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MYANMAR ECONOMIC MONITOR

JAN 2023

NAVIGATING UNCERTAINTY

MYANMAR ECONOMIC MONITOR: NAVIGATING UNCERTAINTY

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Preface and Acknowledgements

The Myanmar Economic Monitor (MEM) is published semiannually and is a product of the World Bank's Myanmar office. This edition was prepared by a team led by Kim Alan Edwards (Program Leader and Senior Economist) and included Thi Da Myint (Country Economist), Kemoh Mansaray (Senior Economist), Faya Hayati (Senior Economist), and Aka Kyaw Min Maw (Consultant). Fang Guo (Economist) and Paul Samuel Minoletti (Consultant) led the preparation of Part III. The MEM was developed under the guidance of Sebastian Eckardt (Practice Manager, Macroeconomics, Trade, and Investment) and Mariam J. Sherman (Country Director).

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Table of Contents

Preface and Acknowledgements.....	ii
Abbreviations	vii
Executive Summary.....	1
I. Recent Economic Developments	6
A. Navigating uncertainty and volatility.....	6
B. Economic performance has been mixed.....	9
C. Prices have risen sharply	19
D. Trade has been relatively resilient.....	22
E. The exchange rate has been volatile.....	26
F. Financial institutions are facing a range of operational issues	30
G. The fiscal position has strengthened.....	31
H. Livelihoods remain under severe pressure	37
II. Outlook and Risks	39
III. Recent exchange rate developments: A historical perspective	43
A. Recent changes in exchange rate policy.....	43
B. The potential for exchange rate unification.....	47

LIST OF FIGURES

Figure ES 1: Exchange rate	4
Figure ES 2: CPI inflation	4
Figure ES 3: Conflict intensity	5
Figure ES 4: Merchandise exports (2019 average = 100)	5
Figure ES 5: Firms' average operating capacity	5
Figure ES 6: Manufacturing Purchasing Managers' Index	5
Figure ES 7: Real GDP growth and contributions to real growth by sector (year ended Sep)	5
Figure ES 8: Real GDP per capita (year ended Sep)	5
Figure 1: Conflict intensity in Myanmar	7
Figure 2: Firms' average operating capacity	10
Figure 3: Challenges to firms' operations	10
Figure 4: Retail mobility	11
Figure 5: Transport mobility	11
Figure 6: Retail and wholesale firms' performance	11
Figure 7: Alexa internet traffic ranking for shop.com.mm (higher rank denotes less traffic)	12
Figure 8: Number of vehicle sales	12
Figure 9: Domestic Outbound Flights from Yangon International Airport	13
Figure 10: International tourist arrival index	13
Figure 11: Freight transport (ton miles)	13
Figure 12: Manufacturing Purchasing Manager's Index	14
Figure 13: Manufacturing Purchasing Managers' Index – regional comparison	14
Figure 14: Manufacturing firms' performance	15
Figure 15: Number of vehicles produced	15
Figure 16: Total number of construction permits issued	16
Figure 17: Number of construction permits issued vs cement imports (tons)	16
Figure 18: Price of construction materials	16
Figure 19: Natural Gas export and Production volume (million cubic feet) between October to January	17
Figure 20: Natural gas export to Thailand (MFSCFD)	17
Figure 21: Agricultural firms' performance	19
Figure 22: CPI inflation	20
Figure 23: Inflation (MoM)	20
Figure 24: Fuel price and key drivers, January 2021=100	20
Figure 25: Contributions to non-food inflation	20
Figure 26: Basic food prices (Index July 2020 =100)	21
Figure 27: Purchasing Managers' Index (PMI) input and output prices	21
Figure 28: Trade flows	22
Figure 29: Exports and imports of laden containers	22
Figure 30: Myanmar's goods exports in comparison with regional peers (2019 average = 100)	23
Figure 31: Myanmar's exports to China	24
Figure 32: Myanmar's exports to Thailand	24
Figure 33: Major exports by product groups	25
Figure 34: Manufacturing exports by products	25

Figure 35: Total garment imports by the EU, Japan, and Korea	25
Figure 36: Myanmar's natural gas exports to Thailand and China	25
Figure 37: Imports by product groups.....	26
Figure 38: Refined mineral oil imports by product.....	26
Figure 39: Balance of payments (USD, millions)	27
Figure 40: FDI commitments	27
Figure 41: US dollar transactions.....	28
Figure 42: Asian currencies per US dollar (index, January 2019 = 100)	30
Figure 43: Myanmar kyat/USD (Reference rate, counter rate, parallel market rate)	30
Figure 44. Revenue 2019–2023 (% of GDP).....	31
Figure 45. MOPF tax collection (% of GDP)	32
Figure 46. Spending estimates 2019–2023 (% of GDP)	33
Figure 47. Expenditure by sector/ministry % of total.....	34
Figure 48. Supplementary budget April 2022 – March 2023 (% of new planned expenditure)	34
Figure 49. Fiscal aggregates (% of GDP).....	35
Figure 50. Public sector debt 2017–2023 (% of GDP).....	36
Figure 51. Quarterly government securities auction (MMK, billions).....	37
Figure 52. Government securities auction Total FY sales and % of FY deficit	37
Figure 53: Real GDP growth and contributions to real growth by sector (percent, percentage points)	39
Figure 54: Real GDP per capita.....	39
Figure 55: Forecast real GDP level in 2023 (2019=100)	40
Figure 56: Inflation forecast.....	40
Figure 57: Global oil price and exchange rate assumptions.....	40
Figure 58: Myanmar kyat/USD	43
Figure 59: USD sales in FX auctions	43
Figure 60: Narrow Money Supply (M0), 2012-2021 (MMK, millions).....	44
Figure B 1: Market-Determined Nominal USD-MMK Exchange Rate, 1950s-2010s	45
Figure 61: Unification of official and parallel exchange rates in 2012.....	48

LIST OF TABLES

Table ES 1: Economic data and projections for the year ended September 2023	3
Table 1: Economic data and projections for the year ended September 2023.....	41

LIST OF BOXES

Box 1: Declining power supply.....	7
Box 2: Exchange rate developments through Myanmar's history.....	44
Box 3: Historical precedents for Myanmar's current exchange rate policy	47

Abbreviations

ACLED	Armed Conflict Location and Event Data Project
AD	Authorized Dealer
AML/CFT	Anti-Money Laundering/ Combating Financing Terrorism
ASEAN	Association of Southeast Nations
bb1	Barrel of Crude Oil
CBM	Central Bank of Myanmar
CDD	Customer Due Diligence
CERP	COVID-19 Economic Recovery Plan
CMP	Cut-Make-Pack
CPI	Consumer Price Index
ETI	Ethical Trade Initiate
FATF	Financial Action Task Force
FAO	Food and Agriculture Organization
FECs	Foreign exchange certificates
FESC	Foreign Exchange Supervisory Committee
FDI	Foreign Direct Investment
FX	Foreign Exchange
FY	Fiscal Year
GDP	Gross Domestic Product
GWh	Gigawatt hours
H1	First Half
H2	Second Half
HS	Harmonized System
IFPRI	International Food Policy Research Institute
JV	Joint Venture
KYC	Know Your Customer
LNG	Liquefied Natural Gas
MEM	Myanmar Economic Monitor
MFI	Micro Finance Institution
MHWS	Myanmar Household Welfare Survey
MLPTA	Myanmar Rice and Paddy Traders' Association
MESC	Mandalay Electric Supply Corporation
MW	Megawatt
MMK	Myanmar Kyat
MOC	Ministry of Commerce
MOGE	Myanmar Oil and Gas Enterprise
MOPF	Ministry of Planning and Finance

NBFI	Non-Bank Financial Institutions
NPO	Non-Profit Organizations
OCHA	The UN Office of the Coordination of Humanitarian Affairs
PER	Public Expenditure Review
PMI	Purchasing Managers' Index
Q1	First Quarter
Q2	Second Quarter
REER	Real Effective Exchange Rate
SEE	State Economic Enterprise
SGT	Special Goods Tax
SEZ	Special Economic Zone
SVAR	Structural Autoregressive
TA	Temporary Actual
UN	United Nations
USD	US dollar
YBS	Yangon Bus Services
YESC	Yangon Electric Supply Corporation
yoy	year-on-year

Executive Summary

Myanmar has experienced significant macroeconomic volatility over the past six months. Between June and December 2022, the kyat lost about a quarter of its value against the US dollar, to be down by more than 50 percent from its level two years earlier (Figure ES 1). In conjunction with still-elevated global commodity prices and logistics constraints, this depreciation has resulted in significant price pressures which continue to filter through the economy. The latest available CPI data shows inflation rose to nearly 20 percent over the year to July, weighing on real incomes, consumption and investment (Figure ES 2). Exchange rate volatility was reported as the main constraint faced by businesses across all sectors in the September round of the World Bank firm survey, reflecting a particularly sharp depreciation episode in July and August. While the kyat has stabilized in recent months, foreign currency shortages persist, which together with onerous trade restrictions have affected businesses' ability to supply of a range of imported products. At the same time, foreign currency surrender requirements continue to impose a substantial tax on many exporters, reducing their competitiveness on international markets.

