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Choosing Survival:

Finding a Way to Overcome Current Economic and Political Quagmires in Myanmar

Prepared for

Proximity Designs | Myanmar

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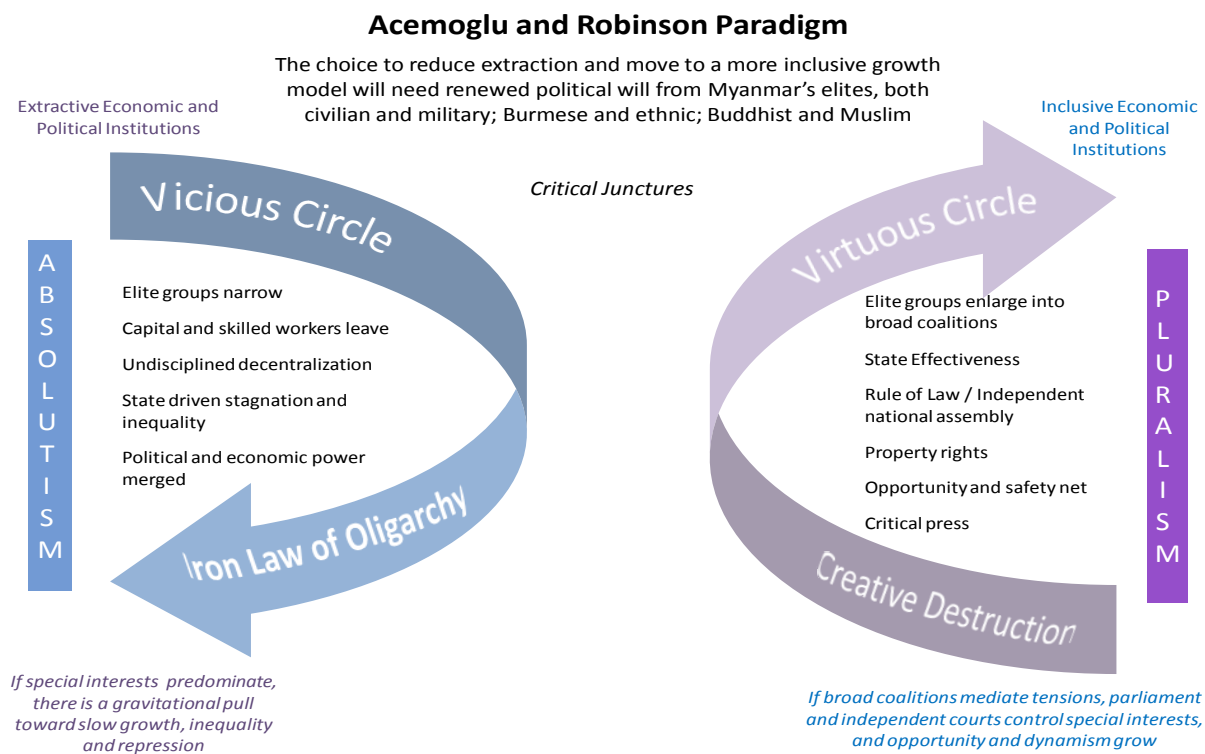
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Background

Myanmar faces a choice between maintaining some version of the *status quo* in which the military holds sway while allowing some limited forms of democracy or creating a genuine shift to a more open and inclusive system. This is not just a choice about who gets what share of the national output or even how fast that output grows, though that is part of the choice. The main choice is between national survival and unity or weakness and division. Myanmar may end up more like Pakistan than Turkey.¹ To avoid this, it needs a broad coalition of interest groups that support federalism, resource sharing, and taxation of resources for productive public investment. Such a change requires a fairly elected government and a stronger rule of law, including protection of minorities and those with wealth, however acquired. The current path is producing religious tension, very little if any growth (in spite of good intentions and high reported GDP growth), and ethnic and religious conflicts. The following graphic summarizing Why Nations Fail, a recent book, illustrates the situation. However, Myanmar is leaning to the left side of the diagram – closer to failure than success.



There has been much upbeat commentary about Myanmar, seeking to beat the drum for a new emerging market. Long years of political isolation from all but some Asian countries have meant very

¹ Pakistan is a country in which the military retain a large role in many aspects of governing, including the economy. It has experienced slow (2.5% per capita GDP) growth since 1990, an insurgency, and much corruption. In Turkey there is faster growth, a “normal” role for the military, and peaceful and democratic elections. The sum of governance indicators for Pakistan is 106 (lower than Bangladesh); Turkey is over 300 (better than Thailand).

low levels of western investment. There is no doubt that western aid and investment levels will rise, but it is crucial to understand where Myanmar is starting from. It is not just poor; it is still partly dominated by the military. It has never been a peaceful, united nation. There has been no normal system of public finance. Basic structures of government have atrophied as the military has displaced almost every other group, aside from their business associates. Negotiations to end civil conflict in the ethnic areas are undermined by major offensives. Endemic religious violence appears to be instigated by those who calculate the disturbances work to their advantage. These are dangerous trends that could derail the process of nation building and successful development. If the current situation of decisive military influence and extraction persists, the chances for economic and political success are low and even effective national survival is in question. A choice to direct huge mineral resources to national development is needed – and this can only be accomplished by a broad coalition supporting federalism.

Box One: A Note to Those Who Dislike Federalism

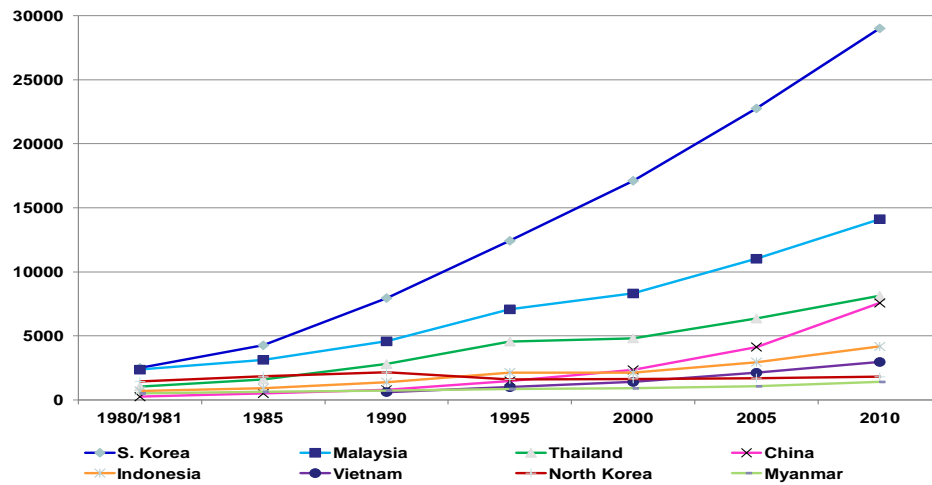
The Army has fought for over a half century to keep Burma and then Myanmar united. It has seen federalism as separatism, the division of the nation. Even using the word causes many to question the legitimacy of the speaker or writer. The argument in this paper is that a type of negotiated federalism – in which the army is a partner to the negotiations – *is necessary for the survival of Myanmar as an independent nation*. Either the nation stays in tension and conflict and is gradually dominated or it becomes a developmental state and grows stronger. If natural resources are used for military or private ends rather than nation building, the results will be poverty, instability and an effective loss of national sovereignty. The Army has to become smaller as peace takes root, but also more professional and capable. A scholar and friend and resident of Burma, Professor J.S. Furnivall, wrote in 1931: “If as is but too probable, the obstacles prove insurmountable... [it] can only be a matter of time and, after a period of anarchy more or less prolonged, our descendents may find Burma a province of China. China has a great civilization and it is quite possible that the absorption of Burma by the Chinese will be the best destiny for the Burmese.” (*An Introduction to the Political Economy of Burma*, page xxiv.) Giving some local autonomy and share of resource revenues to fairly elected governments in ethnic states (or divisions) is the only way to keep the nation intact and independent. The successful decentralization of Indonesia with its own regional pressures shows this is not just academic speculation.

