

Inclusive and Sustainable Growth Assessment

Myanmar

2017–2021

(Draft as of 3 March 2017)

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CURRENCY EQUIVALENTS

(as of 1 March 2017)

Currency unit	–	Kyat (MMK)
MK1.00	=	\$0. 00073
\$1.00	=	MK 1,365

ABBREVIATIONS

ADB	–	Asian Development Bank
CBM	–	Central Bank of Myanmar
FDI	–	foreign direct investment
GDP	–	gross domestic product
ICT	–	information technology and communications
NLD	–	National League for Democracy
PRC	–	People's Republic of China
TVET	–	technical and vocational education and training
UNDP	–	United Nations Development Programme

NOTE

In this report, "\$" refers to US dollars

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I. INTRODUCTION

1. Myanmar has achieved rapid growth following the initiation of dramatic reforms in 2011. However, a complex array of factors—many of which stem from decades of isolation and stagnation—prevent Myanmar from fully capitalizing on its strategic location and achieving rapid, inclusive, and sustainable growth in the medium term. Overcoming these challenges will require strong national leadership, political stability, a successful peace process, a commitment to economic reform and institutional development, and support from the international community in transitioning towards global good practice. This assessment examines the prospects for inclusive and sustainable growth in Myanmar to inform the formulation of the Asian Development Bank (ADB) Myanmar Country Partnership Strategy, 2017–2021. It assesses Myanmar’s historical legacy, recent socioeconomic development trends, and policy and institutional challenges, including an analysis of progress, challenges, and priorities related to all three pillars of ADB’s conceptual framework for inclusive growth, which focus on: (i) rapid and sustainable growth to expand economic opportunities; (ii) expanded human capacities, especially for disadvantaged groups, to promote equitable access to opportunities brought by economic growth; and (iii) strengthened social protection to reduce vulnerabilities and prevent extreme deprivation.¹

II. ACKNOWLEDGING THE LEGACY OF THE PAST

2. In the 1950s, Myanmar’s economic prospects were among the most promising in Asia. Myanmar was the world’s largest rice exporter; controlled rich timber, mineral, and oil resources; and had an educational system that was considered among the best in the region. Following the 1962 coup, however, the country embarked on a path of socialism and autarky. The government ran large public sector deficits financed through money creation. To combat the resulting inflation, the government fixed key prices, including the exchange rate. Predictably, the real exchange rate appreciated, eroding the international competitiveness of Myanmar’s tradable sectors, especially agriculture. Economic growth stalled, reinforcing a vicious circle of inflation, price controls, exchange rate overvaluation, and stagnation. Trade and investment sanctions imposed by the international community further isolated Myanmar from the global economy.²

3. Over time, administrative controls spread over most of the economy, leading to widespread smuggling and the emergence of a shadow economy where corruption and rent-seeking flourished. Economic stagnation, rising poverty, a deterioration in institutional quality, and a breakdown in the rule of law sparked increased rivalry for the country’s natural resources and control over narcotics production and trade, much of it in ethnic areas along the country’s borders. This intensified the government’s conflict with ethnic armed groups that sought to retain control over resources in their respective areas. Military operations accounted for an increased share of public expenditures, diverting resources from much-needed infrastructure development, and public health and education services. By 2012, when the first quasi-civilian government under President Thein Sein took power, the country faced ongoing ethnic conflict, and its economic and social development indicators had fallen well below its Southeast Asian neighbors.

¹ ADB. 2015. *Revised Guidelines on Inclusive Economic Growth in the Country Partnership Strategy*. Manila.

² V. Nehru. 2012. Myanmar’s Economic Policy Priorities. *Carnegie Endowment for International Peace Working Paper Series*. No. 50014: Washington, DC.

III. UNDERSTANDING THE PRESENT

4. **Reforms.** The economic and political reforms announced by the Thein Sein administration in 2011 caught many observers by surprise. Economic reforms (i) revamped the foreign exchange system; (ii) transformed telecommunications; (iii) sharply increased budgetary allocations for health, education, and infrastructure; and (iv) overhauled the legal, regulatory, and institutional framework for foreign investment; the financial and agricultural sectors; and property rights over farmland. Political reforms were even more fundamental, culminating in free and fair elections in November 2015, which were won by the opposition National League for Democracy (NLD), led by Aung San Suu Kyi.

5. Myanmar's political and economic reforms prompted a positive response from the international community. The Paris Club wrote off or restructured \$15 billion of external bilateral debt in 2013 after ADB and the World Bank had their arrears cleared and resumed lending. External financing and technical assistance poured in from around the world. The United States gradually but significantly eased sanctions, with an almost complete removal in October 2016, while the European Union lifted its sanctions altogether.

6. While specific economic priorities have yet to be fully detailed, the NLD government set out broad economic priorities in July 2016, with the vision of achieving inclusive and sustainable economic development with national reconciliation, equitable development, protection of natural resources, and job creation as overarching goals. Stated policy priorities include fiscal prudence, reform of state-owned enterprises, building human capital, improving infrastructure, job creation, agricultural development, private sector and financial sector development, sustainable cities, tax reform, property rights to promote innovation, and private sector readiness for the Association of Southeast Asian Nations Economic Community.