Economic activity has continued to be disrupted by persistent conflict, which has had devastating impacts on lives and livelihoods, and by electricity shortages. Data from the armed conflict location and event data project (ACLED) suggests that the overall conflict level remains much higher than in 2019 and 2020, though the number of incidents has declined in the last six months (Figure ES 3). Estimates indicate that around 30 thousand people have died from conflict in Myanmar since the end of 2020, while the number of internally displaced people has risen by about a quarter over the last six months to 1.5 million.¹ Many of these displaced people have been forced to live in extremely difficult conditions, without access to basic services and productive employment opportunities. Security issues have also affected trade, with outbreaks of violence and an increasing presence of roadblocks and checkpoints inhibiting the movement of goods within the country and across land borders. Meanwhile, widespread power outages have resumed in recent months, and power generation is expected to drop further in the dry season from January to April, especially in those areas where conflict is most severe. No additional generation capacity is expected to come online in the near term.

Policy uncertainty has risen. A number of the 'reform reversals' highlighted in the July 2022 edition of the MEM have subsequently been wound back, including the abovementioned foreign currency surrender requirements which were partially eased in August. At the same time, changes in rules and regulations – many of which are not publicly announced – have become more frequent. *Inter alia*, these changes have increased uncertainty around access to foreign exchange and imports, reduced confidence in payment systems, and delayed customs clearance processes. Some businesses are finding ways to navigate this opaque policy environment: either because they are benefitting from regulatory exemptions and more favorable access to foreign currency, or because they are finding ways to circumvent regulatory constraints, including by switching to informal payments and trade channels. But the inefficiencies caused by the resulting distortions worsen the business environment and impede economic growth. Other businesses continue to struggle to access foreign exchange, make outbound payments, obtain import licenses, and turn a profit amid weak domestic demand and elevated input prices.

¹ UN Office for the Coordination of Humanitarian Affairs (OCHA), Myanmar Humanitarian Update No. 25, 30 December 2022.

Against this challenging backdrop, recent economic indicators have been mixed. Mobility at retail outlets has improved to levels last seen in the pre-pandemic period, but retail sales remain weak. Despite higher costs, activity in the transport sector has picked up, though international tourism arrivals remain negligible. Construction activities continued to expand due to the resumption of public infrastructure projects and construction of residential buildings. Natural gas exports have remained steady. Firms reliant on merchandise export demand have tended to do better than those that sell the bulk of their output to the domestic market, where demand is constrained by lower nominal incomes and sharply higher prices. Nevertheless, merchandise exports – while still higher than in 2021 – have declined since September 2022, and over the past two years have provided much less impetus to economic growth in Myanmar than has been the case in other countries in the region (Figure ES 4).

Business surveys indicate that operating conditions have improved in the agriculture sector but weakened in manufacturing. While some firms remain constrained by low demand, higher prices, and electricity outages, in the December round of the World Bank firm survey a higher proportion of firms reported not experiencing any challenges to their operations. Agricultural firms reported operating at a higher proportion of their capacity and the share of agricultural firms reporting conflict to be a major constraint fell (Figure ES 5). On the other hand, the manufacturing Purchasing Managers' Index (PMI) indicates that output and new orders have contracted since July, and manufacturing firms have reported operating at a lower proportion of their capacity in November than earlier in the year (Figure ES 6).

The fiscal deficit narrowed in the six months to March 2022, while public debt is estimated to have risen above 60 percent of GDP. Improved revenues and lower spending saw the fiscal deficit decline to 4.7 percent of GDP from 9.2 percent in FY2021. Spending on critical public services has declined faster than other spending. Combined, public health and education spending accounted for just 8.5 percent of total spending during the period between October 2021 and March 2022, a significant reduction from previous years. At the same time, public debt is estimated to have increased by more than 20 percentage points of GDP since FY2019, with fiscal deficits, the large economic contraction in FY2021, and exchange rate valuation effects all contributing to the rise. The use of central bank financing has increased, accompanied by a shift away from T-bills and T-bonds issuance. According to the authorities' projections for the twelve months to March 2023, around two-thirds of public financing needs are expected to be met by the CBM, with the rest covered by the issuance of T-bills and T-bonds (16 percent) and external debt (19 percent). This marks a significant unwinding of previous efforts to reduce the share of government gross financing needs covered by the central bank, and will likely add to inflationary and exchange rate pressures.

The difficult economic situation has severely affected household welfare and increased vulnerability. Household incomes also continue to be stretched by the cumulative impact of recent shocks. In a survey conducted by the International Food Policy Research Institute (IFPRI) in July and August 2022, 46 percent of households reported experiencing income losses compared to the previous year (which itself saw a sharp contraction in incomes), and about half of all households reported reducing food and non-food consumption. With incomes weak and inflation high, food and nutrition security have deteriorated in 2022. The proportion of households with a low food consumption score (a measure of dietary diversity and food frequency) increased from 9.4 percent at the beginning of the year to 17.2 percent in July-August 2022, with 4 percent of households facing moderate to severe hunger.

Looking ahead, GDP is projected to grow by a modest 3 percent in the year ending September 2023 with output expected to remain well below its 2019 level (Table ES 1 and Figure ES 7). The economic recovery from the shocks of COVID-19 and the military coup is expected to remain subdued in the near term, constrained by significant macroeconomic and regulatory uncertainty, persistent conflict, and ongoing electricity outages. The forecast implies that GDP per capita this year would still be around 13 percent lower than in 2019, indicative of the persistent impacts of recent shocks to both the supply and the demand side of the economy (Figure ES 8). The failure to return to pre-pandemic levels of activity sharply contrasts with the situation in the rest of the East Asia and Pacific region, where GDP in all large countries has already recovered to above 2019 levels.

Table ES 1: Economic data and projections for the year ended September 2023

	FY17/18	FY18/19	FY19/20	FY20/21e	FY21/22e	FY22/23f
Real GDP growth, at constant factor prices	6.4%	6.8%	3.2%	-18%	3%	3%
Agriculture	0.1%	1.6%	1.7%	-12.5%	-3.0%	3.0%
Industry	8.3%	8.4%	3.8%	-20.6%	8.6%	3.7%
Services	8.7%	8.4%	3.4%	-18.4%	1.6%	2.3%
Inflation (CPI), year average	5.9%	8.5%	5.8%	3.6%	16.5%	7%
Current Account Balance (% of GDP)	-4.7%	-0.2%	-2.0%	-1.4%	-3.3%	-4.7%
Fiscal Balance (% of GDP)	-2.9%	-3.1%	-7.0%	-9.2%	-4.7%	-6.7%
Public Sector Debt (% of GDP)	38.4%	37.0%	42.2%	60.0%	61.5%	62.3%

Note: To facilitate comparisons over time, the FY22/23 forecast relates to the period October 2022 to September 2023, which differs from the budget fiscal year (April to March). e = estimate; f = forecast.

Amid easing global commodity prices, annual average inflation is expected to moderate to 7 percent in the year ended September 2023, from 16.5 percent in FY22. This reflects the expectation of an ongoing gradual moderation in global energy prices and the assumption that the exchange rate remains relatively stable at current levels. Current account and fiscal deficits are expected to widen, reflecting weaker global demand for exports and declining energy-related revenues.

The outlook is subject to significant risks. Domestic conflict and political instability could worsen in the lead up to planned elections, causing disruption to economic activity and weighing on business and consumer confidence. The global environment could also become more challenging than assumed in the baseline, including through lower growth, worsening geopolitical tensions and higher commodity prices. In addition, Myanmar also remains vulnerable to other sources of risk, including a resurgence of COVID-19 or a natural disaster, which would severely test the authorities' capacity to respond. On the upside, a stronger than expected recovery in China after the recent roll-back of COVID-19-related restrictions could provide some boost to bilateral trade and investment flows.

Myanmar's longer-term potential to achieve inclusive growth has been severely diminished over the past two years. The business environment is unlikely to improve materially while electricity shortages, logistics disruptions, trade and foreign exchange restrictions and regulatory uncertainty persist. Recent changes in the policy and political environment are likely to see growth suffer over the longer term as resources are allocated away from more productive and competitive uses. Funding to critical health and education services has been curtailed and a lack of trust in the public provision of these services is in any case reducing their use. Lost

months of education, together with rapid increases in unemployment and displacement, will reduce already low levels of human capital and harm productive capacity over the longer term. Migration is reportedly increasing through both formal and informal channels: while this is likely to benefit migrants and those receiving remittances, it is also leading to increasing reports of labor and skills shortages within the country.

As the special topic section of this report shows, exchange rate policy provides an example of how policy responses have exacerbated rather than dampened economic shocks. Over the past two years, there has been a shift away from the previously managed float regime and toward reliance on administrative controls aimed at retaining foreign exchange within the economy. This has led to the emergence of multiple exchange rates which have distorted price signals and the allocation of resources, while providing avenues for inefficient rent-seeking behavior. Foreign currency shortages and trade restrictions have limited the availability of many products, pushing up their price. The overvalued exchange rate and surrender requirements have eroded the competitiveness of exporters, acting as a tax on exports and squeezing margins even further given the rise in kyat-denominated costs facing most businesses. Throughout Myanmar’s history, similar policies have been associated with high inflation (including because of the monetary financing of large fiscal deficits), weak exports and low rates of economic growth. At the same time, international experience as well as Myanmar’s own liberalization and unification of the kyat exchange rate in 2012 indicate that a move toward a more market-oriented exchange rate system could help stabilize the economy and boost growth in productivity and trade.