This paper lays out the facts about where Myanmar has been, where it is, and what kinds of changes are needed to create conditions for unity, peace and inclusive and sustainable development. While the analysis in this paper is cautionary and often negative, its purpose is to solve problems, not complain. Creating a coalition for nation building will be easier if the poor current situation is better understood. Achieving the desired goals will not be easy and will likely take longer than many understand or imagine. Avoiding narrow coalitions that would continue current extractive policies is necessary to move forward.

However, a feasible path exists and many current government policies are meant to put the nation on that path. This paper aims to contribute to those efforts and build on the progress already made.

Past Levels of Performance

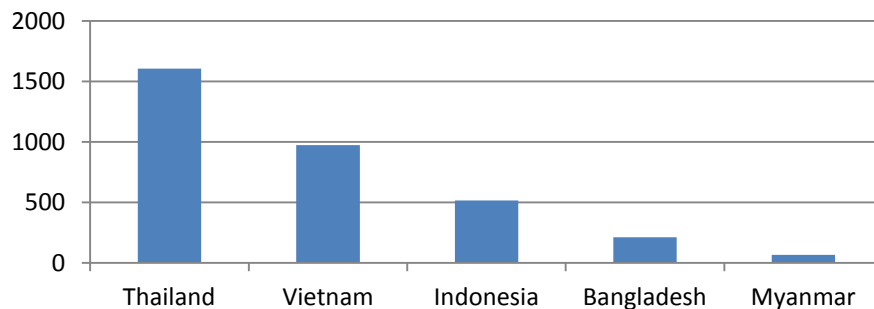
GNI Per Capita (PPP), at current international \$ for selected Asian Economies Over 30 Years



Source: ADB and World Bank websites; for Myanmar, Ash Center estimates

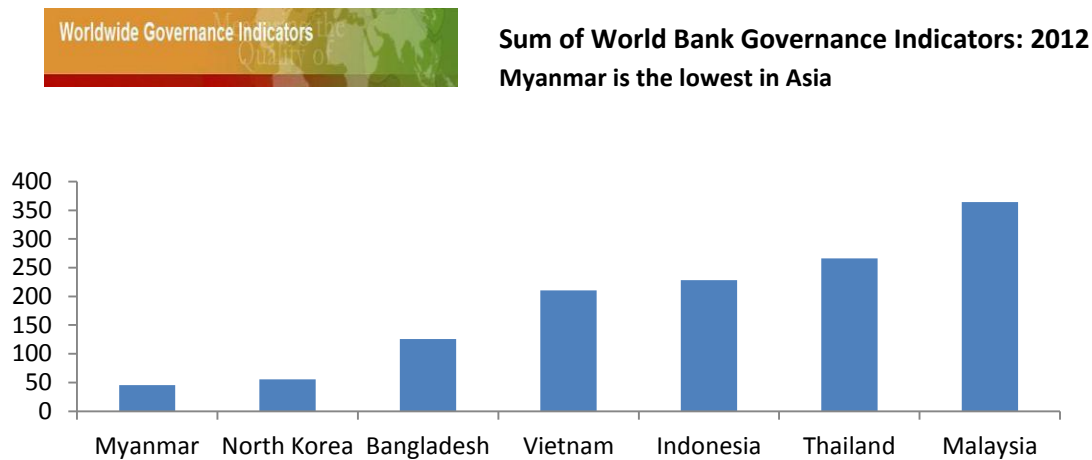
This graph shows per capita GDP in purchasing power parity (equivalent international price terms) for selected Asian nations since 1980. Myanmar – the bottom light green line – has grown, but very slowly. Its PPP GDP per capita in 2012 was \$1400 according to the IMF. Bangladesh was \$2000; Cambodia was \$2400; Vietnam was \$3500 and Indonesia was \$5000. Since Myanmar (then Burma) was richer than Indonesia in 1960, it is clear that the last decades have been ones of very modest progress. Another way of showing this is to graph the change in electricity consumption per capita since 1990. This shows the increase in total electricity sales divided by population from 1990 to 2011. (Source: World Bank data bank.)

Change in kWh per capita, 1990-2011



It is noteworthy that Bangladesh is one of the poorer nations in Asia and Indonesia is notorious for its underinvestment in power and infrastructure. Even so, the change in per capita electricity was three times greater in Bangladesh than in Myanmar while Indonesia gained seven times as much. This measure avoids many of the data problems that bedevil attempts to estimate GDP per capita.

