Country Report

Myanmar (Burma)

Myanmar (Burma) at a glance: 2005-06

OVERVIEW

Hardliners within the ruling military junta, the State Peace and Development Council (SPDC), have taken a firm grip on power. Although the junta will continue to espouse political reforms, the prospect of meaningful change taking place during the next few years is remote. The SPDC's reform rhetoric will lack credibility as long as Aung San Suu Kyi, the leader of the opposition National League for Democracy, remains under house-arrest. Real GDP growth will be held back by international sanctions, sluggish domestic demand, credit limitations and severe shortages of power. The junta will maintain a highly overvalued official exchange rate, and double-digit inflation and deteriorating confidence will exert downward pressure on the free-market exchange rate.

Key changes from last month

Political outlook

- Although the Association of South-East Asian Nations (ASEAN) continues to adhere to its long-standing principle of non-interference in member states' domestic affairs, a number of ASEAN members, particularly Malaysia and Indonesia, continue to call on the junta for meaningful political reform.

Economic policy outlook

- The government remains reliant on funds from the Central Bank of Myanmar to meet its spending requirement. The general government deficit will remain above 5% of GDP.

Economic forecast

- Exports of natural gas to Thailand jumped by 53% year on year in January-October, according to the Bank of Thailand (Thailand's central bank). Gas exports to Thailand will continue to expand in line with the recent discovery of additional reserves in the Yetagun gasfield.

January 2005

The Economist Intelligence Unit
15 Regent St, London SW1Y 4LR
United Kingdom

The Economist Intelligence Unit

The Economist Intelligence Unit is a specialist publisher serving companies establishing and managing operations across national borders. For over 50 years it has been a source of information on business developments, economic and political trends, government regulations and corporate practice worldwide.

The Economist Intelligence Unit delivers its information in four ways: through its digital portfolio, where the latest analysis is updated daily; through printed subscription products ranging from newsletters to annual reference works; through research reports; and by organising seminars and presentations. The firm is a member of The Economist Group.

London
The Economist Intelligence Unit
15 Regent St
London
SW1Y 4LR
United Kingdom
Tel: (44.20) 7830 1007
Fax: (44.20) 7830 1023
E-mail: london@eiu.com

New York
The Economist Intelligence Unit
The Economist Building
111 West 57th Street
New York
NY 10019, US
Tel: (1.212) 554 0600
Fax: (1.212) 586 0248
E-mail: newyork@eiu.com

Hong Kong
The Economist Intelligence Unit
60/F, Central Plaza
18 Harbour Road
Wanchai
Hong Kong
Tel: (852) 2585 3888
Fax: (852) 2802 7638
E-mail: hongkong@eiu.com

Website: **www.eiu.com**

Electronic delivery

This publication can be viewed by subscribing online at www.store.eiu.com

Reports are also available in various other electronic formats, such as CD-ROM, Lotus Notes, online databases and as direct feeds to corporate intranets. For further information, please contact your nearest Economist Intelligence Unit office

Copyright

ISSN 1361-1445

Symbols for tables

"n/a" means not available; "–" means not applicable

Printed and distributed by Patersons Dartford, Questor Trade Park, 151 Avery Way, Dartford, Kent DA1 1JS, UK.

Outlook for 2005-06

Political outlook

Domestic politics

The ruling military junta, the State Peace and Development Council (SPDC), continues to claim that it will proceed with political reforms. However, the recent purge of government officials who appeared to be in favour of some form of dialogue, albeit limited, with the main opposition party, the National League for Democracy (NLD), suggests that the likelihood of meaningful political reform taking place over the next few years remains low. In addition, despite the reported mass release of nearly 15,000 prisoners in the past few months, only around 40 of them were political prisoners. There are still around 1,300 political prisoners in the country, and the NLD's leader, Aung San Suu Kyi, remains under house arrest. According to the NLD, the junta recently extended her period of detention for another year.

The junta's hardliners, headed by the SPDC's chairman, Senior General Than Shwe, and its vice-chairman, Deputy Senior General Maung Aye, have successfully restored the balance of power firmly in their favour, most notably by sacking the prime minister and head of military intelligence, General Khin Nyunt. Other members of the government loyal to General Khin Nyunt have also been ousted and replaced by army personnel with close loyalties to the senior generals. Although the decision to remove General Khin Nyunt from power was officially made because of his "involvement in major bribery and corruption cases", the decision to dismantle the military intelligence suggests that General Khin Nyunt's growing power base, and that of the military intelligence, was troubling his seniors, who head the regular army.

