Myanmar

Modest rates of growth in recent years have been based on high prices for natural gas exports, heavy public expenditures, and an improving agricultural performance. However, macroeconomic stability is vulnerable to fiscal deficits that are financed through money creation, in turn prompting double-digit inflation. The Government has taken tentative steps toward a more market-oriented system in agriculture and finance, and should build on these reforms.

Economic performance

Official estimates put GDP growth at above 10% in recent years (and 12.7% in FY2006, ended 31 March 2007), but variables correlated with GDP suggest that actual growth was significantly less than this, and below potential. Changes in production inputs such as energy, fertilizer, and capital goods are also consistent with modest economic growth. More broadly, official statistics are constrained by weaknesses in resources and institutions, making objective assessment of economic performance difficult.

Agriculture contributes about 43% of GDP and its performance has improved in some areas. Industry accounts for roughly 20% of GDP and has benefited from high prices for natural gas, the leading export. Construction is supported by government investment spending, including outlays on the new capital city, Naypyidaw.

The Government took some modest steps to reform the economy in 2007, particularly in agriculture and finance, and through market-oriented pricing reforms in state-owned enterprises (SOEs). (See Box 3.26.1.) In agriculture, some SOEs have been privatized or reoriented toward research and extension activities, and the role of the private sector has been enhanced in production, import, and distribution of important inputs, including fertilizer, seeds, and equipment. Restrictions on exports of rice have been lifted for rice grown on newly developed fallow lands. Such liberalization has encouraged production. In particular, output of pulses and beans, where the state has a minimal role in production and marketing, has grown rapidly. Production of pulses has increased threefold in the past 10 years and exports exceed 1 million tonnes.

In banking, several administrative measures put in place during a banking crisis in 2003 have been relaxed: the ceiling on deposit-to-capital ratios was increased from 7% to 10% in FY2006 and six private banks received approval to open new branches. Although foreign banks are still not allowed to operate branches or subsidiaries, 13 were licensed to run representative offices last year, and draft legislation that is planned to establish special economic zones is likely to permit foreign banks to operate in those areas.

3.26.1 Development challenges

Macroeconomic management will remain problematic, particularly in view of the high rate of inflation caused by monetized fiscal deficits. Still, the Government has started a modest transition toward a more market-oriented economic system, and needs to build on these reform moves. Likewise, it should develop institutional capacity to manage such initiatives. The comfortable level of international reserves has opened an opportunity to push through with reforms.

In this regard, possible steps in the important agriculture sector include lowering export restrictions, eliminating production targets, and using more market-oriented pricing. Similarly in finance, further liberalization of banking and the development of nonbank institutions in fields such as insurance and capital markets should be pursued, in addition to strengthening the monitoring, supervision, and prudential oversight of banks.

More broadly, the private sector could make a much more substantial contribution to the economy if the investment environment was significantly improved. Finally, unifying the exchange rate would go some way to eliminating distortions and to improving incentives in the economy.

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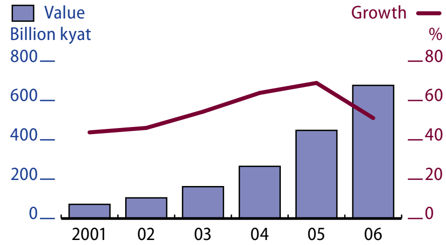
Nonetheless, formal financial intermediation remains low and the financial sector is underdeveloped. In the absence of an effective government debt market, monetary policy remains subservient to high fiscal deficits. Tax revenues have been rising (Figure 3.26.1), in part because of reforms since 2004 to improve tax administration and to increase tariff receipts from the use of a more depreciated exchange rate than the official one for valuing imports. However, revenue gains have been offset by high government expenditures, driven by large increases in civil servants' salaries in 2006 and investment outlays, including those related to the new capital city. Consequently, the consolidated fiscal deficit, which covers SOEs, has remained at about 4% of GDP, and is financed mainly through money creation by the central bank.

Broad money thus grew by almost 27% in FY2006, on top of 25% in FY2005 and 33% in FY2004, pushing inflation well into double digits. The price of rice rose by nearly 40% in the 12 months to August 2007. The administered price of gasoline was raised by nearly 70% in August 2007, the price of diesel was doubled, and the price of natural gas was raised fivefold. These sharp rises led to a doubling of public transport fees as well as price increases of several other basic commodities. Widespread protests followed.

Rising export revenues from natural gas continued to bolster the external position (Figure 3.26.2). The capital account also benefited in FY2006 from increased foreign direct investment in gas and oil. Gross official international reserves rose by 88% to $1.8 billion in the 12 months to June 2007, equivalent to 8 months of imports. Despite high inflation and monetary growth, the strong balance of payments resulted in the parallel market exchange rate for the kyat stabilizing at about K1,300/$1 in the second half of 2007, implying some real appreciation. The official exchange rate remained at K5.5/$1.

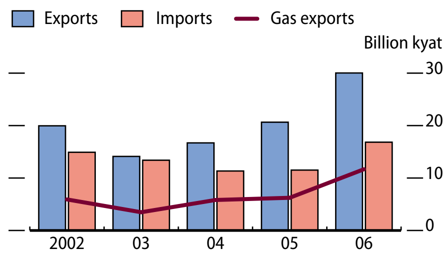
3.26.1 Tax revenues



Source: Myanmar Central Statistical Organization, available: www.csostat.gov.mm, downloaded 11 March 2007.

Click here for figure data

3.26.2 Trade indicators



Source: Myanmar Central Statistical Organization, available: www.csostat.gov.mm, downloaded 11 March 2007.

Click here for figure data

Economic prospects

GDP growth is expected to remain modest, supported by public expenditures and buoyant energy export prices; inflation is seen staying high. Although the Government's 5-year plan for 2006–2010 envisages average GDP growth of 10%, an outturn of half that target is likely over the medium term. The economy is vulnerable to a global economic downturn to the extent that activity slows in major trading partners, including the People's Republic of China, India, and Thailand. Conversely, if these countries maintain strong growth then the outlook is enhanced.

Historically high prices for gas exports are likely to be sustained in 2008, supporting strong export revenues and the current account. The volume of gas exports is expected to increase as more infrastructure is completed. However, the investment climate remains weak, given infrastructure and policy constraints, international trade and investment sanctions, and expectations of high inflation. Monetized fiscal deficits are likely to continue in the wake of outlays on the capital city and on highway projects. The fiscal deficits put macroeconomic stability at risk and complicate any further liberalization initiatives, given that controls, such as those in place, often generate revenues for the Government.