One reason for this underperformance is that the past governments in Myanmar were extractive and placed a low priority on funding even basic infrastructure, much less health or education.² This was possible in part because economic data were often falsified and partly believed – economic growth rates of 12% a year were regularly recorded even when electricity per capita barely grew and rice per capita output was falling! World Bank governance indicators provide a useful measure of Myanmar’s level of governmental functioning. These are six dimensions of governance measured in percentiles³, so a maximum score would be 600. As the graph on the next page shows, Myanmar scored 45 out of 600 in 2012 – similar to the North Korean governance score! Rapid growth with this very low level of governance is all but impossible since uncertainty deters investment.⁴



While budget data have been mostly secret and are still not fully disclosed, the World Development Indicators 2012 report total health care spending in 2010 was 2% of GDP and only an eighth of that was publically funded – a mere 0.25% of GDP. Bangladesh spent 3.5% of GDP on health and public spending covered one-third of that, or 1.2% of GDP. (Cambodia is higher still.) Myanmar’s share of public health spending is among the lowest in the world. Similar recent data for educational spending are not available, but in 1999, only 6.6% of GDP per capita was spent on a secondary school student. Bangladesh

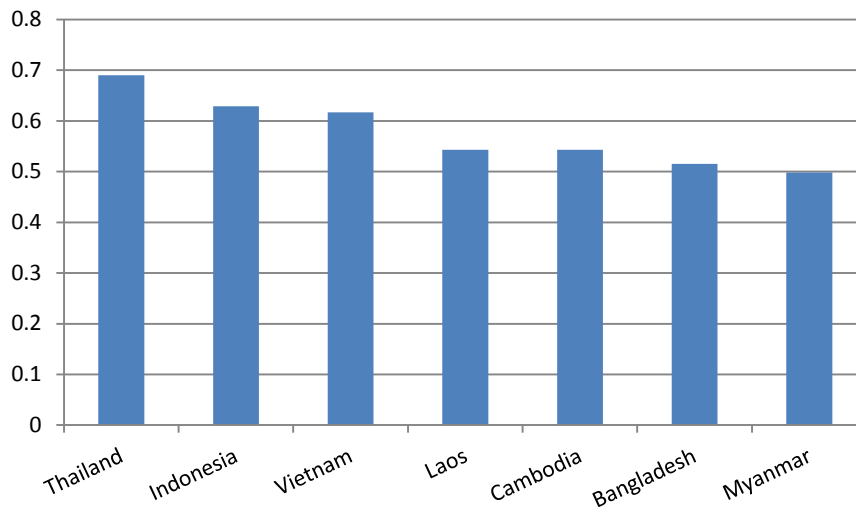
² This underinvestment is being corrected as gas revenues are finally collected at a reasonable exchange rate, but tax revenues from other minerals are still well below levels typical in other nations.

³ The six types of governance are 1. Voice and accountability; 2. Political stability and absence of violence; 3. Government effectiveness; 4. Regulatory quality; 5. Rule of law; and 6. Control of corruption.

⁴ Quality investors want a level playing field, clear rules, security against confiscation and a government that is more like a fair referee than another player seeking to drain their business of revenues. Crony investors want the opposite – special favors and exclusion of competitors, even if it means sharing revenues with those making and enforcing the rules.

and Cambodia then had about 12%. Things since then have not improved much if at all, so it is safe to conclude that public spending on health and education is among the lowest in Asia and possibly in the world.⁵ Certainly the sporadic shutting down of the universities has severely depleted the supply of skilled workers and managers. The graph on the next page shows the UNDP calculated Human Development Index for 2012. This is an index that reflects levels of education, health and income per capita. Myanmar is lower than Bangladesh and Cambodia in stark comparison to a period after World War II when it was among the most educated nations in the region. Even worse, many of the most educated have left Myanmar and the composition of the workforce reflects both the past decades of underinvestment and the migration of educated workers to neighboring and more distant nations.

2012 UNDP Human Development Index



The miserable governance in the recent past, lack of electricity and failure to train the work force has led to minimal levels of foreign direct investment. According to the 2012 World Investment Report by UNCTAD, Myanmar had only \$200 per capita in its stock of FDI, mostly for raw materials. Cambodia had nearly three times as much and Vietnam four times. Even landlocked Laos had twice as much FDI per capita. Japan, which sees itself vying for influence in Myanmar with China, has been boosting its aid levels but Japanese businesses have been reluctant to invest in Myanmar even as they exit China in search of alternatives.⁶

There has been massive government mal-investment and underinvestment. Billions of dollars were spent on Nay Pyi Taw (which itself is questionable), but the road to the new capital from both Yangon and Mandalay did not use reinforced steel rods, so trucks cannot use the road. This greatly diminishes the economic value of that investment. Regulations kept cell phones so expensive that Myanmar lagged

⁵ A recent sampling of some rural areas with a functional literacy test found that about half of rural adults could answer all three simple questions correctly when the answers were clearly written and in front of them. This was not a national sample but suggests that official literacy data, with more than 90% literacy, may be overstated.

⁶ The amount of licensed (not realized) FDI from 1988 to July 2012 was \$43 billion, largely from Asia excluding Japan. China including Hong Kong alone accounted for 48% of that total and Thailand for 23%.

behind Africa. The cell phone situation is improving, but mobile coverage in 2012 was still only 11 per 100, compared to 64 per 100 in Bangladesh.⁷ Internet use in 2012 was 1 per 100 people. Trucking costs are five to ten times higher per ton-kilometer than in Thailand or China according to surveys by Harvard researchers. Except for natural resources and \$700 million of garments⁸, there is little export activity. In short, the country lags well behind its neighbors in almost every relevant dimension.

Ethnic and Religious Violence

It is perhaps not surprising that in a country where income is so concentrated and widespread progress so limited, there has been conflict. The long-running ethnic conflict, going on and off since the 1950's, appeared last year to be drawing to a close except in Kachin state where 150 battalions fought the Kachin Independence Army over jade and trade routes. This created nearly 100,000 internally displaced people and resulted in dozens of villages being destroyed. There is yet another cease fire, but combat has flared up again as of mid-September and the threat of land seizures persists⁹. The cease fires, first negotiated in the 1990's, basically allowed the Burmese Army and the armed ethnic groups to unevenly split the resource rents, smuggling, drug profits, and road tolls and other "contributions" but held back any real progress in the ethnic states. The lack of economic progress and threat of violence contributed to the millions of workers who moved to Thailand and other nations. Many of these are skilled workers (Singapore is said to have over 40 thousand engineers from Myanmar) and labor shortages are reported in some of these ethnic states, even where it is peaceful. If the "solution" to this conflict is an imposed peace with continued extraction, it would be a huge negative for development and national unity. Such an imposed settlement would result in continued economic stagnation (except for continued resource extraction) and migration.

In addition to the ethnic conflicts there has been a recent upsurge in anti-Muslim violence. At first this was largely confined to Rakhine state next to Bangladesh where radical Buddhist monks suggested with little evidence that there had been uncontrolled migration and rapid population growth among Muslims due to multiple wives, large numbers of children, and conversions.¹⁰ One monk in particular, Wirathu, had been jailed for his inflammatory preaching but was released after the 2007 suppression of the Buddhist monks by the military government. He is now the head of a large monastery and enjoys tacit government support.¹¹ Muslims account for only 4% or so of the population (a new census is needed, but that ratio stayed the same from 1929 to 1983 and conditions have not improved in Myanmar

⁷ Data from: <http://www.itu.int/en/ITU-D/Statistics/Pages/stat/default.aspx>

⁸ While garment exports have risen in recent years, Cambodia in 2012 had garment exports of \$307 per capita while Myanmar in 2012/13 had less than \$12.

