MYANMAR

ECONOMIC TRANSITION AMID CONFLICT

A SYSTEMATIC COUNTRY DIAGNOSTIC

Executive Summary

WORLD BANK GROUP

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i. **Myanmar is endowed with a wealth of natural resources and a strategic location between China and India, surrounded by 40 percent of the world's population.** Adding to its strategic position are 1,200 miles of uninterrupted coastline that stretch from the Bay of Bengal to the Andaman Sea, and a wealth of natural resources. It has enormous potential to translate these assets into progress for its 53 million people.

ii. **Myanmar is a nation in transition, seeking to break with a past marred by authoritarian rule, economic mismanagement, and multiple conflicts that persist today, driven by social exclusion and predatory natural resource extraction.** The country's opening, in 2011, and the first democratic elections, in 2015, marked critical turning points for Myanmar, generating a wave of optimism. The Nationwide Ceasefire Agreement (NCA) started a new political dialogue on what the future structure of a democratic and inclusive Myanmar state could look like. Reforms led to remarkable progress on economic growth and improved living standards. Progress on economic transition has been substantial, whereas progress on political transition has been moderate, and progress towards peace more modest.

iii. **The momentum of the transition has slowed recently. Resolute policy action is needed to accelerate growth and share its benefits more widely.** Weak state response to the Rakhine crisis, heightened violence in Kachin, Shan, and Chin, and unsteady progress on harder, second-generation economic reforms until recently have exposed the complexity of the transition process and revealed challenges to inclusive development. The military response in Rakhine State in 2017 against people who self-identify as Rohingya,[1] which led to loss of human lives and the forced displacement of about 725,000 refugees to Bangladesh, exposed the limits of the democratic transition and was met by widespread international condemnation. Global economic uncertainty presents an additional challenge. In 2019, especially after the cut-off point for the analysis presented in this document,[2] economic reforms have picked up. Reviving and sustaining progress in the three intertwined dimensions of the transition—from a planned to an open market economy, from military to civilian rule, from conflict to peace—will require deeper reforms and greater state institutional capacity.

iv. **This Systematic Country Diagnostic is the second prepared by the World Bank since it reengaged with Myanmar in 2012.** Building on the much larger body of data and evidence available today, it explores the drivers of Myanmar's growth and poverty-reduction performance since the country's opening, identifies the challenges to maintaining and improving this performance, and defines three pathways to address the challenges that lie ahead. In doing so, it examines government policies up to April 2019, including those set out in the 2018 Myanmar Sustainable Development Plan (MSDP).

Despite a legacy of conflict, poor economic management, and a uniquely complex transition, Myanmar's opening led to strong economic performance

v. **Decades of civil conflict and tight military rule have marked Myanmar's political, social, and economic life since its independence from British rule in 1948, and they still affect the country**

1 In line with the Report of the Advisory Commission on Rakhine State (2017), the remainder of the document will refer to those who self-identify as Rohingya as "Muslims" or "the Muslim community in Rakhine". This does not include the Kaman Muslims in Rakhine or other Muslims in the country.

2 The analysis presented in the SCD was completed in April 2019. Data released since this date and policies enacted in recent months (e.g. banking sector, electricity tariff reforms) are not reflected in this document.

today. Myanmar is home to some of the longest and most complex civil wars in the world, many dating from independence, when rebellions erupted across the country and numerous ethnic groups took up arms. These conflicts have cost thousands of lives, diverted resources from public services, and threatened the unity of the country. Against this backdrop, Myanmar's military, the Tatmadaw, represented itself as a force for unity and governed the country for half a century. Those decades were marked by brutal repression of dissent and public debate. The Burmese Way to Socialism was launched in 1962: industries were nationalized; trade, currency, fiscal management, and banking were centralized; and the country did not begin to open up to a market economy until the 1990s. Some elements characterizing those decades still affect Myanmar today, and efforts to address them will take time.