7. **Economic performance.** Myanmar's economic performance has been improving. The NLD inherited an economy that is among the fastest growing in the world, albeit from a low base. Annual gross domestic product (GDP) growth averaged 5.4% during 2009–2011, and accelerated to an estimated 7.9% in 2012–2015.³ Since 2012 growth has been accompanied by structural change. Agriculture, which accounts for about 52% of employment, fell from 37% of GDP in 2010 to 27% in 2015; the share of services increased from 37% to 39%; and the share of industry climbed from 27% to 34%. Two-thirds of growth was concentrated in Myanmar's central regions, especially in the urban growth poles of Yangon and Mandalay. As a result, rising rural–urban income inequality led to large numbers of migrants leaving rural areas in search of informal sector jobs in urban centers.⁴ The official headcount poverty ratio was 26% in 2010 (an update is pending); the poverty incidence is estimated to be twice as high in rural areas.⁵

8. The record on macroeconomic stability has been mixed. Inflation declined from over 22.5% in 2008 to an average of 6.4% in 2012–2014, notwithstanding a temporary hike in 2015 in the aftermath of severe floods. The fiscal situation has also improved due to better

³ ADB. 2016. *Asian Development Outlook 2016*. Manila.

⁴ The rise in the share of services in overall GDP, particularly retail and wholesale trade, reflects this movement of labor into urban informal labor markets.

⁵ Government of Myanmar. 2011. *Integrated Household Living Conditions Survey in Myanmar (2009–2010)*. Nay Pyi Taw.

revenue collection and renewed aid flows. However, the consolidated public sector deficit widened to 6% of GDP in 2015, mostly financed by placement of government treasury bills with state banks, and monetary financing from the Central Bank of Myanmar (CBM). The current account deficit widened, partly as a result of the import of capital goods related to foreign investment, and was financed mainly by foreign direct investment (FDI) and aid inflows. FDI approvals climbed from less than \$1 billion per year in 2008–2010 to an average of \$4.9 billion in 2012–2014, and \$9 billion in 2015. The natural gas sector has attracted the highest share, followed by transport, communications, and manufacturing. Total external debt fell from 24.7% of GDP in 2012 to 14.7% in 2015.

9. **Sectoral reforms.** Reforms initiated by the previous administration (most notably in telecommunications) have provided some foundation for accelerated growth.⁶ A new law and the opening of the sector to foreign companies through transparent bidding helped lower telecommunications prices dramatically and expand mobile coverage to 85% (January 2017) of the population. Nevertheless, penetration rates are well below those of neighboring countries. Similarly, despite being incomplete, financial sector reforms have improved the quality and availability of financial services, encouraged technological innovation, and begun to repair confidence in the currency and in the stability and reliability of the banking system. Nevertheless, Myanmar lags behind neighboring economies in most indicators of financial sector development. Only 10% of the population has a bank account, and less than 3% has any formal insurance. The regulatory framework is embryonic; the CBM is erecting a regulatory framework to ensure financial stability and minimize systemic risk.⁷

10. **Development indicators.** Recent economic performance notwithstanding, Myanmar's economic legacy bears heavily on its social development indicators. Reflecting the broad breakdown of public services, Myanmar ranks 148th out of 188 countries on the Human Development Index, significantly below its Southeast Asian neighbors.⁸ Myanmar's ranking is much the same in terms of other development indicators, including finance, education, and health services; or the per capita availability of clean drinking water, paved roads, electricity, and formal employment. Myanmar consequently made mixed progress in achieving the Millennium Development Goals,⁹ although the government's increased focus on social development did contribute to impressive achievements in some areas, including infant mortality (which declined from 78 per 1,000 live births in 1990 to 40 in 2015). Maternal mortality rates have also declined but remain high. Life expectancy climbed from 60 to 67 years from 1990 to 2014. The enrollment rate in primary schools appears near universal, but it declines rapidly in secondary and high school, and pedagogic outcomes are worrying. Indicators that have worsened or seen marginal change include the prevalence of malnutrition, tuberculosis, and HIV. The new government has made a strong commitment to the Sustainable Development Goals, and it will be important to set clear targets and plans and track progress as baseline data on indicators become available.¹⁰

⁶ ADB. 2014. *Myanmar: Unlocking the Potential—Country Diagnostic Study*. Manila.

⁷ S. Turnell. 2016. *Banking and Finance in Myanmar: Present Realities, Future Possibilities*. Unpublished paper prepared for the United States Agency for International Development.

⁸ United Nations Development Programme (UNDP). 2015. *Human Development Report 2015*. New York.

⁹ ADB, United Nations Economic and Social Commission for Asia and the Pacific, and UNDP. 2015. *Making It Happen: Technology, Finance and Statistics for Sustainable Development in Asia and the Pacific*. Manila.

¹⁰ Government of Myanmar and UNDP. 2016. *Readiness of Myanmar's Official Statistics for the Sustainable Development Goals*. Nay Pyi Taw.

11. **Inequality.** Past growth has been non-inclusive, with marked inequality of opportunity across population groups. For example, urban–rural gaps in school enrolment and completion rates widen markedly after primary school, while a much higher proportion of rural children are underweight, stunted, or wasted than their urban counterparts. Children from poor households are more than twice as likely to be underweight than children from the wealthiest. The proportion of expectant mothers in urban areas that can expect institutional deliveries is more than double that in rural areas. Myanmar ranked 85th of 155 countries on the gender inequality index in 2014 (footnote 8), a relatively high ranking compared to other development indicators, but gender-related challenges remain. The maternal mortality rate declined from 580 to 282 during 1990–2014, but Myanmar still ranks low in international comparison. While the proportion of central and local parliamentary seats held by women doubled after the 2015 elections, the proportion is well below neighboring countries. While females outnumber males in higher education, their participation in wage employment is much lower.