Figure ES 1: Exchange rate

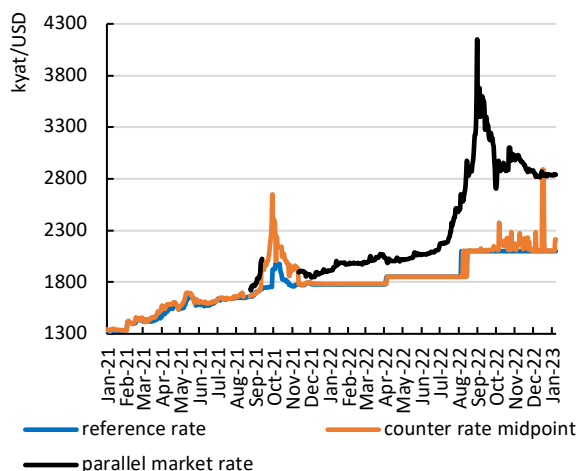


Figure ES 2: CPI inflation

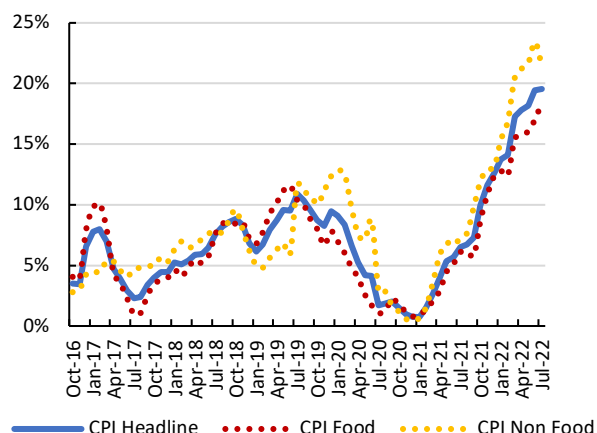


Figure ES 3: Conflict intensity

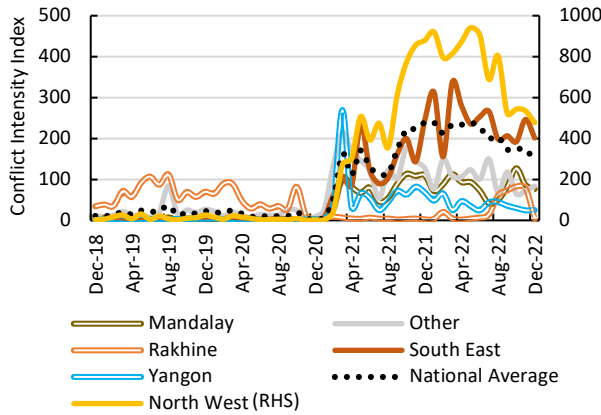


Figure ES 4: Merchandise exports (2019 average = 100)

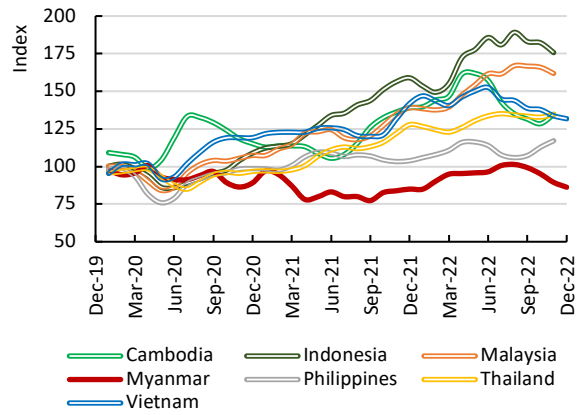


Figure ES 5: Firms' average operating capacity

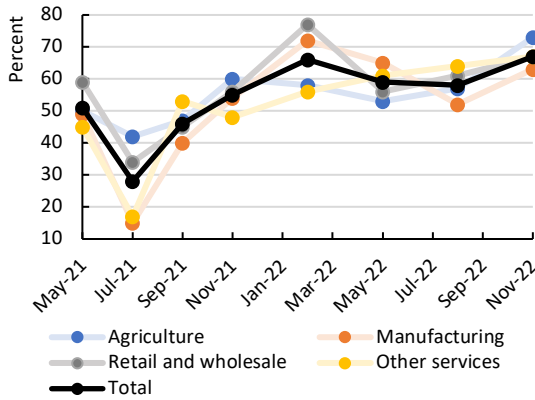


Figure ES 6: Manufacturing Purchasing Managers' Index (< 50 indicates contraction, > 50 indicates expansion)

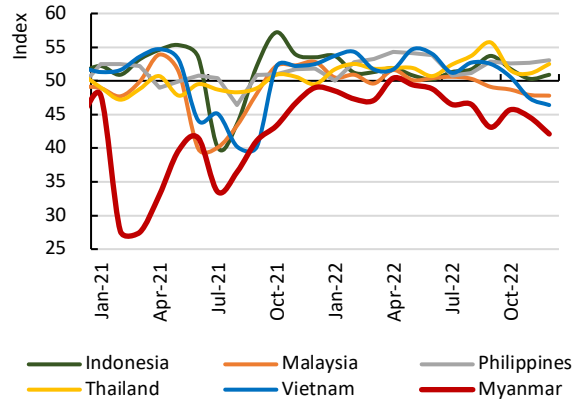


Figure ES 7: Real GDP growth and contributions to real growth by sector (year ended Sep)

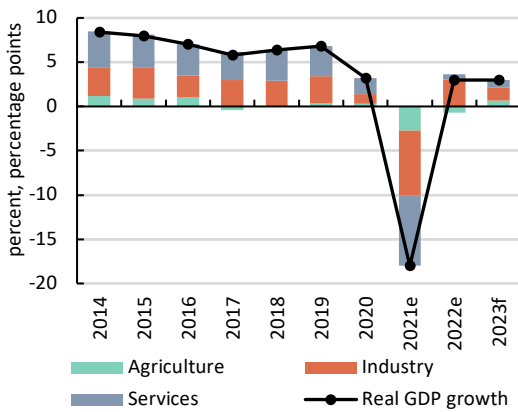
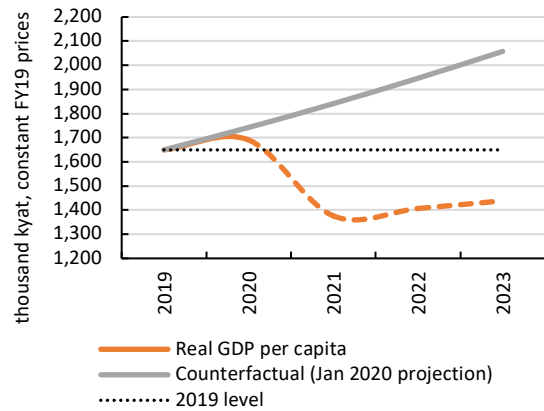


Figure ES 8: Real GDP per capita (year ended Sep)



I. Recent Economic Developments

A. Navigating uncertainty and volatility

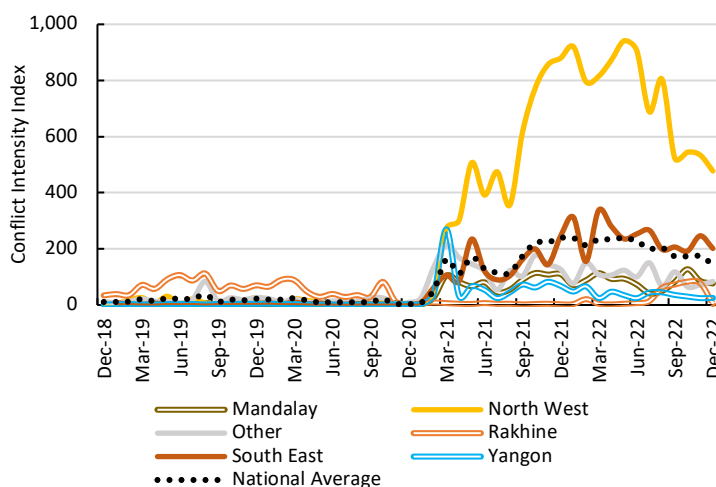
Myanmar's economy has experienced significant uncertainty and volatility over the past six months. Business operations have been disrupted by ongoing conflict, electricity shortages, and changing rules and regulations. Although some businesses and industries have shown signs of resilience (see section B), indicators of domestic demand remain weak. Household incomes continue to be stretched by the cumulative impact of recent shocks. In a household survey conducted by IFPRI in July and August 2022, 46 percent of households reported experiencing income losses compared to the previous year, and about half of all households reported reducing food and non-food consumption in response.

A substantial kyat depreciation combined with high global prices and ongoing logistics constraints has caused import costs to rise sharply, fueling domestic inflation and further reducing the real incomes of households. In the September round of the World Bank firm survey, kyat volatility was reported as the main constraint faced by businesses across all sectors: from the beginning of July to the end of August, the kyat depreciated by almost 50 percent against the US dollar, with commensurate increases in the kyat prices of many imported goods and widespread reports of foreign currency shortages. Even prior to that episode of exchange rate volatility, prices had risen steeply, by almost 20 percent over the year to June (see Section C).