⁹ The military is still taking land throughout the nation, often with few legal niceties. See: <http://www.bangkokpost.com/business/news/366469/myanmar-s-land-grab-problem>

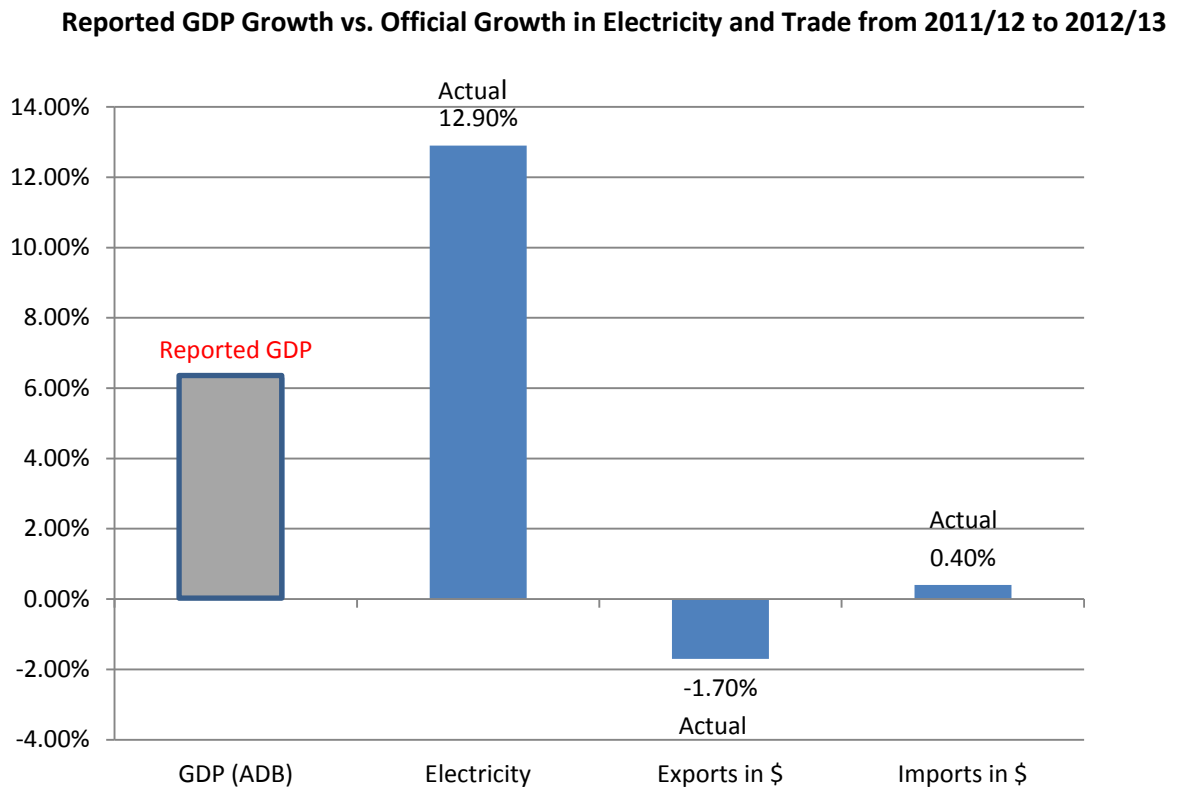
¹⁰ Indeed, the 1978 "King Dragon" operation under Ne Win had produced a flow of 250 thousand Muslim refugees to Bangladesh, contributing to a net outflow of migrants to India and Pakistan.

¹¹ A recent agreement between Wirathu and a Muslim leader is unlikely to sustainably improve conditions on the ground. Effective prohibitions on voluntary inter-marriage are still supported and Rakhine state is excluded from the agreement. Rohingya – or Rakhine Moslems for those who dislike the term Rohingya - who are born in Myanmar are still without citizenship. "Spontaneous" mobs that burn, rob and murder Muslims are also unlikely to be much influenced by this agreement.

relative to Bangladesh since then) and the organized violence with little official protection or subsequent prosecution suggests that at least some elements of the security forces allow or support these actions. It goes without saying that systematic persecution could attract international *jihadi* attention. This is not what the tourist industry, bridges, pipelines or power stations need.

Current Economic Progress

A reasonable retort might be that as bad as things were in the past, the present is much brighter. For example, the ADB and IMF estimated real GDP growth of 6.3% in 2012. Compare that estimate of GDP growth with other official Myanmar government data: (Source: <https://www.mnped.gov.mm/>)



This extreme slowdown or even decline in trade is not at all consistent with the brisk growth reported by the ADB and IMF. In particular, falling dollar exports are not usually consistent with rapid growth.¹² Recently revised electricity output does indicate growth, though it is not clear if the growth in grid electricity displaced diesel generation.¹³ A lack of economic growth makes political settlements much more difficult as it is hard to negotiate gains for each group if the pie is not increasing much or even

¹² Gas exports to China, starting in later 2013, will bump exports up but not change the overall picture.

¹³ This is, however, a complicated topic. See Appendix I for an in-depth discussion.

shrinking.¹⁴ This lack of progress also reflects a lack of governance – the inability of the government to control fully the levers of power. This inability to prevent blackouts or to extend power lines will weaken the legitimacy of the government as well as curtail the rate of growth and jobs.

Land and Agriculture

While Thailand and Vietnam each export five to ten millions of tons of rice a year, Myanmar has not been able to sustain even one million tons of exports a year or one third as much as it exported in the 1930's.¹⁵ Independent estimates of rice production suggest that per capita output has been declining for some time.¹⁶ There are many reasons for the low productivity in agriculture, but one of the most important is the precarious status of land use rights. Millions of acres have been taken over by officials for little or no compensation, for use by the military or influential domestic or foreign investors. This threat lies over most farmers, who are understandably reluctant to invest much in their land if it will only be taken away. The problem is most severe in ethnic areas where land ownership has historically been communal rather than individual, and so farmers lack deeds. This land is said to be “unoccupied” by those taking it, who then expel those who have been farming it for generations. This communal system needs legal recognition. It is difficult for local groups to research and raise these issues because land takings are one major source of revenue or wealth for the military and officials. This issue was not really raised in recent USAID reports on agriculture, nor have the World Bank, ADB or FAO emphasized it. Note that estimates of resource flows on page eighteen of this paper do not include estimates of the millions of acres taken by military and official personnel, nor the billions of dollars of timber sold.