12. **Natural resources.** Myanmar has relied heavily on natural resource exploitation for economic growth, energy production, and to sustain livelihoods. Forestry, agriculture, fisheries and mining have been critical to the country's development and economic transformation. However, the environment and natural resource base is under increasing stress from the expanding population, commercial exploitation, climate change, and natural disasters.¹¹ Unsustainable land and water management practices have resulted in decreasing forest cover, declining agriculture productivity, and poor water quality. Since the early 1990s, Myanmar has lost 10.2 million hectares of forest (over 15% of the country's land area). Urban residents suffer from deteriorating water supply, drainage and sewerage, and solid waste disposal systems, while urban air quality is worsening, particularly in Yangon. Myanmar is also highly vulnerable to natural disasters—floods, drought, cyclones, landslides, and earthquakes—with a resulting average annual loss of \$2 billion (3% of GDP). This has far-reaching implications, particularly for large numbers of poorer rural households, small businesses and farmers, and marginalized groups.¹² Myanmar is highly sensitive to climate change, including sea level rise, warming sea surface temperatures, salt water intrusion in river deltas, extended droughts, and the impacts of shifting weather patterns on agriculture. Efforts are underway to strengthen technical, legal, and financial capacity to reduce risk and mitigate the effects of climate change.¹³

IV. SHAPING THE FUTURE: STRENGTHENING THE DRIVERS OF INCLUSIVE AND SUSTAINABLE GROWTH

13. In view of these challenges, to achieve rapid, inclusive, and sustainable economic development Myanmar will need to successfully undertake and coordinate many interconnected reforms and dramatically expanded investments in numerous sectors, while strengthening institutional capacities and tackling crosscutting issues. While ADB's assistance in Myanmar will need to be focused (complementing support from other development partners), the analysis below provides a broad assessment of key priorities for

¹¹ Myanmar State of Environment Report, under preparation.

¹² United Nations Office for Disaster Risk Reduction. 2015. *Global Assessment Report on Disaster Risk Reduction 2015*. Geneva. Myanmar is ranked among the three most vulnerable countries to extreme weather events.

¹³ Government of Myanmar. 2015. *Myanmar's Intended Nationally Determined Commitment*. Nay Pyi Taw.

government-led reforms, drawing on ADB's conceptual framework for inclusive growth (footnote 1).

A. Building Infrastructure for Inclusive Growth

14. Infrastructure improvements will be particularly important to advancing rapid and sustainable growth to expand economic opportunities (pillar 1 of ADB's inclusive growth framework). Strengthened physical capital (including infrastructure) can help drive economic growth, particularly if policies and investments in improved quality and quantity of infrastructure capture economies of scale, while also broadening access to economic opportunities and public services. Reforms and investments related to energy and transport infrastructure will be especially critical in addressing key economic constraints, alongside strategic infrastructure investments in other sectors (e.g., agriculture and urban development). In addition to impacts on economic growth, infrastructure-related strategies and investments should prioritize equitable access (including via rural–urban connectivity) to help ensure that future economic prosperity is shared.

15. **Energy.** Despite having ample energy resources, Myanmar has the lowest electrification rate in Southeast Asia.¹⁴ Just over one third of households are connected to the national grid, and Myanmar has one of the lowest per capita electricity consumption in Southeast Asia. Foreign investments in oil, gas, and hydroelectric projects have largely aimed at supplying regional markets. The domestic electricity supply has suffered from inadequate investment, with an outdated energy generation and transmission infrastructure, and an incomplete national grid; financial constraints pose large challenges for proper maintenance, and for new investment in domestic supply infrastructure.

16. Electricity demand is expected to increase fivefold by 2030, especially if all homes gain access to electricity as set out in the National Electrification Plan¹⁵. ADB estimates that a least-cost strategy to meet the demand–supply gap by 2025 would require an annual investment of \$4 billion per year over 2016–2025. Financing such investment will prove challenging; foreign investors could be invited to focus on profitable electricity generation projects, while scarce budgetary and aid resources finance less profitable transmission and distribution projects. The new electricity law prompted a surge in unsolicited private sector electricity generation proposals, but progress in signing power-purchase agreements has been slow; by 2015, independent power producers accounted for only 10% of installed capacity. It will also be important to improve financial sustainability and efficiency. Promoting appropriate private sector participation in electricity generation and distribution may also lead to improved sector efficiency. Priorities include phasing in electricity tariff increases to safeguard the financial viability of existing investments, attract private investors, and reduce the budget burden of electricity subsidies. At the same time, it will be critical to prioritize equity and progress toward universal access.

17. **Transport.** After decades of underinvestment, Myanmar's transport systems are weak.¹⁶ Weak infrastructure undermines Myanmar's economic competitiveness, with 60% of trunk highways and much of the rail network requiring urgent maintenance or rehabilitation, and infrastructure supporting inland waterways lacking. Meanwhile, 20 million people lack

¹⁴ Government of Myanmar. 2016. *Myanmar Energy Master Plan*. Nay Pyi Taw.

¹⁵ Government of Myanmar. 2014. *Myanmar National Electrification Plan*. Nay Pyi Taw.