Conflict remained severe in the second half of 2022, with the level of intensity varying across the country (Figure 1). Data from the armed conflict location and event data project (ACLED) suggests that the overall conflict level remains much higher than in 2019 and 2020, though the number of incidents has declined in the last six months. However, conflict in the North West (Sagaing, Magway, Chin and Kachin), and the South East (Kayah, Kayin, Mon and Tanintharyi) remained above the national average in 2022. In 2021 and 2022, almost 30 thousand people are estimated to have died from conflict in Myanmar. The number of internally displaced people has been estimated by UN OCHA to have risen by about a quarter over the last six months to 1.5 million. Many of these displaced people have been forced to live in extremely difficult conditions, without access to basic services, and have struggled to deal with the inflated costs of basic food items and fuel.

In addition to its devastating impacts on lives and livelihoods, conflict has continued to disrupt both external trade and trade within the country. Conflict in the southeast has disrupted land border trade with Thailand, frequently resulting in intermittent closures of transport routes and border posts. In late 2022, fighting on the Asian Highway linking Myanmar and Thailand reportedly led to cargo trucks and passenger vehicles resorting to using 'forest paths' to maintain transport links, with predictable impacts on freight costs. Security challenges and the establishment of roadblocks and checkpoints (which often require payment of a toll or levy) are delaying the movement of goods within the country and causing some truck operators to scale back their operations because of safety considerations. These constraints in conjunction with significantly higher fuel prices have resulted in a marked increase in freight costs. Interviews with selected transportation and logistics companies indicate that domestic trucking freight prices have increased on average by 30-50 percent for various routes since the beginning of 2022. Recent IFPRI surveys indicate that increased transport costs are the most significant issue faced by agricultural traders.

Figure 1: Conflict intensity in Myanmar



Sources: Armed Conflict Location and Event Data Project (ACLED)

Note: The North West includes Sagaing, Magway, Chin, and Kachin. The South East includes Kayin, Kayah, Mon, and Tanintharyi. Other includes Ayeyarwady, Bago, Nay Pyi Taw, and Shan. Conflict intensity is calculated as a geometric mean of events and fatalities. Events include battles, explosions, and remote violence, protests, riots, and violence against civilians. Fatalities represent the total fatalities resulting from each event.

After some improvement in mid-2022 with the onset of the rainy season, widespread power outages have resumed since October. Daily peak generation has fallen by about a third between late 2020 and late 2022, due to declining power supply and deterioration of key infrastructure (Box 1). Electricity loss, measured by the gap between generation and consumption, has increased sharply since May 2021 and is currently estimated at 20 percent monthly average generation, far above the global average of 8 percent. Reliance on hydropower plants during the rainy season has resulted in faster than normal depletion of water levels, affecting the capacity of hydropower plants to generate electricity from October onwards. In Yangon, the power utility announced in December that electricity would only be provided on a rotating basis to households and businesses in different zones (for 3-to-5-hour access periods); in practice, electricity supply is erratic and does not always adhere to the announced schedule. Many townships in other parts of the country are experiencing still more severe power shortages which have worsened in recent months.

Box 1: Declining power supply

Power generation has fallen short of demand over the past two years, with daily peak generation declining from 3,878 MW in November 2020 to 2,635 MW in December 2022. A number of factors are responsible for this decline, including:

- A reduction in power supply, due to the suspension of operations of gas-fired power plants, including liquefied natural gas (LNG)-to-power plants; delays in the completion of new power generation projects; and lack of new investment in the sector since early 2021;

- Poor maintenance of existing infrastructure resulting from labor strikes and lower electricity bill payments which have tightened budget constraints;
- Reduced capacity of poorly maintained pipelines carrying natural gas from Yadana and Zawtika offshore fields to power plants in Yangon;
- Worsening power infrastructure security, resulting from attacks on strategic power infrastructure and electricity offices.

Power generation is expected to drop further in the dry season from January to April due to seasonally lower rainfall levels, conflict-related disruptions, and limited capacity to renovate and repair exist infrastructure, especially in those areas where conflict is most severe. No additional capacity is expected to come online in the near term, and the authorities have announced that electricity will be rationed at certain times of the day, including in the Yangon metropolitan areas. Unpredictable blackouts are already commonplace across Myanmar and households and firms are preparing to deal with the summer electricity shortage by acquiring solar systems and diesel generators.

While there have been efforts to increase electricity supply over the medium term, deteriorating operating conditions pose challenges to meeting demand. A 135 MW gas turbine power plant project at Kyaukphyu, Rakhine State was commissioned in October 2022. Approval for investment of \$2.5 billion was provided for a 1,390 MW LNG-to-power plant project at Mee Laung Gyaing, in Ayeyarwaddy, in May 2021. Two other LNG-to-power plants in Tanintharyi and Rakhine were also planned to bridge the supply-demand gap. However, these projects have been delayed or cancelled due to operating constraints including rising global LNG prices, limited access to finance, inadequate transmission infrastructure and foreign exchange restrictions. The authorities are also assessing the potential to use nuclear energy for electricity generation, though any move in this direction is likely to face several hurdles and does not provide a feasible near- or medium-term solution to Myanmar's electricity supply shortfall.

Frequent regulatory changes have created substantial uncertainty in the business environment and made compliance increasingly difficult. Several of the restrictions introduced earlier in the year have been partially relaxed: the foreign currency surrender rules have been eased and the imposition of some trade license requirements has been unwound. But other restrictions have been tightened, for instance importers have been restricted to using foreign currency earnings from exports or remittances to fund their purchases of imports. Non-trade related outward payments of US dollars remain heavily restricted and businesses continue to be instructed to reschedule foreign loan repayments. Rules around the use of different currencies for trade settlement have changed several times in recent months. The customs clearance process has reportedly become more difficult and lengthier due to ad-hoc changes in rules and regulations and rigidity in the application of customs checks. In general, these changes have often not been transparent, and the scope of their application has been subject to discretion. Moreover, full implementation of the introduced regulations in many cases would require significantly more administrative capacity than what is currently available, creating further uncertainty around how they are applied.

While some firms are coping with these challenges, others are struggling. Firms reliant on export demand – which has been comparatively robust over the last twelve months – have tended to do better than those that sell the bulk of their output to the domestic market, where demand remains weak and constrained by lower nominal incomes and sharply higher prices. Businesses able to afford generators and sharply higher diesel costs have been able to manage during periods where electricity is scarce. Some firms are benefitting from access to

favorable exchange rates and exemptions from regulatory requirements. Others have been able to circumvent the foreign exchange and trade restrictions, including by switching to informal and/or unregulated channels for international payments and goods trade. But the need to make such adjustments reflects the existence of distortions and inefficiencies which will continue to impede economic growth for as long as they remain in place. At the same time, there are many businesses that are continuing to struggle to access foreign exchange, make outbound payments, obtain import licenses, and turn a profit amid weak domestic demand, elevated input prices, and foreign currency surrender requirements. Reflecting these challenges – as well as a variety of other concerns related to safety and security, reputational risks, and the possibility of further international sanctions – international firms have continued to announce their exit from Myanmar in recent months. These include skin care company Beiersdorf, telecommunications company Ooredoo, petroleum company Puma Energy, and ANZ bank, among others.

B. Economic performance has been mixed

The most recent rounds of firm surveys run by the World Bank and others paint a mixed picture across sectors and time periods. In December 2022, it appeared that firms (on average) had recovered from the introduction of foreign exchange restrictions and kyat volatility observed over the period April and September 2022, which was previously reported as the most significant operational challenge. Firms on average reported operating at 67 percent of their capacity in December 2022, in line with March levels, and an improvement from the weaker results reported in the June and September rounds (Figure 2). Moreover, the share of firms reporting that they did not experience any challenges to their operations increased to almost 38 percent (Figure 3). But these aggregate results mask substantial variation across sectors, with manufacturers and retail and wholesale firms still operating below March levels while the performance of agricultural and other service-oriented firms has improved since earlier in the year. Notably the share of agricultural firms reporting conflict as their most prominent challenge has fallen substantially over the past six months, potentially related to the moderate easing of conflict activity over that period (Figure 3).