vi. **Since 2011, a triple transition has been underway in Myanmar.** The transition is simultaneously transforming the country's institutional and governance structures, reforming its economic, political, and social spaces, and seeking peaceful solutions to long-running civil conflicts. These shifts are part of a managed, long-term process, in which the military retains one-quarter of the votes in parliament and continues to lead three key ministries. The transition is also contested, as multiple ethnic armed organizations continue to battle for greater autonomy, and groups seek to shape the future of an eventual federal state. This transition is redefining the social contract between the state and its people, and the relationships between different communities living in the country. It is doing so under the stewardship of a civilian administration, long in waiting and gaining new governance experience, charged with bringing progress across multiple policy areas while managing the sensitive relationship with the military.

vii. **The country's opening—both *inwards* through democratic reforms and outwards through trade, investment, and migration—delivered immediate gains, and high expectations of continued progress.** Myanmar's economy grew at the extraordinary rate of 7 percent annually between 2011 and 2017—among the five fastest-growing countries in the world, and second only to China in the region in terms of historical growth acceleration. Capital accumulation, supported by foreign direct investment and, to a lesser extent, productivity improvement, contributed to this development. Growth improved living standards and helped to lift millions out of poverty. Poverty declined from 48 percent in 2005 to 32 percent in 2015, and it is estimated at 25 percent in 2017.[3] Basic infrastructure and services expanded. The share of households using candles as their main source of lighting plummeted from nearly 50 percent in 2005 to just 7 percent in 2017, as the public grid expanded and solar technology took off. The country also embraced the ICT transformation: mobile phones became pervasive, with 81.5 percent of households owning a phone, the vast majority internet capable.

Widening disparities, unsteady economic reform momentum, and environmental risks challenge further progress

viii. **Despite significant progress, growth has not been as pro-poor and inclusive as it could have been.** In contrast to the remarkable economic growth, the rate of poverty reduction, at 6.4 percent annually from 2010 to 2015, was close to the global average, and modest in comparison to Myanmar's peers in East Asia and the Pacific (EAP). Myanmar is one of the few countries in the EAP region where the income of the bottom 40 percent of the population grew more slowly than the national average (2.0 vs. 2.8 percent annualized growth) from 2005 to 2015. Inequality has been rising over the same period, along with steady urbanization. Those with land, capital,

3 The updated poverty headcount for 2017, based on the 2017 Myanmar Living Conditions Survey (MLCS), was released in late June 2019, and is reported here. The poverty analysis presented in this report, however, was completed in April 2019, ahead of the public release of new data. It thus covers the period up to 2015.

and education saw faster improvements following the country's opening. Other inequalities persist, with rural areas, conflict-affected states, and ethnic and religious minorities lagging in most dimensions of welfare—from stunting to educational attainment and access to electricity and basic sanitation. Improvement in these dimensions is fundamental for a fair start in life, and for the opportunity to move out of poverty and vulnerability.

ix. **The momentum of transition has started to wane, and with it the optimism that had characterized the early transition years.** Economic growth has decelerated from 8 percent in 2014/15 to an estimated 6.2 percent in 2017/18. The exchange rate and inflation are volatile. Fiscal resources remain extremely limited, with a tax-to-GDP ratio among the lowest in the world. Historically, State Economic Enterprises (SEEs) provided the largest share of public revenues, but they have now become net loss-makers, contributing to the fiscal deficit. Efforts towards deepening the decentralization agenda were visible in recent years, for example with initiatives distributing fiscal resources. Decision-making remains, however, rather centralized, and public institutions could better reflect Myanmar's diversity. Progress on the NCA has stalled, and violence has intensified. Little progress has been made in addressing the underlying causes of violence and exclusion in Rakhine, including the lack of freedom of movement or a viable pathway to citizenship for Muslim communities. Exclusion along ethnic, religious and geographic lines has fueled grievances that at times have resulted in violence in many states, underscoring the nation's fragility as it undergoes transition.