¹⁶ ADB. 2016. *Myanmar: Transport Sector Policy Note*. Nay Pyi Taw

basic road access. Moreover, the pressure on transport infrastructure is rising. Car and truck ownership doubled during 2012–2015; in the absence of corrective policies it could continue to double every 5–7 years. Yangon, which accounts for 70% of Myanmar’s registered vehicle fleet, has already seen travel speeds halved since 2012. A focused program of infrastructure investments and institutional reforms can reduce transport costs by close to 30%, ease production bottlenecks, and provide basic road access to close to 10 million people. The road subsector should receive the largest share of investment, but with appropriate policy attention, financial support, and operational reforms, the railway and river transport systems could also contribute to inclusive and sustainable growth.

18. Public investment in transport infrastructure will need to rise from 1.0%–1.5% of GDP to 3%–4% in the near term, in line with other countries at a similar stage of development. Maintenance must be prioritized. New investments should be made where they offer the highest social, economic, and financial rates of return, with special emphasis on the main national north–south and east–west corridors, and the main urban hubs. The government should outsource maintenance and investment projects to the private sector where possible, and apply clear procurement procedures when selecting contractors. The expanded infrastructure maintenance and development program will need to be financed by a combination of public savings, user charges, and government borrowing from bilateral and multilateral concessional sources. Private investors could also become partners, provided the government keeps its contingent liabilities within reasonable limits. Effort should continue to be made to corporatize the government’s transport service delivery units. These companies need to operate on a commercial basis with full autonomy from government, start with a clean balance sheet and adequate startup capital, and be governed by independent and competent boards. Consideration could be given to privatizing these companies in due course.

19. It will be important that transport reforms and investments promote inclusiveness, including through regional and rural–urban interconnectivity, and expansion of transport networks into underserved rural areas.

B. Improving Human Capital for Inclusive Growth

20. In Myanmar, half a century of underinvestment in education and health has stunted human capital development and led to skill shortages at all levels. Business surveys consistently cite a shortage of human capital as a leading constraint to growth.¹⁷ Current skills gaps and mismatches will become more acute as Myanmar attempts to transform its economy to focus on modern manufacturing and services. Continued progress in reforms and expanded investment in education and health will be critical to address human capital as a binding constraint to growth, and to promote equitable access to opportunities brought by growth (this is the second pillar of ADB’s inclusive growth framework).

21. **Education.** Challenges related to educational access, quality and relevance, and management obstruct the sector’s contribution to inclusive growth.¹⁸ More than 80% of youth

¹⁷ S. Tanaka, C. Spohr, and S. D’Amico. 2015. Myanmar Human Capital Development, Employment, and Labor Markets. *ADB Economics Working Paper Series*. No. 469. Manila: Asian Development Bank.

¹⁸ ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Loan for the Equipping Youth for Employment Project in the Republic of the Union of Myanmar*. Manila (Linked Document: Sector Assessment [Summary]: Education). <https://www.adb.org/sites/default/files/linked-documents/48431-003-ssa.pdf>

complete primary education, but only 44% complete lower secondary education, and just 18% complete upper secondary education. Although reforms are forthcoming, at present the outdated curriculum, pedagogy, and assessment are reflected in high dropout rates after primary school, a consistent two-thirds failure rate each year on the upper secondary education graduation exam, and the burden of private tutoring as the largest component of household spending on education.¹⁹ Employers complain that even youth who successfully complete secondary or higher education lack key critical thinking, problem-solving, and communication skills, leaving them ill-equipped for employment, and “untrainable”. At the same time, technical and vocational education and training (TVET) has not effectively met industry demands for practical skills (e.g., welding and construction-related skills). Prior to ongoing TVET reforms, challenges have included low access (especially for disadvantaged youth and workers), and outdated, supply-driven, and overly theoretical approaches.

22. These challenges have clear implications for the pace, nature, and inclusiveness of growth. It will be critical that ongoing reforms enhance access and completion rates, quality and relevance, and management across all education subsectors. Given the particular past neglect, reforms and investments may be especially critical in (i) secondary education, which is where the majority of youth exit the education system; it accounts for the largest share (47%) of entrants into even non-agricultural formal wage employment; and (ii) TVET, which currently accounts for less than 1% of workforce entrants and requires urgent expansion. Reforms that focus on quality will be critical in aligning secondary education and TVET with the critical thinking and practical skills needed in a modern economy. Important steps taken by the government toward such reforms include tripling public investment in education (from 0.8% to 2.0% of GDP) during 2011–2013 (although the level remains well below that of regional comparators, who spend about 5% to 6% of GDP on education). Importantly, the government (with support from ADB and other development partners) completed a Comprehensive Education Sector Review²⁰ to diagnose sector challenges and provide an evidence base for reforms and increased, better-prioritized investment under the new National Education Strategic Plan, 2016–2021.²¹

23. **Health.** Although Myanmar’s health indicators have improved, they still lag behind its Southeast Asian neighbors. Malaria is the leading cause of morbidity and mortality, and tuberculosis remains a leading cause of death. Non-communicable diseases—cancer, diabetes, cardiovascular diseases, and chronic respiratory disorders—are increasing, and particularly affect poor and rural populations. Cancer has become a major public health problem; most cases are found at a late stage, because of poor public awareness and inadequate early detection programs. These challenges reflect underinvestment that has undermined health system performance and forced households to finance over 70% of health expenditures out of pocket. Public health spending has increased from 0.2% of GDP in 2011–2012 to 1.2% in 2015, but remains the lowest in Southeast Asia; regional comparators spend some 3% of GDP on health. There are few health care centers and health care professionals. The absence of public services has resulted in expansion of private service providers, particularly in larger cities. A key health issue is access to clean water, particularly in rural areas, and for the poor. The share of the urban population without access to clean water has increased since the middle of the 1990s. The incidence of

¹⁹ ADB. 2015. *Support for Post Primary Education Development*. Consultant’s report. Manila. <https://www.adb.org/sites/default/files/project-document/201636/47177-001-tacr-02.pdf>

²⁰ Various reports produced as part of the Comprehensive Education Sector Review can be accessed at <http://www.cesrmm.org>.