Figure 2: Firms' average operating capacity

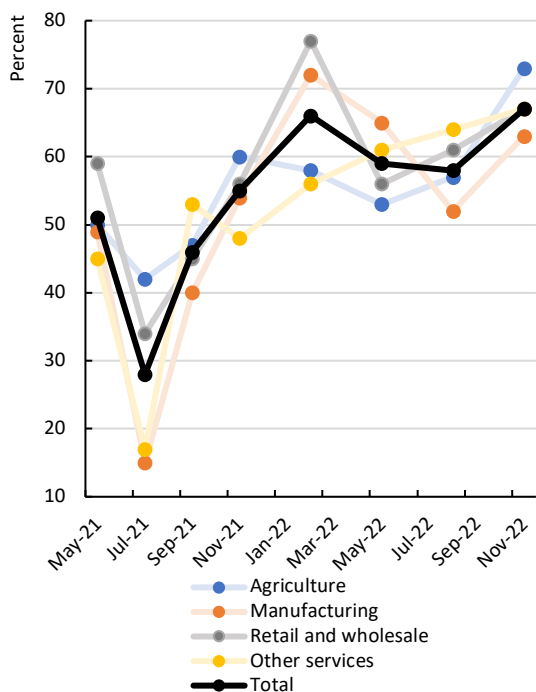
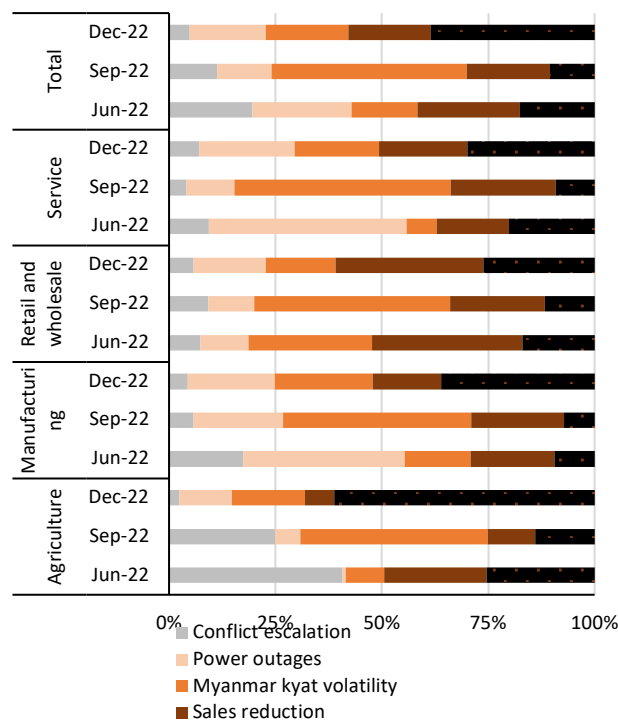


Figure 3: Challenges to firms' operations



Source: World Bank firm monitoring surveys

Note: Firms were asked to report about the last completed month.

Mobility has returned to close to pre-COVID-19 levels, though the recovery of movement through retail venues has been slower than in the rest of the region. Mobility at retail and recreation venues approached the pre-COVID-19 benchmark in October 2022 (at which point the series was discontinued), around 10 months later than the average for the rest of the region (Figure 4). While mobility at transport hubs has also improved since mid-2021, it plateaued at around 10 to 15 percent below pre-COVID-19 levels over the six months to October 2022 (Figure 5). Other data indicates that overall passenger miles (via air, land, and inland water transport) have recovered since FY2021 but remain well below 2020 levels.

Figure 4: Retail mobility

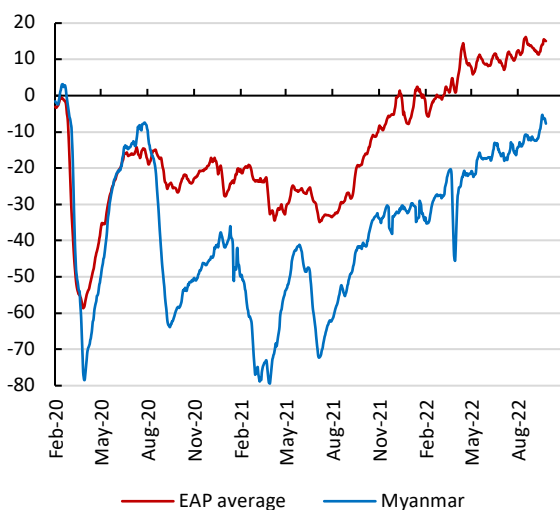
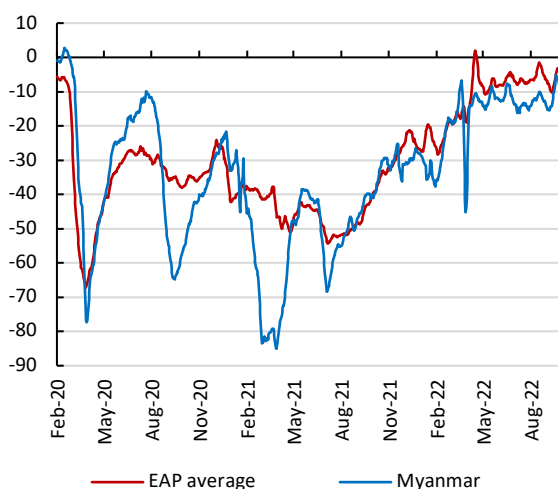


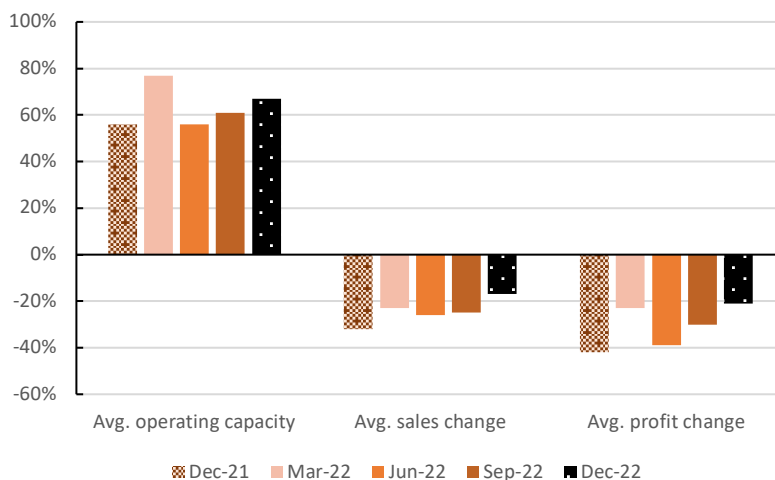
Figure 5: Transport mobility



Source: Google COVID-19 community mobility report

Note: Smoothed series. EAP average includes Indonesia, Malaysia, Philippines, Thailand, Vietnam, Cambodia, Lao PDR, Mongolia, Myanmar, Fiji and PNG. Data series discontinued in October 2022.

Figure 6: Retail and wholesale firms' performance



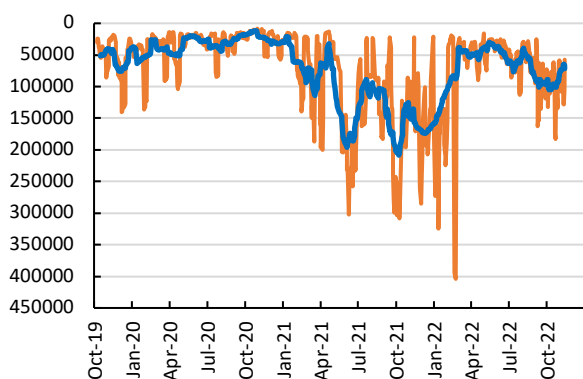
Source: World Bank firm monitoring surveys

Note: Firms were asked to report about the last completed month. In December 2021 and March 2022, firms were asked to report about sales and profits compared to January 2021, while in other periods they reported changes compared to the same period last year.

Despite improved mobility, the retail and wholesale sector has been adversely impacted by higher prices, import shortages, and weak consumer demand. In the World Bank firm surveys, retail and wholesale firms report that sales are 17 percent lower in December 2022 than they were in December 2021, following a 32 percent reduction over the year prior (Figure 6). Over the last six months, some imported goods have been in short supply due to import restrictions, difficulties in obtaining import licenses and foreign

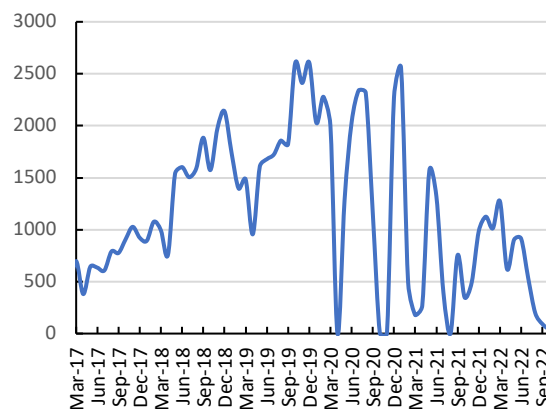
exchange, and rising transport costs. Some domestically produced items have also been in short supply due to restrictions on imported raw materials. At the same time, increasingly strained household budgets (see section H) appear to have prompted consumers to reduce consumption and delay non-essential purchases. Indicators of retail activity on shop.com.mm also suggest that purchases weakened in the second half of 2022 (Figure 7). Vehicle sales have trended sharply lower since the two COVID-19 waves in 2020 (Figure 8). While sales volumes have fallen, retailers have attempted to maintain profit margins by passing on increased costs to consumers. Some retailers have reportedly reduced packaging sizes while maintaining existing sticker prices.

Figure 7: Alexa internet traffic ranking for shop.com.mm (higher rank denotes less traffic)



Source: shop.com.mm

Figure 8: Number of vehicle sales



Source: ASEAN Automotive Association

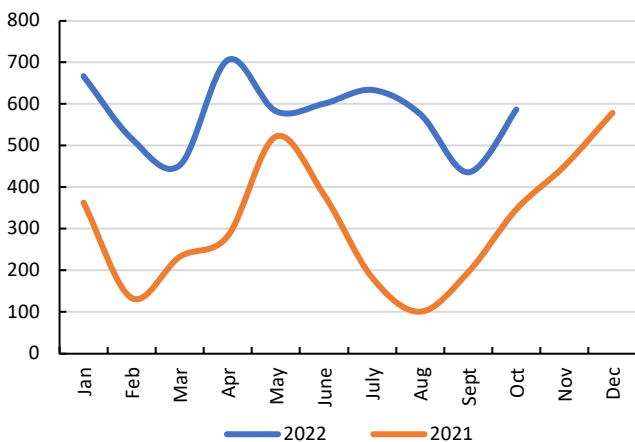
The recovery in the use of public transport services has likely been dampened by a significant increase in prices. Railway services have resumed operation since July 2022 although not all routes are operational and there has been an average 60 percent increase in ticket prices. The number of daily passengers on Yangon Bus Services (YBS) has increased from an average of 800,000 in May 2022 to 1.3 million in October 2022. The bus fare system in Yangon has changed from fixed charges to distance-based fares. While public transport operations have been recovering, increasing prices have reduced affordability, especially in Yangon where the low-income populations depend on bus services for commuting to jobs and access to services.