x. **Structural transformation has been slow, impeded by high cost of doing business, especially for small and medium enterprises (SMEs).** According to government data, the number of private firms registered through the Department of Investment and Company Administration (DICA) nearly doubled, from 30,407 in 2012 to 58,789 in 2015. Despite this welcome development, large conglomerates, some with foreign investors, still account for a large part of private sector activity. Decades of isolation from regional markets—despite membership in ASEAN—also have left global value chains underdeveloped, and few firms are innovating. About 85 percent of workers still are employed in informal activities that face considerable challenges (Labour Force Survey 2015). Basic factors of production such as finance, land, and electricity are expensive and difficult to access.

xi. **The potential for agricultural growth is still unfulfilled, although this sector is key for poverty reduction.** Agriculture accounts for about 70 percent of jobs in rural areas and among poor households. Incomes from agriculture have contributed to at least half of poverty reduction in the last decade. Myanmar's agricultural exports have been highly responsive to the opening of trade opportunities in recent years, but overall productivity is constrained. Agricultural growth is limited by thin input markets, reflecting the broader investment climate, and poor institutional infrastructure such as irrigation, extension, and marketing services. Low-quality physical infrastructure reduces productivity and limits value-chain potential.

xii. **Infrastructure investment has not followed the pace of development.** Myanmar has one of the lowest electrification rates in Southeast Asia (42 percent in 2018) and the average annual consumption per capita (193 kWh per person in 2016) is 3.5 times lower than the average for developing countries in the EAP region. Regulated tariffs are below costs, which limits private investment in the sector. It is estimated that around 20 million people, or half of the rural population, lack basic road access. Despite a doubling in the number of vehicles since 2012, the current level of investment in transport, from both public and private sources, is estimated at 1–1.5 percent of GDP, compared to 3–4 percent of GDP in other countries at a similar stage of development. The potential to leverage ICT solutions to connect people to services, markets, and institutions is still largely untapped.

xiii. **Investment in human capital remains insufficient, and Myanmar's demographic advantage will soon begin to diminish.** The global Human Capital Index (HCI) estimates that children born in Myanmar today can expect to be only 47 percent as productive when they grow up as they would be with access to high-quality health, nutrition, and education services. This is well below the HCI of many of Myanmar's neighbors. Lack of skilled employees is cited by firms as one of the main constraints to growth, and this is due to dramatic underinvestment by the state in basic service-delivery systems. While public spending on education, health, and social protection has risen rapidly in recent years, and human development outcomes have improved, this only partly reverses the historical neglect of human capital investments. Inadequate efforts to reach the most underserved and disadvantaged have also limited the potential of Myanmar's human capital to contribute to the economy. Myanmar's demographic transition from a youthful to an aging population is likely to be short—only about 25 years according to current demographic projections. Ensuring that those who enter the workforce in the future have the appropriate skills and access to health care is a key element of a high-growth scenario.

xiv. **The current use of natural resources increases risks to sustainable growth.** Reliance on nonrenewable assets and mismanagement of natural resources are depleting natural capital (minerals, fisheries, forests), to the advantage of a small elite and without generating broad gains for the population at large. Deforestation in Myanmar is among the fastest in the world. The current use of natural resources, together with challenges emerging from steady urbanization, is accelerating environmental degradation and affecting water quality, with consequences for livelihoods and health. Disaster risks are also heightened, but preparedness to withstand and mitigate the impact of weather and climate-induced shocks, to which the country is highly exposed, is limited.

xv. **Recent policy responses have shown a will to tackle challenges.** Recent steps to open the wholesale, retail, insurance, and banking sectors to foreign investment could potentially spur growth and poverty reduction, as did the opening of the telecommunications sector in the early transition period. Stepped-up investments in nutrition, basic education, and social protection systems bear promise. Legal and regulatory frameworks for environmental management have been introduced. Importantly, Myanmar has recently laid out a comprehensive vision for its future as a democratic, peaceful, and prosperous country, in the form of the MSDP.