²¹ Myanmar Ministry of Education. 2017. *National Education Strategic Plan, 2016-2021*. Nay Pyi Taw.

diarrhea among children under 5 years of age is considerably higher than elsewhere in Southeast Asia, and contributes to Myanmar's high child mortality rate.

24. The aim should be to improve health outcomes for all people, regardless of location, income level, ethnicity, and gender. To achieve this, key reforms will include (i) further increases in public expenditures on health; (ii) raising the efficiency of health service delivery while lowering the cost burden on poor households, including by prioritizing preventative measures, procuring drugs and medical consumables more efficiently, eliminating wasteful spending, streamlining institutional processes, and ensuring an adequate budget to maintain existing health care facilities; and (iii) encouraging an expanded, more effective, and equity enhancing private sector role in the health sector through a streamlined regulatory system that ensures appropriate standards of care. The Ministry of Health and Sports is finalizing a National Health Plan, which includes several of these dimensions and aims to advance progress towards universal health care to improve equity and reduce out-of-pocket expenditures.

C. Reducing Vulnerability through Strengthened Social Protection

25. The third pillar of ADB's inclusive growth framework recognizes the need for social protection—defined as comprising (i) social insurance; (ii) social assistance, including disaster risk reduction; and (iii) TVET and other labor market programs—to reduce vulnerabilities and prevent extreme deprivation. Myanmar's population (and particularly the poor and those in disaster-prone areas) is vulnerable to a wide range of shocks. The government has begun to establish a more comprehensive social protection system, and approved a National Social Protection Strategic Plan (NSPSP) in late 2014.²² The Ministry of Social Welfare, Relief and Resettlement has commenced pilot testing a maternal and child cash transfer program in Chin State (one of eight NSPSP flagship programs); it and other ministries are also developing new disaster risk reduction strategies, with technical assistance from ADB and other partners. Other ministries' programs that relate to the NSPSP include efforts towards universal health care (which would decrease out-of-pocket expenditures and impoverishment due to health shocks), stipends that target poor basic education students, and efforts to expand TVET programs that target disadvantaged youth.

26. Operationalizing the NSPSP will require careful prioritization, sequencing, and multi-ministry coordination in view of limited institutional capacity and budgetary resources. Various estimates place Myanmar's budget allocation for social protection at less than 0.5% of GDP, compared to an average 1.1% of GDP in low-income countries. In addition to increased funding, requirements include system building; strengthening of strategic alignments; and expanded investments in interventions that simultaneously contribute to social protection and other inclusive growth objectives, such as expanding TVET targeted at disadvantaged youth, and prioritizing local infrastructure that reduces communities' vulnerability, and increases their resilience to seasonal and disaster-related risks. Similarly, efforts to develop Myanmar's financial sector and insurance markets could contribute to the introduction of new and affordable instruments, such as health and unemployment insurance.

²² Government of Myanmar. 2014. *Myanmar National Social Protection Strategic Plan*. Nay Pyi Taw.

D. Reforming Institutions and Improving Governance

27. To achieve inclusive and sustainable growth, Myanmar will need to strengthen core institutions and governance, while promoting public sector transparency and accountability. Strengthening institutions to ensure macroeconomic stability and a stable and well-supervised financial system will be particularly important for securing inclusive and sustainable growth. Fiscal deficits need to be kept in check and financed through prudent borrowing from domestic and foreign concessional sources. Monetary policy should focus on keeping inflation within appropriate limits. The authorities will also need to build a financial system that intermediates efficiently between savers and borrowers, effectively manages risks, and universalizes access to finance. To support Myanmar's economic transformation, the government will need to maintain a competitive exchange rate that supports manufacturing and agriculture, even as the country exploits its comparative advantage in natural resources. Similarly, an open trade and investment environment will enable producers to attain economies of scale by selling to world markets and obtaining imported inputs at globally competitive prices.

28. Myanmar has already made progress in these areas. The government is taking a disciplined approach to public spending, while adjusting inter-sectoral allocations to better align with development priorities such as health and education. The government has also expanded the revenue base and rationalized commercial tax rates. In 2014, an office was established for large taxpayers to enable them to assess their own tax obligations; encouragingly, the new system reports 95% compliance. In a move to improved transparency and accountability, parliamentary debates on the budget are televised and the approved budget is published. Additionally, Myanmar took a major step toward improving transparency by becoming a member of the Extractive Industries Transparency Initiative; its first report on Myanmar²³ was a milestone in the transparency of Myanmar's extractive industries, which account for an estimated 6% of GDP and 24% of government revenues. These are important steps towards improving governance and accountability, and should continue. Transparency of public finances can be enhanced by publishing national and subnational budget outturns, audit reports on government finances, and detailed budget data using the standard international classification. Extra-budgetary government revenues and expenditures will need to be brought on budget, including donor-funded projects, military expenditures, and financial arrangements with state enterprises.