While the aviation sector has been recovering, there has only been a marginal increase in international tourists. The number of domestic flights from Yangon International Airport from January to October 2022 was twice as high as the same period in 2021 (Figure 9). Both domestic and international air travel increased following the relaxation of COVID-19 restrictions and resumption of international flights in April 2022. More international airlines have commenced regular flights to Myanmar since June 2022, and covid restrictions have eased.² But in sharp contrast to the rest of the region, international tourism arrivals remain more than 90

² In September 2022, Myanmar Airways International (MAI) began operating round-trip flights between Yangon, Dubai, and Hanoi twice a week and Ho Chi Minh city once a week. Further additional direct flights to Phuket and Phnom Penh from Yangon twice a week were launched in October and November 2022, respectively.

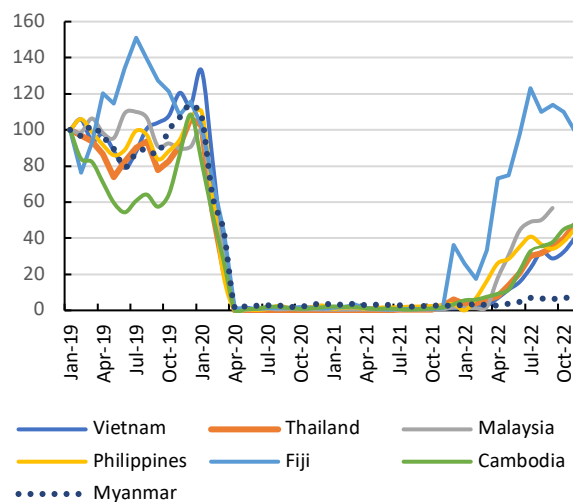
percent below pre-pandemic levels (Figure 10). Prior to the pandemic, tourism was estimated to account for around 5 percent of GDP.

Figure 9: Domestic Outbound Flights from Yangon International Airport



Source: Yangon Region Public Transport Committee (YRTC)

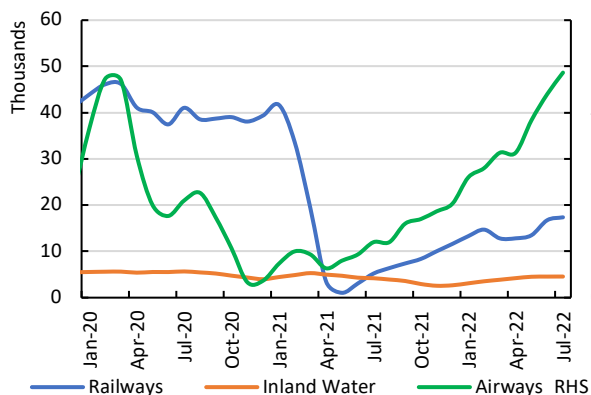
Figure 10: International tourist arrival index (Jan 2019 = 100)



Source: Haver Analytics and CEIC

Domestic freight transportation has continued to rise gradually in 2022 (Figure 11) but remains constrained by rising fuel prices and constraints on movement, including those associated with security checkpoints and border closures. Freight prices per ton have increased on average by 30-50 percent since the beginning of 2022. Freight by rail remains well below 2020 levels.

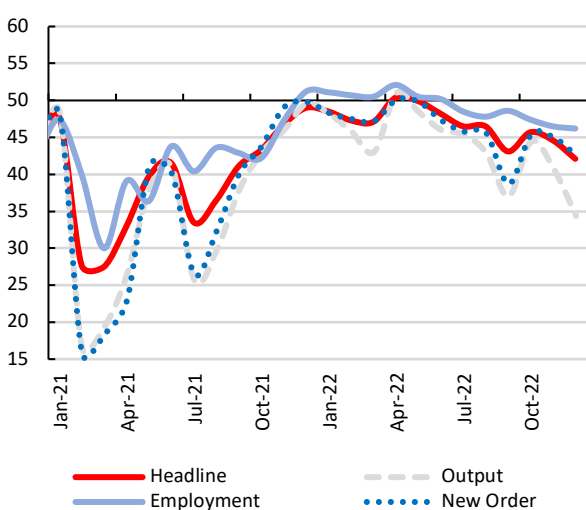
Figure 11: Freight transport (ton miles)



Source: Central Statistical Organization

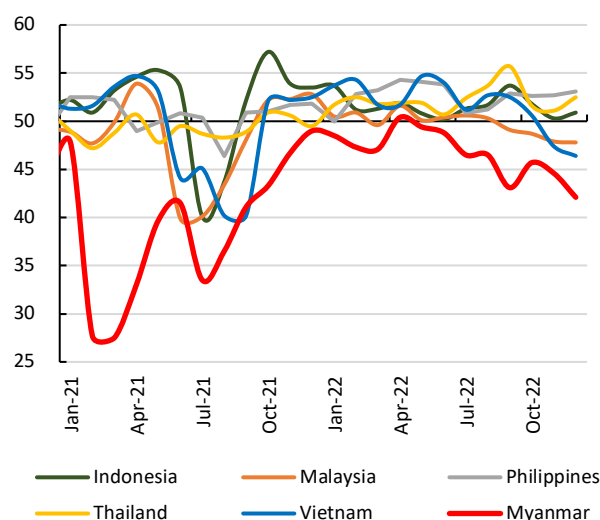
Survey data indicates that the manufacturing sector has contracted since mid-2022 due to weaker demand, rising costs, power outages, and logistics constraints. The manufacturing Purchasing Managers' Index has contracted since May 2022, after showing signs of stabilization earlier in the year (Figure 12). The performance of the sector remains substantially weaker than that observed in the rest of the region (Figure 13). New orders have fallen due to weak customer demand, in part attributed to financial constraints and the cumulating impacts of rising prices on real incomes. On the supply side, production has been constrained by shortages of materials and electricity outages. Supply chain pressures (as proxied by suppliers' delivery times) worsened significantly in the September quarter, in part due to rigid customs checks, but appear to have eased in more recent months. The contraction in the sector has had an impact on employment, due to a combination of resignations and staff cuts due to lower sales, though almost 90 percent of the surveyed firms reported no change in hiring activity.

Figure 12: Manufacturing Purchasing Manager's Index
(>50 indicates expansion, < 50 indicates contraction)



Source: IHS Markit

Figure 13: Manufacturing Purchasing Managers' Index – regional comparison



Source: IHS Markit

World Bank firm surveys indicate that manufacturers were adversely affected by the exchange rate volatility experienced in July and August, but that conditions have improved since. In September, forty-four percent of firms reported that kyat volatility was their biggest challenge in September (Figure 3), and firms reported operating at just 52 percent of their capacity, down from 72 percent six months earlier, with sales and profits sharply lower (Figure 14). By December, the share of manufacturing firms reporting exchange rate volatility as their biggest challenge had halved. Average operating performance had also recovered, but remained below levels earlier in the year.

Supply and demand conditions continue to vary across manufacturing sub-sectors. The export-based garment sector performed comparatively well through most of 2022, with a sharp rise in manufacturing exports in the middle of the year driven by a seasonal increase in demand from major trading partners, and some

reported frontloading of this demand as businesses anticipated constraints following the announcement of FATF blacklisting. However, motor vehicle production has declined rapidly since July (Figure 15), reflecting foreign exchange shortages and reduced demand (in part due to supply-side increases in costs). The rice milling industry has been adversely affected by electricity and fuel shortages, as well as expected declines in local production (see below). In general, manufacturers of food and consumer goods have been more adversely affected by weak domestic demand, although some retailers and consumers have turned to locally produced goods – particularly food products – as the price of imports has risen.