Reforms need to be deepened and transition benefits shared more widely

xvi. **Today, building on the deep changes initiated during the early transition, Myanmar may wish to follow three interrelated paths to revive growth momentum, share the benefits of growth more widely, and ensure sustainability for future generations.** Doing so will require bold policies and farsighted and inclusive institutions to drive reforms. Table 0-1 below summarizes prioritized policy areas and actions for progress within the following three pathways:

Pathway 1: Strengthening economic and financial sector management to sustain growth and job creation

xvii. **Economic reforms now need to go deeper for strong, continuing growth.** Thus far, Myanmar has focused mostly on getting the fundamentals right. This has generated immediate gains. Reducing fiscal deficits and financing less of those deficits from a more independent central bank has lowered inflation and supported the unification of the exchange rate. Opening sectors such as telecommunications and manufacturing to investment, especially from abroad, and

deregulating trade has shrunk the trade deficit, increased employment, and made a wider range of goods and services available at lower prices. But sustaining long-term economic progress requires strengthening these foundations and building on them. Second-generation reforms to support infrastructure and efficient markets will be harder, but the benefits can be longer lasting—reforms such as raising electricity tariffs to cost-recovery levels while protecting low income users; following through on well-regulated foreign investment in the banking, insurance, and retails sectors; and gradually deregulating bank interest rates. These reforms will raise the potential for growth by stimulating the private sector through the power of competition and connecting people to services and markets without discrimination.

Pathway 2: Building inclusive institutions and human capital for all to foster peace and shared prosperity

xviii. **Myanmar needs a greater focus on inclusion to take full advantage of opportunities to promote peace, build shared prosperity, and reduce poverty.** Sharing the benefits of the transition more widely across geographic areas and income groups will not only be key to reducing poverty but will also increase the potential for peace and sustained growth going forward. A stunting rate of 29 percent, middle school enrollment of just 71 percent, and lack of year-round access to basic water for more than 30 percent of the population will be felt for years to come, as these disadvantages limit the full productive potential of human capital. Inequality in welfare and in access to quality basic services, based on location and identity, fuels grievances that have at times turned violent. Addressing these gaps is even more crucial in the face of a peace process that has lost momentum and the crisis in Rakhine State. More representative institutions and equitable fiscal arrangements that balance power and responsibility between the center and the states and regions, together with cooperation with nonstate providers of services in conflict-affected areas, can help stabilize the country. They can also ensure that service delivery effectively meets differing local needs. This will avoid tensions that might reverse the economic advances of recent years, foster peace, and build investor confidence. At the same time, underlying formal and informal barriers to the inclusion of ethnic and religious minorities will need to be addressed. Effective and equitable investments in improved service-delivery systems will also result in a stronger human capital base, and this will unleash greater productivity and economic growth for decades to come.

Pathway 3: Managing natural endowments sustainably and building resilience for long-term prosperity

xix. **Enhancing environmental sustainability and managing disaster risks are also critical for long-lasting and inclusive growth.** Growth should not come at the expense of future generations. Nor should it deplete natural resources and damage the environment in a way that negatively impacts livelihoods and risks the safety of the population today, particularly the poorest. Myanmar needs to change the way it manages, monitors, and uses its wealth of natural assets. More equitable legal frameworks are needed for the use of land, forests, and fisheries. Myanmar could also do more to manage environmental degradation and disaster risks linked to steady urbanization—for example, by improving urban planning and waste management. The country can go beyond managing the impact of degradation and attempt to reverse it—for example, by implementing the National Forest Rehabilitation and Restoration Program. Similarly, the country needs to increase its preparedness for weather- and climate-related shocks and other natural disasters such as earthquakes, in addition to mitigating their consequences.