The extent to which differences over how to handle Aung San Suu Kyi contributed to General Khin Nyunt's downfall is unclear. General Khin Nyunt was by no means a reformist, but he was perceived to have been more aware than the other top generals of the need to improve the junta's image. By appointing Lieutenant-General Soe Win as prime minister, the senior generals have left little room for doubt that they are determined to defy calls for Aung San Suu Kyi's freedom. Lieutenant-General Soe Win is thought to be deeply opposed to making any concessions to the NLD. However, the junta has stated that it will stick to its "road map" for democratic reform, which was unveiled by General Khin Nyunt in August 2003. This is probably because it has already placed a great deal of emphasis on this process, which it hopes will mollify pressure from foreign governments for political change.

The road map, however, lacks credibility, with opposition political and ethnic groups boycotting the National Convention (NC), the reconvening of which was the first step of the seven-point road map. Although the NC, which has the task of drafting the principles for a new constitution, will resume in February 2005, the most likely outcome is still that the junta will drag out the activities of the NC and proceed slowly with the road-map process. In the unlikely event that the junta edges towards holding a tightly controlled election within the next few years, it will do so only with the assurances of, first, having parliamentary seats reserved for the military, and second, possessing a powerful political wing, namely the Union Solidarity Development Association, that is capable of suppressing support for the NLD.

International relations

The Association of South-East Asian Nations (ASEAN) continues to adhere to its long-standing principle of non-interference in member states' domestic affairs. This was most recently demonstrated during the ASEAN summit in Laos in late November, when no mention was made of the lack of political reform in Myanmar in the final official communiqué. However, a number of ASEAN members, particularly Malaysia and Indonesia, continue to call on the junta for meaningful reform, including the release of Aung San Suu Kyi. This primarily reflects concerns about how the group's image will suffer when Myanmar takes over as chair of ASEAN for a year in 2006. The US government has already stated that it might boycott ASEAN meetings during this period if the junta fails to implement meaningful reform. The US has already passed a range of economic sanctions (including a ban on all investment and imports), and the EU has tightened its restrictions. In stark contrast to this isolationist approach, the governments of neighbouring China and India, fearful of rapid political change in Myanmar, remain keen to engage the junta in order to promote their own strategic objectives.

Economic policy outlook

Policy trends

The SPDC has neither the will nor the capability to deal effectively with the country's grave economic problems. The junta's pariah status internationally means that it cannot access vital external financial assistance; it therefore remains heavily reliant on a destabilising policy of monetising its budget deficit. The junta's medium-term economic policy focus seems to be one of reducing reliance on imported inputs and boosting agricultural output—a reasonable enough aim, given that the economy is largely agrarian. However, the junta has done little to promote investment in the agricultural sector or to improve the welfare of farmers. Indeed, it has often backtracked on its efforts to liberalise trade in key agricultural goods, and this trend is likely to continue in 2005-06. There is also a high risk that the government will continue to implement blunt ad hoc policy initiatives with negative side effects.

Fiscal policy

Although government revenue from taxes continues to expand, revenue growth in real terms is weak. Tax collection is structurally depressed because of the fact that much of the economy operates in the untaxed "grey" area. The government consequently remains reliant on funds from the Central Bank of Myanmar to meet its spending requirement—by end-July (latest available data) the Central Bank's claims on the government had expanded by 35% year on year. Although the government does not produce regular and timely data on expenditure, there is unlikely to have been a reduction in state spending in recent years, as the junta has been unwilling to restructure inefficient state enterprises and reduce defence spending. (There have, however, been cuts in spending on areas such as health and education.) Over the next few years the junta is unlikely to change this stance, and the general government budget deficit will remain above 5% of GDP. With the junta failing to secure budgetary support from foreign donors to meet its financing needs, its policy of monetising its budget deficit will remain in place.