Figure 14: Manufacturing firms' performance

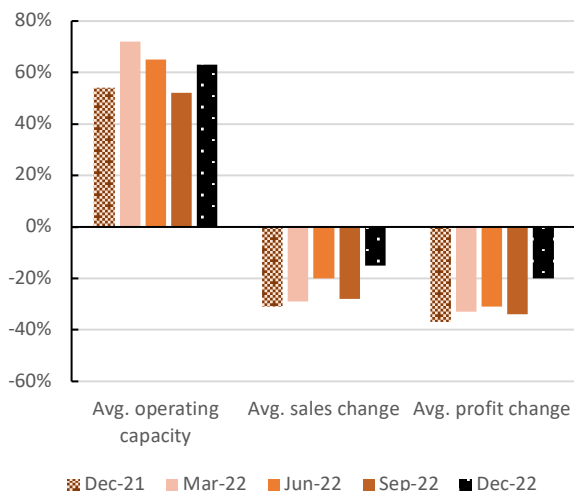
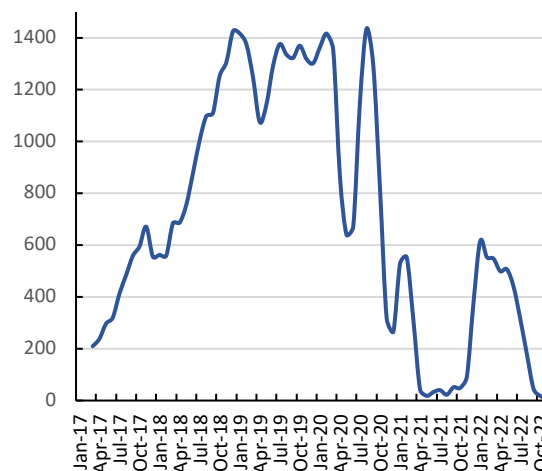


Figure 15: Number of vehicles produced



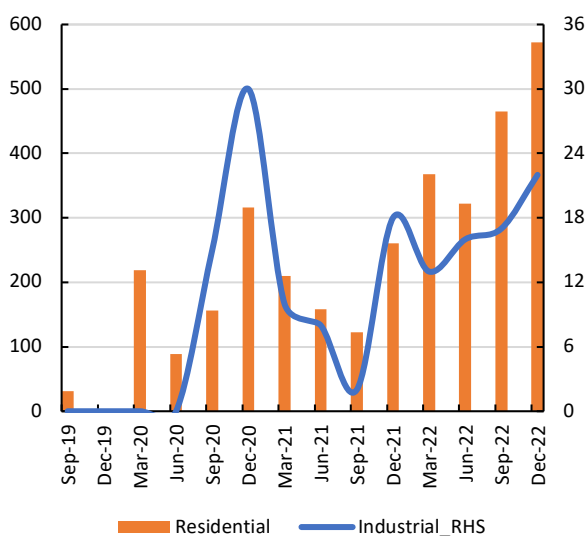
Source: World Bank firm monitoring surveys

Note: Firms were asked to report about the last completed month. In December 2021 and March 2022, firms were asked to report about sales and profits compared to January 2021, while in other periods they reported changes compared to the same period last year.

Source: ASEAN Automotive Federation

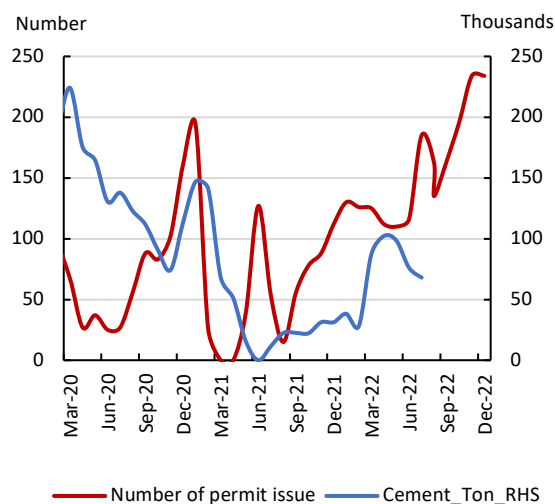
Construction activity has continued to expand driven by residential buildings and the implementation of public sector infrastructure projects in some sectors. Residential construction, which contributes around half of total construction work, has increased substantially since mid-2021 based on the increase in construction permits for residential buildings over this period (Figure 16). There is generally only a short lag (one month) between issuing construction permits and starting construction. Residential construction has been supported by increased investment in affordable housing projects and increased demand for housing, partly driven by an increase in demand for safe assets. The construction sector has also been supported by increased investment in the construction of bridges and railway upgrades, among other public infrastructure projects. However, commercial construction activity (such as hotel and shopping center projects) remained weak during FY22, reflecting continued economic uncertainty and weakness in demand. The trend upwards in cement imports provides further evidence of an expansion in construction activity since mid-2021 (Figure 17).

Figure 16: Total number of construction permits issued



Source: Yangon City Development Committee

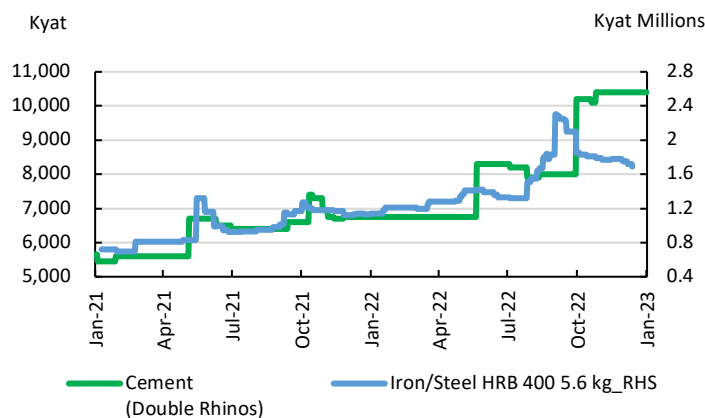
Figure 17: Number of construction permits issued vs cement imports (tons)



Source: Yangon City Development Committee and CEIC

However, construction activities continue to be constrained by rising input prices. Import price increases and shortages of imported inputs have caused delays and reduced the profitability of ongoing projects. The cost of construction materials has increased significantly due to import restrictions, exchange rate depreciation, supply chain disruptions and logistics constraints. As of late 2022, the price of imported cement was 27 percent higher than in June and 54 percent higher than in January (Figure 18). The price of iron and steel rod doubled over the year to September 2022. Locally produced construction materials prices have also increased due to rising transportation costs.

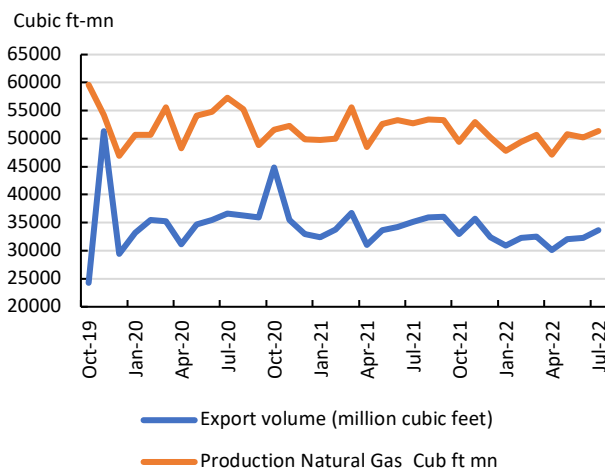
Figure 18: Price of construction materials



Source: Retail shop of construction materials

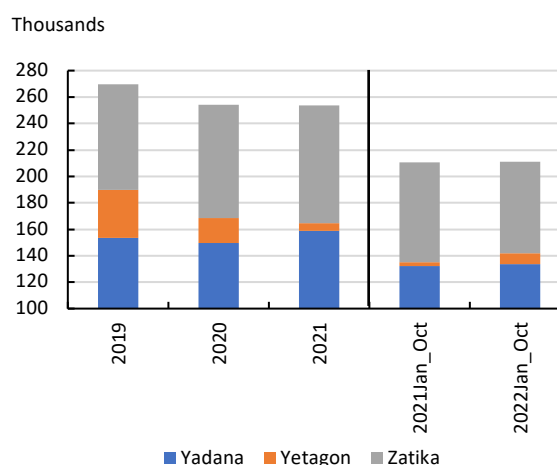
Natural gas production has remained resilient. Oil and gas production was broadly stable in the year ended September 2022 (Figure 19). Between October 2021 and September 2022, production and export volumes to Thailand from the Yadana and Yetagan fields were up by 5 percent and 57 percent year-on-year, respectively, offsetting the decline in exports from Zawtika (Figure 20). But overall production at Yetagan remains very low, reflecting the gradual depletion of gas stocks, with production rates dropping below the technical threshold. The PTTEP has launched the next phase of oil and gas development by offering large contracts for four wellhead platforms at the Zawtika offshore gas project.

Figure 19: Natural Gas export and Production volume (million cubic feet) between October to January



Source: CEIC

Figure 20: Natural gas export to Thailand (MFSCFD)



Source: Thailand Ministry of Energy

Agricultural production has been hampered by higher input prices, logistics constraints, and exchange rate surrender requirements. Paddy production is expected to have declined in 2022 due to less favorable agronomic conditions at the onset of the monsoon season and lower use of inputs. Overall, the total paddy production in the 2022 calendar year, including the secondary crops to be planted at the end of the year, is forecast at 23.8 million tons, about 10 percent below the five-year average level. Prospects for the 2022 monsoon season crop (usually around 80 percent of the total annual rice production) point toward a lower output, with more than half of all rice millers surveyed by IFPRI expecting monsoon output to decline by more than 10 percent. While rice prices have increased, this appears to be mainly because of low domestic production rather than higher domestic or foreign demand. Moreover, Myanmar’s rice exports have become less competitive in international markets due to the establishment of foreign exchange surrender requirements which force conversion of foreign currency earnings at the overvalued official exchange rate.