Exchange Rates and Finance

The real exchange rate of Myanmar has been a problem for the economy and is still troublesome in spite of some recent movement. The nominal exchange rate was 1100 kyat to the dollar in 2005, fell to below 800 in 2012 and recovered to 970 kyat in 2013. However, during this period domestic prices more than doubled while global inflation was modest, less than 3% a year. Inflation in developing Asia rose less than 5% a year, half of Myanmar's rise. The result is that it is cheap to import manufactured goods

¹⁴ The findings that food poverty had fallen in half from 2005 to 2010 and that food intake per person was higher than in Sweden (from the 2010 Household Survey) are equally implausible.

¹⁵ While there was a huge jump in rice shipments to China in 2012 to take advantage of high Chinese support price for domestic rice, this has depleted stocks in the country. Rice exports dropped 38% in the April to October period of 2013 vs. 2012 according to the Yangon Times. In addition, the Japanese have offered to buy rice but Myanmar seems unlikely to be able to respond due to domestic shortages... (http://www.mizzima.com/business/trade/9891-myanmar-uncertain-of-fulfilling-japan-s-offer-to-import-rice?utm_source=ISEAS+Library+Daily+News+Alert+-+22+August+2013+&utm_campaign=Info+Alert+20130822&utm_medium=email)

¹⁶ “Revitalizing Agriculture in Myanmar”, p.15, (<http://www.ash.harvard.edu/extension/ash/docs/burma.pdf>) shows rice output per capita falling from 228 kg in 2000 to 201 kg in 2009. In 2012/13 according to the August 2013 Rice Outlook published by the U.S. Department of Agriculture, output had fallen further to only 180 kg pc.

and less profitable to export them or to compete with imports.¹⁷ While a full adjustment to the real exchange rate of 2005 would imply an exchange rate of 1500-1600 kyat per dollar, it is likely that some real improvements in infrastructure or reduced trade barriers would allow a more modest adjustment to perhaps 1100 to 1200 kyat per dollar. Still, unless strong world raw material prices support rural incomes and better infrastructure attracts more labor-intensive exporters, the current exchange rate will remain a drag on many non-resource economic activities. The ability of the Central Bank to manage the exchange rate remains limited and if increased capital inflows or gas export earnings cause the rate to strengthen again, it will require some effort to prevent a further loss of competitiveness. Recent growth in imports while exports decline suggest this is already an issue.

The state of finance in Myanmar is primitive. Most business is on a cash basis. Banks provide very limited credit to firms – private credit is 10% of GDP in 2012/13 according to the IMF, while deposits are 31%, with most remaining credit going to the government or directed credits.¹⁸ The ability of banks to assess risk or to extend lending on commercial terms to farmers or small and medium firms is very limited. Most private lending is for trade or real estate. Commercial bond or equity markets do not exist. Until recently, even using credit cards was difficult and expensive due to sanctions on Myanmar banks. A period of joint venture banking with foreign and local banks followed by more open opportunities is planned, but the system capacity will be limited for the next several years.

Proposed Solutions

The key to creating a future in Myanmar is realizing that improving the fundamental direction of the country depends on a fair settlement of the ethnic conflicts and defusing of the religious violence. The ethnic states want and should be able to negotiate the right to establish states with limited autonomy and self-elected governors within the nation. To have meaningful self-government, states will need revenues and one way to accomplish that is for them to get a share of mineral revenues so that they have some fiscal base. In various papers¹⁹ this is called the “new federalism” to distinguish it from “federalism” which was forbidden to mention in the recent past because it was assumed by the military that it was a code word for dissolution of the nation. It is argued that, to the contrary, “new federalism” is a way to secure the peaceful unification of the nation.²⁰ If instead, the ethnic states are treated by the Army as the Chinese treat Tibet, there will be a need for a large military, limited civil rights, and continued extraction. These conditions are incompatible with the development of democracy and

¹⁷ Garment exports have jumped from \$379 million in 2010/11 to \$695 million in 2012/13, though remain a small fraction of garment exports from Cambodia which were \$4.6 billion in 2012. Decreasing export barriers help to explain the recent growth. Cambodian per capita exports of garments were \$307 compared to \$12 for Myanmar.

¹⁸ In Vietnam, private credit/GDP is over 90% in spite of starting from a very low level in the 1990's.

¹⁹ See: “Creating a Future: Using Natural Resources for New Federalism and Unity,” and “Against the Odds: Building a Coalition” at: (<http://www.ash.harvard.edu/extension/ash/docs/creating.pdf>) and (<http://www.ash.harvard.edu/extension/ash/docs/against.pdf>)

²⁰ It is significant that the powerful speaker of the lower house, U Shwe Mann, has spoken out publically in favor of some form of federalism. This increases the chances of a successful ethnic settlement.

inclusive growth and, as previously argued, may be incompatible with long-term national independence and survival.

The religious tensions need to be de-escalated in at least two ways. One is to strengthen the rule of law. The President has made it clear that all citizens are protected by law and minorities should not be subject to mob action. Yet there have been indications of official complicity or at least inaction in many incidents and most of those arrested have been minorities, not Buddhists. This is in spite of most of the violence being directed against the minorities. Moving to apply the law even-handedly and preventing mob violence is a first and necessary step. If Muslims are attacked, it may be that Christians would be next. This kind of sectarian aggression will have similar negative impacts as the ethnic conflicts.

However, a second step is needed. One reason the rabble rousing rhetoric gains traction is that there has been so little economic progress. If prosperity and opportunity were seen to be rapidly spreading, there would be much less salience to these hateful messages. The government will have to put in place policies that start moving the economy broadly forward and make Myanmar a more attractive place to invest beyond raw materials and real estate. This will include reducing red tape and corruption, creating better power supplies and infrastructure, seeking to extinguish the “road tolls” that raise internal transport costs far above normal levels, and working to attract back and train more skilled labor. In addition, the security of land holdings remains a major issue. As previously mentioned, farmers know that a military officer or government official can take their land for little or no compensation if it is wanted for their purposes – including giving it to a crony investor. This too tends to make the majority resentful and makes it easier to incite violence. This is also a rule of law issue.

The key to making this work is creating a modern public finance system that fairly taxes the excess profits created in exploiting raw materials. If the \$6 to \$10 billion estimate of jade exports in 2011 is correct, the taxes and fees paid to the government amounted to well under 8% of sales when they should have been at least 50% because the cost of production is less than 2% of sales.²¹ This alone would provide billions of dollars a year in additional government revenues. If this principle were expanded to cover other raw materials, there would be adequate amounts to fund critical investments and services in both the ethnic states and central Myanmar. Without such a switch, the elites would remain so wealthy that elections, officials and judges would be bought (and the government would be so poor) that democracy would lose its meaning. This insight was captured in a recent book, “Why Nations Fail” whose fundamental message can be summed up in the graphic appearing on the first page of this paper.