Monetary policy

The junta is not expected to tighten monetary policy in 2005-06 by raising nominal interest rates, owing to the fact that such a move would increase its domestic debt-servicing burden. Even during periods of rapid inflation in recent years the junta refused to raise nominal interest rates, and real interest rates were therefore steeply negative. Although real interest rates rose in the first quarter of 2004 in line with easing inflation, this trend is not expected to continue, as inflation is expected to pick up again and nominal rates will remain unchanged. The development and stability of the banking sector continues to be undermined by the failure to adopt a coherent and flexible monetary policy. Although the banking sector is slowly recovering after suffering a near-collapse in early 2003, without much-needed technical and financial assistance from international financial institutions there remains a high risk that the Central Bank will fail to reverse the overall deterioration in the state of the banking system in 2005-06.

Economic forecast

International assumptions

International assumptions summary
(% unless otherwise indicated)

	2003	2004	2005	2006
Real GDP growth				
World	3.8	5.0	4.2	4.0
OECD	2.0	3.4	2.5	2.4
EU25	1.1	2.4	2.1	2.2
Exchange rates				
¥:US$	115.9	108.2	94.8	94.0
US$:€	1.132	1.242	1.385	1.400
SDR:US$	0.714	0.676	0.631	0.627
Financial indicators				
€ 3-month interbank rate	2.33	2.13	2.10	2.25
US$ 3-month Libor	1.21	1.59	3.36	4.75
Commodity prices				
Oil (Brent; US$/b)	28.8	39.0	36.8	29.0
Gold (US$/troy oz)	363.3	405.5	415.0	396.3
Food, feedstuffs & beverages (% change in US$ terms)	6.6	9.0	-6.0	-1.5
Industrial raw materials (% change in US$ terms)	13.0	20.5	-2.1	-4.7

Note. Regional GDP growth rates weighted using purchasing power parity exchange rates.

The pace of world GDP growth (at purchasing power parity) will slow in 2005 and 2006, to 4.2% and 4% respectively, from 5% in 2004. Continued strong growth in Myanmar's main export markets in Asia, particularly Thailand, China and India, will ensure that external trade remains fairly buoyant. At an annual GDP growth rate of around 5.5-6%, Asia and Australasia (excluding Japan) will enjoy the fastest expansion of any region in 2005-06. The Economist Intelligence Unit expects crude oil prices (dated Brent Blend) to fall to an average of US$36.8/barrel in 2005 and US$29/b in 2006, from US$39/b in 2004. Global prices for food, feedstuffs and beverages will drop by 6% in 2005, before falling slightly further in 2006. However, rice prices will remain strong, rising by 9.7% in 2005 and 4.2% in 2006.

Economic growth

There is little prospect of any marked improvement in the economy in 2005-06. The economy continues to suffer from a number of weaknesses, primarily related to shortages of power and essential imported inputs. According to official figures, in fiscal year 2003/04 (April-March) sales of electricity dropped by 37.7% year on year, and combined imports of capital and intermediate goods fell by 7% year on year in nominal terms. The accessibility and affordability of such imported goods is unlikely to improve over the next few years, owing to continued restrictions and the government's recent decision to increase import taxes. Across specific sectors, the outlook is mixed. Opportunities for manufacturers, particularly in the garment and textiles sector, have worsened owing to the US ban on imports from Myanmar and the increasing prevalence of international consumer boycotts. In the agricultural sector the junta's temporary ban on exports of rice and some other commodities in the first half of 2004 has probably prevented renewed investment, either because of financial constraints or owing to waning confidence. The only sector that is expected to record strong growth in 2005-06 is oil and gas. The recent signing of exploration and production deals with Chinese, Thai, Indian and South Korean firms indicates that this sector will continue to provide the main source of foreign direct investment over the next few years. Owing to the close links between the junta and the governments of China, Thailand and India, there is little risk of such investment being halted on political grounds.

Inflation

Consumer price inflation eased in early 2004 owing solely to the sharp drop in rice prices because of the government's decision to ban rice exports. In the first four months of the year (the latest data available) inflation slowed to 7.8% year on year, from an annual average of 36.6% in 2003 and 57.1% in 2002. However, annual inflation is unlikely to drop to single digits in 2004, with rice prices picking up again—the government eased its restrictions on rice exports in June. Gasoline prices have also risen sharply in recent months. In addition, the SPDC's decision to increase import taxes in mid-June is likely to have introduced additional inflationary pressure into the economy. In 2005-06 upward pressure on prices will persist in line with the junta's continued willingness to monetise its budget deficit.

