevance of higher-level education programs, including technical and vocational education and training, to meet the needs of industry.

Transport and connectivity—Identify and implement priority projects for each subsector based on their potential to generate the highest economic returns; improve rural-urban and regional connectivity through rehabilitation and repair of lower-level road networks and at the borders; and upgrade rail, port, and air transport to ensure adequate connectivity both within the country and with the region.

Electricity—Adopt a least-cost power expansion plan to increase electricity supply, rehabilitate and upgrade existing coal- and gas-fired generation plants to provide a more reliable electricity supply, and facilitate the transition to the use of more efficient generation technologies such as combined cycle gas power plants.

Agriculture—Restructure agricultural support to increase productivity and value-adding opportunities along the entire supply chain through a supply-chain management approach that views agriculture as an agribusiness system; increase public investments in agrisupport services, including research, extension, marketing, credit, and organization of smallholders; strengthen input markets and promote the proper usage use of quality seeds, fertilizers, and pesticides through targeted investments and regulation; and extend and rehabilitate irrigation and drainage systems for rice and high-value crops.

Industrial policy—Pursue cluster-based development for small and medium-sized enterprises; minimize transaction costs for businesses; streamline processes, including for start-ups, construction permits, employing workers, registering property, accessing credit, protecting investors, paying taxes, trading across borders, enforcing contracts, and closing a business; and improve the business environment by clarifying land, legal, and contractual issues.

ASEAN Economic Community—Accelerate implementation of the ASEAN Economic Community commitments and obligations to meet the 2015 deadline; remove tariff and nontariff barriers to trade and investment; and implement policies encouraging efficient FDI including removing corruption, facilitating trade, and enhancing the business environment.

Myanmar: Unlocking the Potential

Country Diagnostic Study

Executive Summary

After 3 years of historic reforms, Myanmar has entered a pivotal stage in its socioeconomic development. Natural, cultural, and demographic advantages are positioning the country for long-term success, but many challenges and potential pitfalls lie ahead. This publication examines how to leverage the opportunities and offers solutions to the challenges. For Myanmar to achieve its economic transition, considerable investments will have to be made in infrastructure and developing human capital, and progress made on building institutional capacity, a regulatory environment for the private sector to flourish, and a modern finance sector. In all reform efforts, the government should embrace good governance, and strive for inclusive, environmentally sustainable, and regionally connected growth. Ensuring that the benefits of growth are shared broadly and regionally balanced stands out in a crowded development agenda.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to approximately two-thirds of the world's poor: 1.6 billion people who live on less than \$2 a day, with 733 million struggling on less than \$1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.



ASIAN DEVELOPMENT BANK

6 ADB Avenue, Mandaluyong City

1550 Metro Manila, Philippines

www.adb.org