29. Institution building will also be critical to attaining peace, political stability, and justice, as well as effective decentralization. Finding a lasting and just political settlement to end civil conflict will be critical to inclusive and sustainable development. The country needs credible and legitimate political and justice institutions that provide rule of law, personal and economic security, and give voice to citizens. The democratic 2015 elections represented a critical historic milestone toward this end. In parallel with efforts toward a lasting peace agreement, Myanmar will need a system that transfers key fiscal responsibilities to local governments. This will require clarifying revenue and expenditure assignments, and agreeing on a basis for fiscal transfers from national to subnational governments. Subnational governments will also need to build their fiscal management and service delivery capability. To assist them, the national government should establish minimum

²³ Myanmar Extractive Industries Transparency Initiative. 2015. *EITI Report for the Period April 2013–March Oil, Gas and Mining Sectors*. Prepared at the request of the Multi-Stakeholder Group.

service delivery standards and encourage civil society organizations to evaluate performance and provide feedback to service delivery organizations.

30. Reform of the public procurement system is an essential part of the improvement of governance standards. Procurement reform is the foremost item on the agenda of the government's new Public Procurement Rules and Regulations Supervision Committee, which was established in 2015 and is developing a national procurement law, rules and procedures, and standardized bidding documents.

E. Promoting Private Investment and Trade

31. A vibrant private sector is essential to the development of a competitive, innovative, inclusive, and sustainable economy, and requires that a strong incentive and regulatory environment be established to empower private investors, while ensuring that private investment supports inclusive and sustainable growth. Improvements in infrastructure, human capital, and governance standards will help promote private and foreign direct investment, but must be accompanied by policies that promote trade, reduce trade transaction costs, lower entry and exit barriers, and facilitate access to finance. The main impediments to private business are a legal and regulatory environment that imposes costly entry barriers to new investors and provides weak investor protection, an underdeveloped financial sector that delivers limited financial services, inadequate infrastructure, a lack of skills and a segregated labor market, and inefficient state-owned enterprises with soft budget constraints.²⁴

32. Recent reforms addressing foreign trade and investment have resulted in increased foreign investment inflows, including in manufacturing. This will be central to diversification away from extractive industries. In addition, reforms have resulted in rapid tourism growth; if properly nurtured, tourism could become a powerful force in reducing poverty. But more remains to be done. Myanmar has the opportunity to take advantage of its location—between the People's Republic of China (PRC), India, and Southeast Asia—to (i) integrate its economy into regional and global value chains, and benefit from vertical and horizontal linkages; and (ii) leverage the scale of and potential infusion of technological, managerial, and marketing knowhow stemming from such linkages. Domestic competition, combined with open trade, will lower costs, increase efficiency, and raise the quality of goods and services. Domestic competition is now hampered by weak contract enforcement, while acquiring and registering property is expensive and cumbersome. Trade costs are also high, in large part because logistics services and customs clearance processes are slow and expensive.

33. A first step for Myanmar is to further reform its trade and investment policies. Tariffs are already low, but import and export licensing remains an impediment. Myanmar's commitments to the Association of Southeast Asian Nations Economic Community and the World Trade Organization require that these be eliminated, except in very limited instances where warranted by phytosanitary and safety concerns. In addition, customs procedures need to be clarified and simplified, with automated customs clearances, and border enforcement and tariff collection enforced. Lowering of entry, exit and trade barriers will discipline state enterprises in contestable markets. State enterprises should be required to abide by the same legal provisions as private companies and to publish audited financial

²⁴ ADB. 2016. *Myanmar: Indicative Private Sector Development Framework and Action Plan*. Nay Pyi Taw.

statements, and be expected to compete for government procurement contracts. Where possible, public–private partnerships should be encouraged as an integral part of the strategy to reform state enterprises.

F. Building an Efficient, Resilient, and Accessible Financial Sector

34. Promoting private investment for inclusive and sustainable growth will require a financial sector that provides firms, farms, and households with a range of financial services. Myanmar's financial sector is small in relation to the economy—the credit-to-GDP ratio is about 19%—and is dominated by state banks. Limited availability of finance is among the most frequently cited obstacle to doing business, and Myanmar does poorly in cross-country rankings of financial access indicators.

35. The CBM has made some progress in building an automated payments and settlements infrastructure, and developing a regulatory, and supervisory framework for the banking system. The government has initiated treasury bond auctions. A Financial Institutions Law was passed in early 2016, and its rules and regulations are expected to be promulgated in 2017. To encourage financial inclusion, the authorities approved a Microfinance Business Law in 2011, spawning a rapid expansion of over 200 microfinance institutions. In 2016, the government issued regulations allowing mobile network operators to offer payment services, including mobile financial services. Thirteen foreign bank branches have been issued licenses to serve the foreign business community but cannot conduct retail banking. The authorities have also issued a dozen licenses to domestic insurance companies. A stock exchange has been established, but only has four firms listed to date (February 2017).

36. These reforms represent progress, and have underpinned strong growth in credit to the private sector, but without more fundamental reforms the financial sector will be constrained in serving as an intermediary. For example, the CBM needs to strengthen supervision and gradually abolish the use of administrative tools such as interest rate controls. The four state-owned banks and policy banks require restructuring; consideration should be given to their closure, merger, and privatization. Ongoing implementation of the newly approved Financial Institutions Law is also important.