This graphic emphasizes the importance of developing a political dynamic which supports growth and equity. There is little doubt that Myanmar is at a critical juncture and will decide in the next few years if it broadens its politics and economics to become more inclusive or remains crony-ridden and extractive. The past elites may well remain in power, but would rule a very poor and failing nation which would fall increasingly under foreign influence. If a decision is made to move towards the upward arrow and

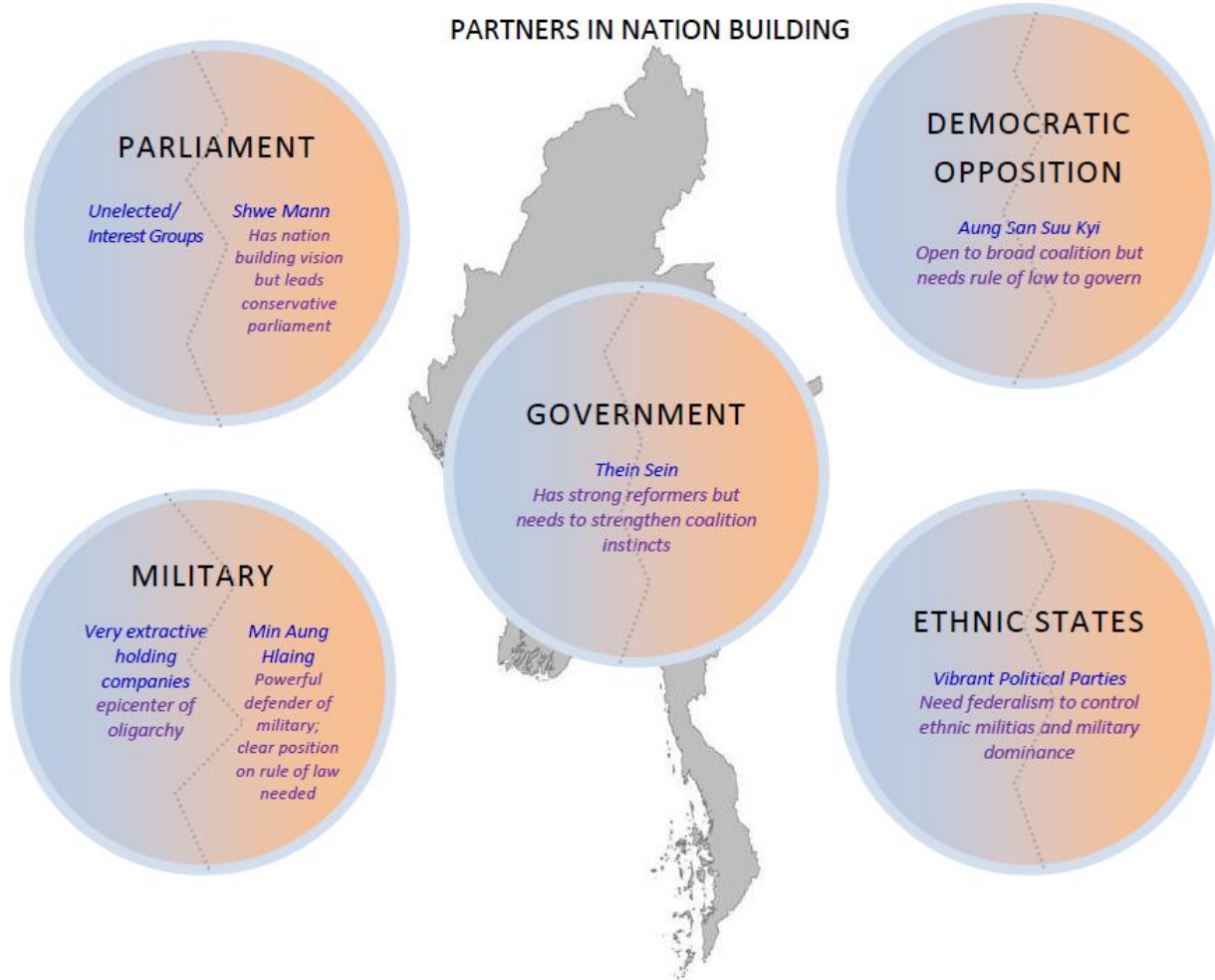
²¹ Precious stones such as jade have low extraction costs, so the ratio of government revenues to sales can be higher than, say, copper. Note even the 8% figure for 2011 of government revenues to sales assumes payment at a realistic exchange rate – something which is not at all certain. The real ratio may be much lower.

market-led competition is allowed to impinge on incumbent products and producers, then there is a promising path forward. However, such a move will prove difficult since so many of the elite have relied on some form of extraction, favored contracts or land access, or monopoly to become wealthy. On the other hand, a fast growing economy with more trade will also present opportunities for those with access to capital and some business experience. The challenge will be to persuade enough of the elite that they and the nation will be better off following an “upward” path. If the future did involve something like the proposed “new federalism” a whole host of implications follows, described in the previously referenced paper “Against the Odds”.²² The sheer magnitude and complexity of the various parties’ interests is daunting. In a small economy, billions of dollars a year and political and economic power is at stake. Only a broad coalition can create a switch to a system in which the natural resources are used for national development.

There will likely be a tendency for some of the essential coalition partners to consider forming a narrow coalition since forming a broad coalition is so difficult. There may be a narrow coalition based on a “military +1” idea. This would combine the military and one of the potential coalition partners. However, if the ethnic groups (for example) remained effectively excluded from real participation, the Union of Myanmar would not be a real nation since so many people would feel excluded and oppressed. The very *idea* of a coalition is hard to understand for those accustomed to one line of authority. It requires groups with different goals and values, even if opposed in the past, to cooperate for a common goal. It requires negotiation and compromise. It means that the circle of influence is enlarged and more interests are considered in making policy. The choice of the kind of coalition formed is the short-term choice that the major groups have to make.

The major groups potentially involved in a broad coalition include the NLD led by Daw Aung San Suu Kyi; the Parliament led by the speaker U Shwe Mann; the current government led by President Thein Sein; the military led by the Commander-in-Chief General Min Aung Hliang and the ethnic groups. The graphic on the following page represents the possible coalition partners.

²² Among the many steps needed to realize a unified and broadly developing nation would be a revised policy towards land rights, taxation of natural resources and the creation of a normal system of public finance, limited self-rule in states, a move to fair and open elections, a strengthened rule of law with diminishing military ability to legally intervene, and adoption of economic policies to boost growth and improve economic welfare for most people. A stronger rule of law would protect minorities and allocate citizenship to those born in Myanmar.



Each group has some tendencies towards supporting a broad coalition and some that are more status-quo oriented.

The NLD, not without reason, may have felt it could win any fair election and therefore did not need to form a coalition. However, it is politically sophisticated and thoughtful, and appears to appreciate the need for a broad coalition.²³ It needs more than popular support though – it needs a rule of law and the agreement of the military to allow real democratic government.