Exchange rates

The government is not expected to realign its official exchange rate with the free-market rate in 2005-06. The grossly overvalued official rate, which is linked to the IMF's SDR, will remain broadly stable during this period at around Kt6:US$1. However, the free-market value of the kyat will continue to fluctuate around a long-term downward trend. After dropping to Kt980:US$1 in June (a few days after the government announced that it had raised import taxes), the kyat since stabilised at around Kt950:US$1. The junta has made a habit of implementing policies, such as the recent raising of import taxes, without warning or explanation, and the subsequent confusion among businesses and consumers is often reflected in a sharp depreciation in the free-market value of the kyat. This is unlikely to change in 2005-06, with the public's confidence in the junta's ad hoc management of the economy remaining low.

External sector

According to the latest available data, export revenue in kyat terms fell by more than 20% year on year in the first four months of 2004, following a decline of 24% in 2003. (However, reflecting Myanmar's inconsistent trade data, in the balance-of-payments accounts for 2003, data for which were recently published by the IMF, exports contracted by only 1.3% year on year.) This downturn has largely been in line with international consumer boycotts and the US ban on imports from Myanmar, which came into effect early in the second half of 2003. The US ban is expected to remain in place in 2005-06, ensuring that exports of manufactured products, particularly textiles and garments, will remain weak. However, mining, energy and agricultural exports to Myanmar's large neighbours, China, India and Thailand, which between them accounted for nearly 45% of total Burmese exports in 2003, will remain fairly robust. Indeed, exports to Thailand, mainly of natural gas, jumped by 53% year on year in January-October, according to the Bank of Thailand (the Thai central bank). Gas exports to Thailand will continue to expand in line with the recent discovery of additional reserves in the Yetagun gasfield. Although the import bill has been pushed up by the high cost of imported refined petroleum products, the shortage of foreign exchange and higher import taxes will dampen overall import demand in 2005-06. The continued weakness in imports will ensure that the merchandise trade account remains in surplus, but this will be offset by a fairly large deficit on the combined services and income accounts. The current account will therefore remain in deficit in 2005-06.

Forecast summary
(% unless otherwise indicated)

	2003[a]	2004[a]	2005[b]	2006[b]
Real GDP growth[c]	-2.0	-1.3	1.3	2.1
Gross fixed investment growth[c]	-0.5	0.5	2.5	4.0
Gross agricultural production growth[c]	-0.2	-3.0	1.8	1.2
Consumer price inflation (av)	36.6[d]	14.5	26.5	27.3
Consumer price inflation (year-end)	17.4[d]	25.0	25.0	30.0
Short-term interbank rate	15.0[d]	15.0	15.0	15.0
Government budget balance (% of GDP)[c]	-4.5	-5.2	-5.5	-5.5
Exports of goods fob (US$ bn)	2.5[d]	2.4	2.5	2.5
Imports of goods fob (US$ bn)	1.9[d]	2.1	2.2	2.1
Current-account balance (US$ bn)	0.0[d]	-0.2	-0.3	-0.2
Current-account balance (% of GDP)[e]	0.6	-1.9	-3.4	-1.7
External debt (year-end; US$ bn)	6.8	7.0	7.2	7.2
Exchange rate Kt:US$ (av)[f]	960.0	910.0	1,090.0	1,150.0
Exchange rate Kt:¥100 (av)[f]	828.3	841.0	1,150.4	1,223.4
Exchange rate Kt:€ (av)[f]	1,087.0	1,130.0	1,509.6	1,610.0
Exchange rate Kt:Bt (av)[f]	23.1	22.5	27.3	29.5

[a] Economist Intelligence Unit estimates. [b] Economist Intelligence Unit forecasts. [c] Fiscal year (beginning April 1st of year shown). [d] Actual. [e] Fiscal year (beginning April 1st of year shown); at free-market exchange rate (which understates the size of GDP). [f] At free-market exchange rates.

Editors: Danny Richards (editor); Graham Richardson (consulting editor) **Editorial closing date:** December 15th 2004
All queries: Tel: (44.20) 7830 1007 E-mail: london@eiu.com **Next report:** Full schedule on www.eiu.com/schedule