37. In addition to efficiency and stability, financial inclusion should be a key focus. Options include liberalizing the collateral requirements for lending; removing impediments to rural and agricultural lending; offering warehouse financing and other lending schemes for farmers; offering greater flexibility in interest rate margins and service fees for microfinance institutions; and allowing foreign insurance companies to enter the market.

G. Ensuring Environmental Sustainability for Sustainable Growth

38. Support for environmental sustainability is a key cross-cutting priority, and the government has begun to strengthen environmental policies, including by aligning new economic development policies with environmental conservation. It plans to amend existing laws and enact new laws on environmental conservation to conserve forests and biodiversity, reduce air and water pollution, control industrial waste, increase renewable energy, and mobilize participation of civil society organizations. The government has already established the Environmental Conservation Law (2012), the Environmental Conservation Rules (2014), the Environmental Impact Assessment Procedures (2015) and the National Environmental Quality (Emissions) Guidelines (2015), as well as the National Water Policy

(2014) and Land Use Policy (2016). New policies and strategies are under preparation, including a National Environmental Policy and Strategy Framework, a Green Economy Policy Framework, a National Climate Change Strategy and Action Plan, National and City Waste Management Strategies, and a National Framework for Community Disaster Resilience. Myanmar approved Environmental Impact Assessment Procedures in 2015, which will be a critical element in the country's environmental and social safeguard system.

39. The country's safeguard system will help ensure inclusive and environmentally sustainable growth. However, the government should hasten the development of more proactive strategies for sustainable natural resource management and environmental conservation. The government should take advantage of its ready access to international financial and technical assistance to build capacity for integrated natural resource management; to integrate sustainable land management within agricultural land use planning; and to target conservation initiatives in critical watersheds, biodiversity hotspots, primary forests, and coastal areas. The government should reinforce efforts to strengthen environmental enforcement; encourage water and energy conservation; increase environmental awareness; and build climate-resilient infrastructure.

40. Particular approaches to foster sustainable use, conservation, and restoration of natural capital include investing in (i) soils, efficient water use, and agro-biodiversity to improve agricultural productivity; (ii) watersheds and freshwater ecosystems; (iii) forestry and protected areas; and (iv) fisheries and marine and coastal ecosystems.²⁵ Options need to be identified for reducing demand by increasing efficiency of use (e.g., agriculture intensification, sustainable land management) and maintaining and increasing supply (e.g., protecting groundwater resources, and maintaining and expanding protected areas). Consideration must be given to removing incentives that drive environmental degradation, in particular open access resource management, and implicit subsidization through royalties that do not reflect full market values.²⁶

H. Advancing Gender Equity Across All Sectors

41. Increased gender equality is an important priority—it raises national productivity, promotes inclusion, builds social capital, makes institutions and policies more representative, and increases the resilience of households to shocks.²⁷ While Myanmar has made important strides in increasing equality of opportunity for women and girls, much remains to be done. Embedding women's rights and gender equality in policies and procedures in the private and public sectors may be the largest challenge.²⁸ Every initiative should be analyzed from the perspective of its impact on gender equality, and statistics should be gender disaggregated whenever possible. Some infrastructure priorities—such as rural electrification, water and sanitation, clean energy sources (especially for household cooking), and rural transport—yield both high economic and social returns and promote gender equality. Similarly, gender-sensitive early childhood programs and reproductive health initiatives yield high economic and social returns. The government should consider

²⁵ Natural capital refers to the country's natural resources and ecosystems, including those that are renewable (such as forests, water and agricultural farmland), and non-renewable (such as minerals and fossil fuels).

²⁶ D. Raitzer, J. Samson, and K.Y. Nam. 2015. *Achieving Environmental Sustainability in Myanmar*. ADB *Economic Working Paper Series*. No. 467. Manila: Asian Development Bank.

²⁷ ADB et al. 2016. *Gender Equality and Women's Rights in Myanmar: A Situation Analysis*. Manila.

²⁸ These should include (but not be restricted to) socioeconomic rights, such as property ownership (including land) and access to education, health, and security.

expeditious enactment of the law to prevent violence against women and increase women's access to justice (especially in rural areas). Women and girls will benefit the most from successful peace talks, which argues strongly for their inclusion in conflict resolution initiatives, as well as post-conflict planning.

I. Other Sector-specific Priorities

42. In parallel with the broad areas outlined above, strategic reforms in areas such as agriculture, water and sanitation, urban development, and information and communication technology (ICT) can make important contributions to inclusive and sustainable growth.

43. In agriculture, the cross-sectoral policies discussed above will help farmers gain access to critical public goods and services—infrastructure, extension services and TVET, market information, and inputs. It is equally important, however, to recognize that farming is a private sector activity, and markets need to be permitted to send price signals to farmers and traders. Another key reform involves enhancing property rights over agricultural land. In designing land reforms, the government needs to consider the interface between agricultural growth, environmental protection, and social security in rural areas. At a minimum, the government needs to stop land confiscation and reclassification until it conducts a cadastral survey, provides registered titles to owners of farmland, and ensures that changes in land classification are transparent and in accordance with the law.