The military, with its blocking position in Parliament and the constitutional right to intervene at will, may also not see the point of gathering many allies. Yet, unless the military’s right to intervene is replaced by

²³ The recent comments by Aung San Suu Kyi about the need for a rule of law and key constitutional changes reflect this sophistication. See: <http://www.bloomberg.com/news/2013-09-22/there-is-no-guarantee-myanmar-won-t-backslide-suu-kyi-says-1-.html?cmpid=yhoo>

a rule of law, no government will govern securely – Pakistan is a cautionary example. If some degree of amnesty for past wealth accumulation and a future military role were negotiated, the long-run position of both the military and the nation would be stronger, even if future extraction were limited and the holding companies no longer functioned as monopoly money machines. However, little is known about the sentiments of the officer corps or any tensions between retired and current duty officers.

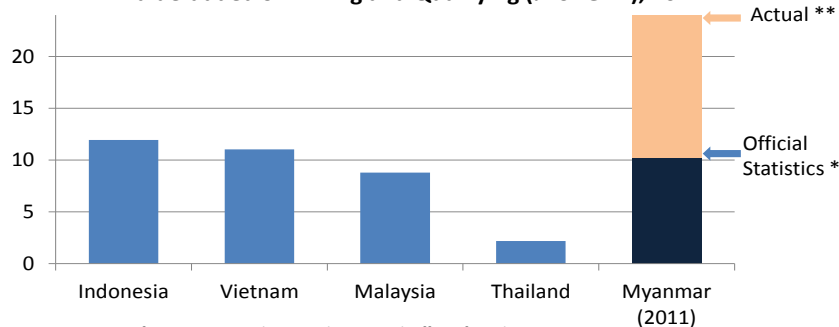
The current Parliament came to power in unfair elections and represents many entrenched and vested interests. Yet within these groups, there are some that would support a different path and others that cling to their present advantages. The speaker, U Shwe Mann, may have a vision of national unity and be a natural leader. He may be able to persuade some of his fellow Parliamentarians that a rule of law that protected minority interests would be in their own self-interest, thus setting the stage for their support for Federalism, resource sharing and a fair election in which the NLD could compete.

The current government has definite reform instincts and has been trying hard to shift policies in that direction. They are stymied by not fully controlling the Army, a lack of skilled implementation capacity, and a tendency to rely on command and control planning more than markets. President Thein Sein has surprised many observers with his astute moves. His suspension of the Myitsone Dam was very popular, as was his allowing of fair by-elections in which the NLD participated. The Peace Process could be a huge step towards ending decades of conflict – **if** the military is willing to cooperate.

The ethnic groups, so often treated as a residual and inferior claimant to their own lands and resources, may understandably be skeptical. Yet the ability of any of these groups to impose its will on the entire nation and society is limited. If they do not figure out a way to negotiate and compromise with each other, it is not likely that one or two of these groups will succeed in creating a better national future. These groups will have to figure out a way for their political parties to control their armed militias and to govern themselves in local matters without violence or excessive corruption. It will not be easy.

It goes without saying that without unity, the ability of powerful neighbors to create an almost colonial extraction of resources would be all but certain. Indeed, that is what the hydroelectric contracts entailed with 90% of power going to China, possibly severe environmental effects and little effective compensation for displaced ethnic groups. A weak government would be susceptible to external pressure, as it would lack resources and struggle to maintain order. That is another reason why a broad and unified coalition is needed. In any case, it is clear that natural resources are a large part of the Myanmar economy, as the next graph shows – and how they are managed will largely determine the future of political and economic reforms and even the integrity of the nation.

South East Asia: The Importance of Resource-based Industries Value-added of Mining and Quarrying (% of GDP), 2011



Source: ADB for Myanmar and National Statistical Offices for other countries.

- Official statistics puts the value of Myanmar’s mining sector at a very low level.
- The resource-rich economy of Myanmar:
 - GDP estimate (2011, IMF): US\$51.9 bn
 - Gas: US\$ 3.3 bn
 - Jade (estimated): US\$ 8.8 bn

*Official exports of minerals for 2011 include official gas and 80% of “other.” No other mineral exports were specified.

** Actual exports include official gas exports and authors’ estimates of jade at emporium values.

This estimate of natural resource exports leaves out non-jade gems, gold and timber. Gas exports will be increasing as the Chinese pipeline begins transporting 400 billion cubic feet of gas a year to Yunnan. Official data typically understate actual exports – even for rubber. In 2011/12, rubber production was estimated by the Ministry of Agriculture at 150 thousand tons but officially recorded exports were only 34 thousand tons. Rubber is a relatively low value to weight product. Goods with a much higher value/weight ratio are much easier to smuggle out to evade taxation. In other words, total resource exports are likely to be a significant fraction – more than 25% -- of Myanmar’s GDP. Each year, that amounts to billions of dollars a year that have not been taxed or directed to needed investments.

In previous papers, the authors had written about “choosing national unity and progress” but that was before the sheer size of the resource extraction was known.²⁴ This makes the “choice” not just one aimed at better economic and social policies, but one of national survival. If the failed policies of the past are sustained through continued extraction from natural resource exploitation, there will be more failure, more division, and more out-migration. These revenues must be directed to productive investments if peace and development are to have a chance – and these are needed for sufficient national strength to be effectively independent. The choice is stark and has much higher stakes than just faster or slower growth.

The list of economic policies needing attention is daunting, but a bit easier if there is a significant flow of revenue. Improving roads, power, ports, water and other infrastructure would improve “hard” infrastructure, but lowering road tolls, port costs and informal fees (“soft” infrastructure) is also critical. Amending the land law to favor smallholders is needed to create some equity and security, but so is a

²⁴ See, for example, “Negotiating Nation Building, A Path to Unity and Progress” by David Dapice. The May 2012 paper was prepared for Proximity Designs/Myanmar and can be found at: <http://www.ash.harvard.edu/extension/ash/docs/nationbuilding.pdf>

mechanism to sort out past land seizures, not all of which were fully legal or justified. Rapid upgrading of the financial sector is needed to get credit to profitable firms that might grow faster, while a more competitive exchange rate would strengthen the profitability of many companies and farms that are now struggling. Strengthening health and education systems is a longer-term project, but one that can and should be started soon. Developing effective urban infrastructure at a reasonable cost and keeping urban land prices reasonable will be another challenge, with many pushing for speculative land profits that would preclude desirable industrial and residential/commercial growth.