Cross-cutting: Reforming public institutions for effective and equitable policy implementation

xx. **Strong institutions are needed to effectively pursue this broad and challenging agenda.** Implementing priority reforms highlighted in this SCD and realizing the MSDP vision with which they are aligned will require better performance from public institutions that coordinate and monitor policymaking and implementation. At both the central and local level, old habits and institutions need to be modernized to support forward-looking policies, including policies that can further accelerate economic growth, and promote a healthy private sector, better public service delivery, and enlightened management of natural assets. A more representative, effective, and efficient public sector is within reach. Myanmar has already taken steps, on which it can build, to empower the National Economic Coordination Committee (NECC), create a modern public financial management system, improve data generation and evidence-based policymaking, and realize the potential of digital solutions for governance and service delivery.

Table 0-1 | Overview of Pathways with Priority Areas and key Policy Actions

Pathway	Priority Area	Policy Action 1	Policy Action 2	Policy Action 3	Priority Level
1. Strengthening economic and financial-sector management to sustain growth and job creation.	**1.1 Maintain fiscal balance and macroeconomic stability.**	Collect more revenues.	Spend more and better.	Manage macro-fiscal risks.	HIGH
	1.2 Develop a sound, efficient, and inclusive financial system.	Maintain financial-sector stability.	Deepen the financial market.	Pursue financial access.	MEDIUM
	1.3 Strengthen the environment for investing and operating businesses.	Improve connectivity and integration with international markets.	Increase coherence in investment policies and investment promotion.	Promote inclusion in developing the private sector.	MEDIUM
	1.4 Close the gap between supply and demand for infrastructure and technology.	Accelerate delivery of quality electricity services to reach all people in Myanmar by 2030.	Expand and improve transport connectivity.	Catalyze growth of the digital economy, for jobs and to prepare for the 4th Industrial Revolution.	HIGH
	1.5 Improve income-generation opportunities and accessibility in rural areas.	Improve productivity and diversification.	Match resources with the needs of rural communities.	Enhance competitiveness.	HIGH

Pathway	Priority Area	Policy Action 1	Policy Action 2	Policy Action 3	Priority Level
2. Building inclusive institutions and human capital for all to foster peace and shared prosperity.	**2.1 Foster peace, social cohesion, and more inclusive governance institutions.**	Strengthen the inclusiveness and representativeness of institutions, including through decentralization.	Promote social cohesion and social inclusion for durable solutions, including in Rakhine.	Reinvigorate the national peace process under the NCA.	HIGHEST
	2.2 Strengthen systems for the delivery of equitable and quality services and risk protection that allow people to lead healthy lives.	Increase the effective coverage of essential services for those lagging behind.	Improve the quality of basic services.	Address vulnerabilities and prevent reversal of gains in human capital assets.	HIGH
	2.3 Ensure education for all and skills for productive employment.	Expand access to quality basic education, to ensure all children get a fair start.	Foster acquisition of needed skills through higher education and TVET.	Match people to jobs, and secure returns on investments in human capital.	HIGHEST
3. Managing natural endowments sustainably and building resilience for long-term prosperity.	**3.1 Manage land and natural resources transparently, equitably, and sustainably.**	Improve monitoring of natural resource production and use for better management of stocks and revenues.	Strengthen legal frameworks, and their implementation, for equitable resource use.	Halt and reverse depletion of natural capital and environmental degradation.	HIGH
	3.2 Build resilience to disasters and mitigate the impact of environmental degradation.	Mitigate risks arising from environmental degradation.	Foster disaster and climate resilience.	Strengthen emergency response and recovery.	MEDIUM
Cross-cutting: Reforming public institutions for effective and equitable policy implementation.	**4.1 Improve effectiveness, transparency, and accountability of public sector institutions.**	Increase the responsiveness and inclusiveness of policymaking.	Strengthen public financial management systems and administrative processes, including by leveraging ICT.	Improve quality and effectiveness of the civil service.	HIGH

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