44. The provision of clean water and sanitation are accompanied by huge institutional, capacity and investment challenges. About one third of the population lacks access to clean water, and one quarter does not have access to modern toilets. Urban water systems are old and supply is intermittent. Raw sewage and septic tank effluent flow through roadside drains, contributing to the spread of waterborne diseases. The government needs to gather information on the coverage of existing water supply and sanitation services. Initially, large public investments will be needed to increase water supply services and extend these to cover low-income, high-density urban areas. This will require strengthening government capacity, exploring the potential for cost recovery, and considering the use of public–private partnerships. Finally, existing laws need to be enforced to ensure the proper treatment and disposal of mining and industrial effluent.

45. Well-planned urban development is important to ensure that ongoing rapid urbanization supports inclusive and sustainable growth. Today, one in three people live in cities; by 2040, it will be one in two. The growing urban population will need to be served with housing, roads, drainage, electricity, water and sanitation, and medical and educational facilities. To meet investment and recurrent expenditure obligations, local governments need to improve their fiscal strength and be supported with adequate fiscal transfers from the national government. A review of the institutional and regulatory arrangements for land use planning and management is needed, with urban plans that maximize the advantages (and minimize the disadvantages) associated with density. It is important to achieve a balance between business, residential, commercial, and recreational facilities. Innovative financial instruments will be needed to increase the availability of affordable housing and support the development of livelihoods. Participatory and consultative approach will help complement scarce government planning and administrative resources.

46. Continued and carefully formulated reforms related to ICT can also advance inclusive growth. Myanmar has made impressive strides in developing a modern telecommunications system. Continued progress in telecommunications and selective

investments in other areas of ICT can help reduce communications costs, and open opportunities for the use of new technologies and improvements in service delivery and governance in various sectors.’ Despite impressive growth in mobile phone penetration since 2014, Myanmar’s ICT development is still in its infancy. The government has prepared a master plan that prioritizes Myanmar’s development into a digitally connected nation by 2020, with goals of providing mobile telephony to over 90% of the population, internet access to over 85%, and high-speed internet access to over 50%. The government’s planned actions to achieve these objectives include preparing a spectrum management plan, launching a national fiber optic policy, developing universal service obligations, ensuring laws and regulations are technology and service neutral, and establishing an independent Myanmar Communications Commission.

V. RECOGNIZING THE RISKS

47. Although considered unlikely, the largest risk facing the reform agenda is a reversal of the fragile democratic transition. Equally central to political stability will be the ability of the government to secure a lasting peace with ethnic armed groups, and ending communal tension. A national peace agreement would inevitably require an arrangement that shares political and economic power between national and subnational governments, which would enable fiscal decentralization and give subnational governments increased responsibility for delivery of key public services. The government’s task of nation building while implementing economic reforms is complicated by weak capacity in basic functions, such as public financial management and public service delivery. In managing public finances, weak controls, a lack of transparency, and limited oversight pose the risk of corruption and mismanagement of the fiscal system.

48. In addition to internal risks, Myanmar’s lack of economic diversification and continued reliance on commodities makes it vulnerable to external shocks. While the growth of manufacturing and services is a government priority, the economy will continue to be buffeted by shocks in world markets. The PRC’s proximity and size as an investor and trading partner makes Myanmar particularly vulnerable to the trajectory of the PRC economy.

49. While Myanmar is highly exposed to natural hazards, appropriate policies and preparation can ensure that these hazards do not lead to disasters. Coastal regions are at high risk of cyclones, storm surges, and tsunamis. Much of the country is exposed to floods, landslides, earthquakes, droughts, and fires. Poverty is often both the cause and consequence of natural disasters. Over-cultivation, poor soil management, and the use of firewood for fuel lead to deforestation, floods, and landslides, which in turn exacerbate problems faced by the poor. Resilience to disasters can be increased, provided needed interventions are embedded in decision-making and larger governance processes at all levels.

VI. SHAPING ADB’S PROGRAM

50. The preceding analysis has identified a series of broad priorities for ADB to help promote inclusive and sustainable growth: (i) investing in key infrastructure, especially energy and transport; (ii) developing human capital; (iii) reducing vulnerabilities via social protection; (iv) reforming institutions and improving governance; (v) promoting private investment and trade; (vi) increasing the strength and inclusiveness of the financial sector; (vii) advancing gender equity; and (viii) ensuring environmental sustainability. Additional

priority areas for inclusive growth include agriculture and, more broadly, rural development; urban development; and new technologies and ICT and associated applications with high potential to accelerate the country's development trajectory and translate relatively quickly in improved livelihoods.

51. Myanmar's unique development context requires that ADB's country strategy and program give particular attention to key principles, including: (i) country priorities—ADB's strategy and program should closely align closely with government priorities, and be planned and delivered in close coordination and cooperation with other development partners and key stakeholders; in so doing, it should ensure that it does not impose an undue burden on the government's scarce administrative capabilities; (ii) capacity building—ADB should pay due attention to the need for capacity building, recognizing that this is a long-term process that requires project-by-project efforts that need to be increasingly complemented by initiatives to develop country systems; and (iii) context sensitivity—building on ADB experiences in fragile and conflict-affected states, ADB's strategy and program should ensure a context-sensitive approach, requiring the application of participatory development and conflict-sensitive ideas to the social and political factors surrounding development; it will involve a detailed analysis of the political economy, state–society and state–non-state relations, and capacities.

52. ADB's country partnership strategy and program must be aligned with national priorities and policies; be closely coordinated and embody strategic partnerships with development partners, civil society, business and other key stakeholders; build on economic and sector knowledge, and effective networks and partnerships; and provide sufficient flexibility to respond to evolving needs and priorities in Myanmar's highly complex and rapidly changing development context.