Anyone who has talked with the ethnic groups knows that it would be a huge effort to shift from groups of militias that live by extraction of resource profits, tolls, smuggling and “donations” to real governments that collect legal taxes and have a democratically approved budget. This will be a messy and long term project, as there has been little preparation for self-government. But if a legal basis for democracy and land ownership is created, along with a flow of resource based revenues to fairly elected governments, there will at least be a chance for better outcomes. As it is now, the prospect of continued migration of the young and most qualified is the most likely outcome if armed groups continue to retain most profits from raw material extraction while raising costs for local businesses through forced donations. It is fortunate that the present government is moving to avoid this outcome by emphasizing genuine negotiations with the various ethnic groups – though many of them fear that the military may have a different set of goals than the government. To the extent negotiations allow the ethnic states a reasonable chance to govern themselves, to that extent the peace process will succeed. The main issues will be the degree and types of federalism or decentralization negotiated; the details of sharing of resource revenues; and the ability of ethnic battalions to serve as they once did in the national army – the “Kachin Rifles” for example. Alternatively, an ethnically integrated army would also be a possible goal, though that may take longer. As for central Myanmar, the role of the military will have to slowly become more “normal” – much as the Indonesian military has accepted its role as a professional force and not a shadow government as it is in Egypt and Pakistan. If fully and fairly contested democratic elections produce a fair winner, the onus will be on the NLD to govern. Without a coalition, this may prove as difficult for them as the African National Congress found it to be in South Africa or the Muslim Brotherhood in Egypt. A coalition is needed not just to get to elections, but to govern.

In order to govern, more than a political coalition will be needed. There will have to be competent officials and analysts who provide a picture of reality and suggest options for the politicians that respond to political needs without excessively falling prey to populism or special interests. This is true at both a state/division and national level. Investing in that capacity is one prong of a strategy aimed at creating the political, technocratic and economic conditions for joint progress. Short term training of the “off the shelf” variety will not be sufficient. Instead, research on local conditions has to be distilled into case studies and lessons for officials so they understand the challenges they face and some possible solutions. Only this kind of training in applied economics, development and public policy can effectively strengthen those tasked with solving the problems governments will surely face. Longer term investment in education and institution building are needed for durable gains.

A path to a better future exists for Myanmar, but it is a long and winding path that will require much patience and effort. The cost of failing to work together could be very high. The choice is between poverty and growing and widely spread wealth; between oppression and democracy; between festering conflict and peaceful unity; and – finally – between an independent nation and a dependency that slowly loses its ability to shape its own future.

Appendix I: How Fast is Myanmar Really Growing?

In somewhat earlier times, it was not unusual for Myanmar to officially report real GDP growth rates well over 10% a year, even faster than China. There is general agreement that this was due to statistics that were more responsive to official directives than actual growth. Nobody is suggesting that similar conditions now apply, but there are still concerns with the quality and reliability of data. This note discusses the real GDP growth rate in 2012/13. The official growth reported was 6.5%, which the ADB and IMF largely agreed with. The World Bank in their Myanmar Economic Monitor (October 2013) use the IMF figure of 6.5%, even though an earlier IMF report from January estimated 6.3%. The question is if other data support such a brisk growth rate or suggest somewhat slower growth.

The Ministry of National Planning and Economic Development maintains a statistics website at: https://www.mnped.gov.mm/index.php?option=com_content&view=article&id=95&Itemid=112&lang=en and this site has official data on trade, production, prices and exchange rates. In particular, if we take the official data on exports and imports in dollars from 2011/12 to 2012/13, we find a **drop** of 1.7% in dollar exports and a rise of 0.4% (less than ½ of 1%) in the dollar value of imports. (These data were accessed from the web site in January, 2014.) If we look at electricity production, we find a rise of 12.9% in electricity production, which is consistent with 6-7% real GDP growth if total demand grew that much. Since diesel imports fell, it is possible that some portion of the growth in the grid simply replaced power previously generated by small diesel units. For trade, there was generally a stable if not rising price level in the later year compared to the earlier one, so it would appear that the trade levels are consistent with very low or even negative growth. They are certainly not consistent with rapid growth of 6-7% in GDP. The question is which set of data are more reliable – the foreign trade or the GDP. (The electricity data are unclear due to the lower diesel imports.)

Normally, foreign trade data are considered fairly reliable because most goods come in through ports or checkpoints on roads. While there might be mispricing of the goods traded, and there is always some smuggling, there would have to be a big change in the rate of mispricing or smuggling to create a real divergence between the change in trade compared to the change in real GDP. However, it is possible that such relationships do not hold in Myanmar as well as in other nations. For example, the Ministry of Agriculture reported 143,000 tons of rubber produced in 2011/12, but only 33.6 thousand tons were reported as being exported. Since domestic consumption of rubber is quite low, it is likely that a lot of rubber exports were not reported. Rubber does not have a high value/weight ratio so is not a prime candidate for smuggling. If it is not reported, it is likely that many other more valuable goods are also escaping official recording. It could be that the vagaries of reporting render trade unreliable.

The World Bank's publication states that exports of goods were \$9.64 billion in 2012/13, an increase of 2.3% over the 2011/12, while the official data for exports were only \$8.98 billion for 2012/13, with a drop of 1.7% from the previous year. World Bank imports are even higher at \$12.9 billion compared to the official \$9.1 billion, with a World Bank growth rate of 10.7% compared to the official growth rate of

only 0.4%. It is unclear what data the World Bank is using – perhaps the IMF – but if export and import growth rates are so much better, perhaps GDP should grow *more* than the official data?

This still leaves the official electricity data, where supply grew 12.7%. Electricity growth is normally higher than GDP growth. Liquid fuel consumption fell by about 350 million liters, enough to produce 1.2 billion kWh if all reduced imports were used for generating electricity. The increase reported in centrally produced electricity from 2011/12 to 2012/13 was 1.25 billion kWh. It is at best uncertain and perhaps unlikely that the electricity data support a GDP growth rate of 6.5%.²⁵

If we are to put the pieces together, we get the following comparison of 2011/12 to 2012/13:

Trade, Power, and GDP from 2011/12 to 2012/13

	<u>Official Data</u>	<u>World Bank Data</u>
Export Growth	-1.7%	+2.3%
Import Growth	+ 0.4%	+10.7%
Power – Production	+12.9%*	N/A
Real GDP Growth	+6.5%	6.5%

*A drop in diesel use offsets some or most of this increase in centrally produced power.

Either the official data should be revised or the IMF/World Bank should explain why they are so much higher than the official trade data but agree with the official GDP growth. It would be helpful if the more reliable sorts of data such as trade and energy were in broad agreement with the important but harder-to-estimate series such as the GDP. If GDP really is lower than 6.5%, it should be known so that policy makers can get an accurate map of where they are going.

²⁵ It may be that offshore gas production is counted in GDP but the offshore power generated is not yet in the official electricity data.