Myanmar

High prices for natural gas exports and a good harvest led to a modest pickup in economic activity. But macroeconomic stability remains elusive with monetized fiscal deficits feeding high inflation. The cushion provided by the gas exports makes now an opportune time to embark on structural reforms, including exchange rate unification, fiscal consolidation, and agricultural liberalization, and to redirect public spending to development of social and physical infrastructure.

Economic performance

According to official data, GDP increased by 13.2% in FY2005 (ended 31 March 2006). The expansion was driven by double-digit growth in agriculture, including livestock and fisheries; energy and power; manufacturing; mining; and services. The economy is heavily dependent on agriculture, which constitutes about half the economy. Industry accounts for roughly 15%, with services and trade the rest.

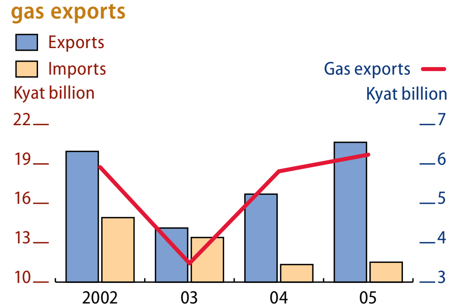
An objective assessment of economic performance and trends is made difficult by fundamental weaknesses in data. Data for variables closely correlated with GDP suggest that economic growth was significantly less than officially estimated. Indicators of inputs, such as energy and fertilizer, imports of capital goods, and expansion of agricultural acreage are consistent with lower than given GDP growth. For example, agricultural acreage grew by 3% in FY2005 when agriculture officially grew by almost 20%, implying a productivity increase not evident in other data. Economic growth in FY2005 nonetheless picked up somewhat, on the back of a stronger export performance (Figure 2.25.1), especially in natural gas; a good agricultural harvest; and growth in construction.

The fiscal deficit, including state enterprises, narrowed to about 4% of GDP. This reflected enhanced tax revenues (Figure 2.25.2) following steps in FY2004 to improve tax administration, reduce evasion, and increase tariff revenues from use of a more depreciated exchange rate than the official rate for valuing imports. Expenditures also declined marginally, but remained high at almost 10% of GDP, reflecting inefficiencies in public expenditure management as well as capital spending associated with a shift of the capital from Yangon to Naypyidaw.

In the absence of a well-developed market for government debt, the deficit is financed through monetization by the Central Bank of Myanmar. Broad money grew by 25% in FY2005 on top of an even higher growth rate the previous year. Inflation consequently accelerated after a pause in FY2004 (Figure 2.25.3), and is in double digits. Fuel price hikes, including an eightfold jump in October 2005, also boosted inflation.

The external balance has been supported by higher export volumes and prices for natural gas. Gross official reserves totaled just over $1 billion in September 2006, equivalent to 6 months of imports. The market-based parallel foreign exchange rate for the kyat appreciated in the second half of 2006, though for the year as a whole it weakened.

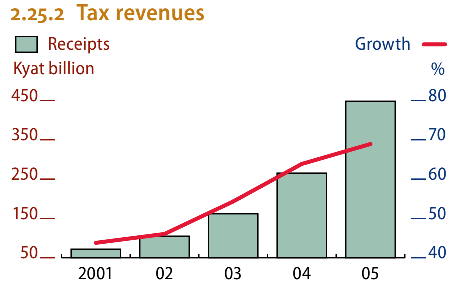
2.25.1 Total exports and imports, and gas exports



Source: Myanmar Central Statistical Organization, available: http://www.csostat.gov.mm, downloaded 2 March 2007.

Click here for figure data

2.25.2 Tax revenues



Source: Myanmar Central Statistical Organization, available: http://www.csostat.gov.mm, downloaded 2 March 2007.

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Economic prospects

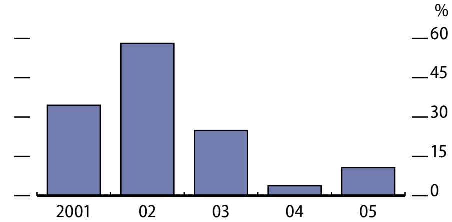
The Government's 5-year plan for 2006–2010 calls for average GDP growth rates of 10%, to be achieved through higher agricultural production, new gas fields, and increases in hydropower generation. The economy would be fortunate to achieve even half that over the medium term. In addition to the trade and investment sanctions by the United States and some others, the investment climate, outside the energy sector, remains poor for policy and infrastructure reasons. One of the few bright spots is the expanding trade relationship with fast-growing neighbors the People's Republic of China and India.

Growth and investment could be constrained as well by inflationary expectations. The economy runs chronic fiscal deficits, financed by monetary expansion. Inflationary pressures will also be influenced by a sharp rise in public sector wages in March 2006. Inflation could move back up from low double-digits to the 30–40% range. This would have a disproportionate impact on the large, poor, majority of the population. It could also prompt further currency depreciation.

The current account was in surplus in FY2005 due to the rising value of gas exports as well as a decline in imports. High gas prices will continue to buffer the external accounts, and exploration for more gas and oil is under way.

Continuing macroeconomic fragility will keep the economy vulnerable to sharp downturns in gas prices, as will shocks such as political strife, poor harvests, or instability in the banking system.

2.25.3 Inflation



Source: Myanmar Central Statistical Organization, available: http://www.csostat.gov.mm, downloaded 13 March 2007.

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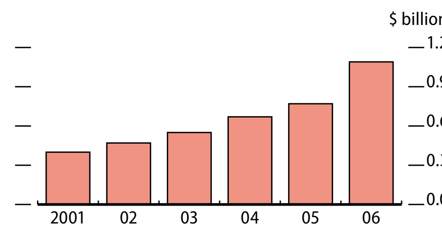
2.25.4 International reserves



Notes: International reserves exclude gold. Data for 2006 are up to September.
Source: International Monetary Fund, *International Financial Statistics* online database, downloaded 2 March 2007.

Click here for figure data

Development challenges

Given the rise in international reserves to relatively comfortable levels (Figure 2.25.4) and the likelihood that gas prices will remain high for some time, now would be an opportune moment to move toward a unified exchange rate. The current system lacks transparency, creates incentives for corruption, and induces distortions in the economy. Although exchange rate reform may adversely affect inflation and the finances of state-owned enterprises that can import at the official exchange rate, gradually introducing measures would help mitigate any adverse impact.

Some steps have been implemented to expand tax revenues, but public finances require further consolidation, in particular through reforms in state enterprises (they often require subsidies). Fiscal consolidation should be accompanied by steps to improve the debt market and to allow greater autonomy for the central bank. Strengthened public finances would enable greater policy flexibility for measures to assist the poor, such as improved social and physical infrastructure, and would lift growth.

Promotion of private sector development requires, among other reforms, improvements in the investment climate (with greater transparency and predictability in regulations). In view of the importance of agriculture and its impact on poverty, strengthening the sector should be a key goal. In this regard, it would be helpful to move away from administrative measures in the form of price controls and periodic export bans toward greater reliance on market-based mechanisms.