Higher costs have affected the use of fertilizers and other inputs, which translates into lower output levels. During the 2022 monsoon growing season, an IFPRI survey in July 2022 found that input prices were substantially higher than the same period last year, especially for urea (+91 percent) and for compound fertilizers (+75 percent), while herbicide and pesticide prices increased by 50 and 40 percent, respectively. These higher prices have led to a decline in fertilizer use. Nation-wide, half of all farm households reduced agricultural

input expenses as one of their mechanisms to cope with shocks.³ Transport costs are another commonly cited constraint. In an August 2022 IFPRI survey, two-thirds of agricultural crop traders reported that rising transport costs were the most significant disruption they experienced that month.⁴

More farmers are holding on to their paddy harvest compared to previous seasons. This could be for a variety of reasons: farmers could be storing for later sowing; for own consumption; or because they are experiencing difficulty selling produce. As of February/March 2022, 35 percent of paddy farmers had not sold rice yet from the monsoon of 2021, compared with 27 percent for the same period one year earlier. In terms of the amount of paddy sold, farmers reported in June 2022 having sold 64 percent of paddy production from monsoon 2021-22, less than the 71 percent of the paddy harvested one year earlier from monsoon 2020-21.⁵

Farmers are attempting to take advantage of higher prices for non-rice cash crops, which have been sustained by foreign demand. Many these crops are grown as a source of sales income rather than for own consumption. Farmgate prices have increased over the last year, especially for export crops, such as maize (+53 percent, exported mostly to Thailand) and pigeon pea (+44 percent, to India). However, the price competitiveness of many these exports has also been affected by the aforementioned foreign currency surrender requirements. Non-export crops showed smaller increases (+15 percent for sesame; +15 percent for groundnut; +7 percent for tomato). FAO estimates for the 2022 calendar year predict maize crop production to be above the average of 2.2 million tons, although average yields will be at the lowest since 2015 due to pests, diseases, and restricted access to agricultural inputs.

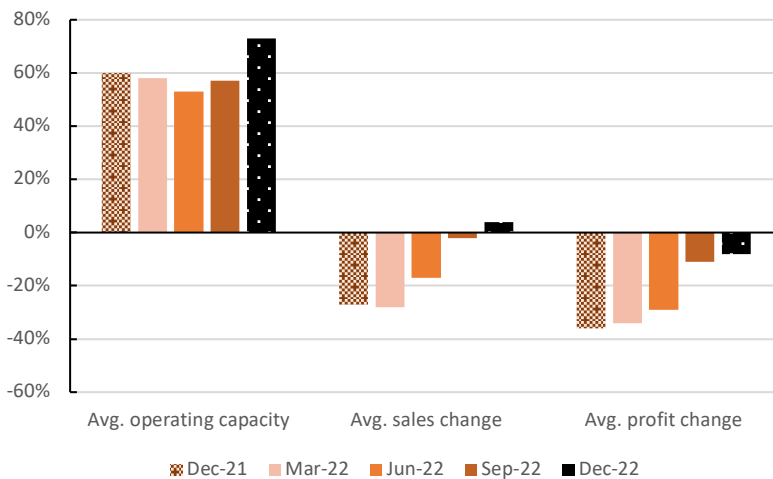
The World Bank's recent firm monitoring survey suggested that agricultural firms' business performance improved in December 2022 (Figure 21). On average, agricultural firms reported operating at almost three quarters of their capacity, a sharp rise from previous quarters and the highest since June 2021. With improved operating capacity attributable to the harvesting season, sales and profits have also improved.

³ IFPRI 2022.. “Vulnerability and Welfare. Findings from the third round of the Myanmar Household Welfare Survey” (July and August 2022), Strategy Support Program Working Paper 26, November.

⁴ International Food Policy Research Institute Myanmar. “Monitoring the Agri-food system in Myanmar: Agricultural crop traders – August 2022 survey.” October 2022.

⁵ IFPRI 2022.. “Myanmar Agricultural Performance Survey (Q1 2022) Farmgate prices and marketing by crop farmers”. Research Note 81, June.

Figure 21: Agricultural firms' performance



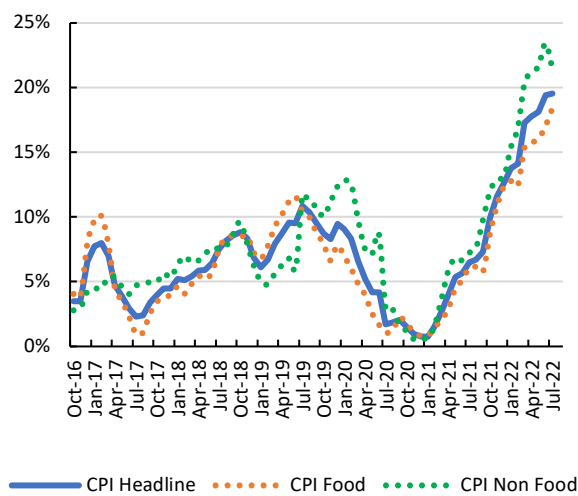
Source: World Bank firm monitoring surveys

Note: Firms were asked to report about the last completed month. In March and December 2022, firms were asked to report about sales and profits compared to January 2021, while in other periods they reported changes compared to the same period last year.

C. Prices have risen sharply

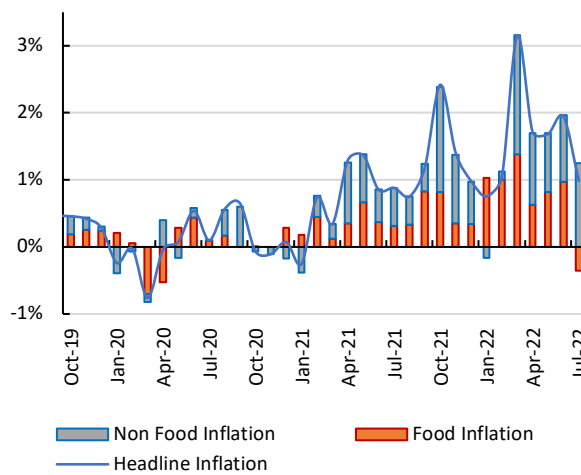
Inflation has risen markedly during FY2022, driven by fuel price increases and kyat depreciation. CPI inflation increased to 19.5 percent (YoY) in July 2022 from 6.5 percent at the same point last year, reflecting increases in both food and nonfood prices. Inflation has been driven by cost-push factors such as input shortages, global price movements and exchange rate depreciation, while demand-pull factors (weak private consumption and investment) have had a containing influence. Non-food inflation rose to 21.4 percent from 7.2 percent last year (Figure 22 and Figure 23), driven mainly by domestic fuel price increases and kyat depreciation, which triggered increases in the prices of a broader range of imported inputs. Although world crude oil (Brent) prices have declined since May 2022, domestic fuel prices have remained relatively high, with the fuel price (Octane 95) around 2,200 kyats per liter in December — 13 percent higher than the end of July, and 53 percent higher than a year ago (Figure 24). The increase in domestic fuel prices is largely explained by sharp exchange rate depreciation and fuel scarcity, which has been more pronounced in Myanmar's remote areas. Several fuel stations across Myanmar — including in Yangon and Mandalay — have at some point in time had to shut down operations (particularly when regulated reference prices have fallen below cost price) or ration limited quantities.

Figure 22: CPI inflation



Source: Central Statistical Organization

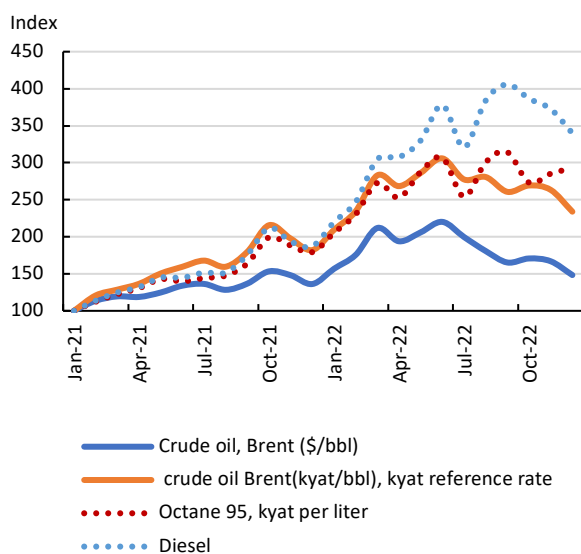
Figure 23: Inflation (MoM)



Source: Central Statistical Organization

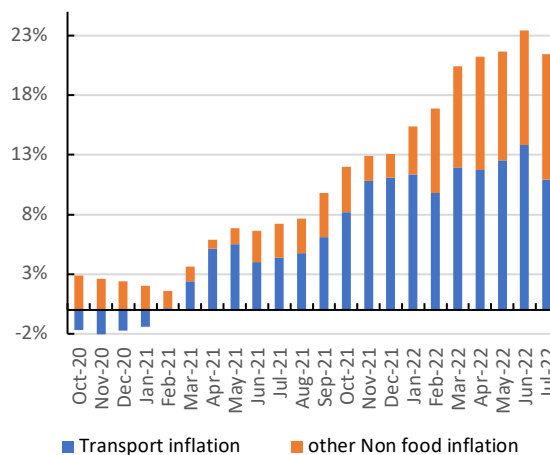
While transport inflation was responsible for almost all of non-food inflation in 2021, the drivers of non-food inflation have broadened in 2022. This indicates that higher fuel prices and exchange rate depreciation have passed through to the prices of a broader range of imported and locally-produced products (Figure 25).

Figure 24: Fuel price and key drivers, January 2021=100



Source: World Bank commodity price, Denko

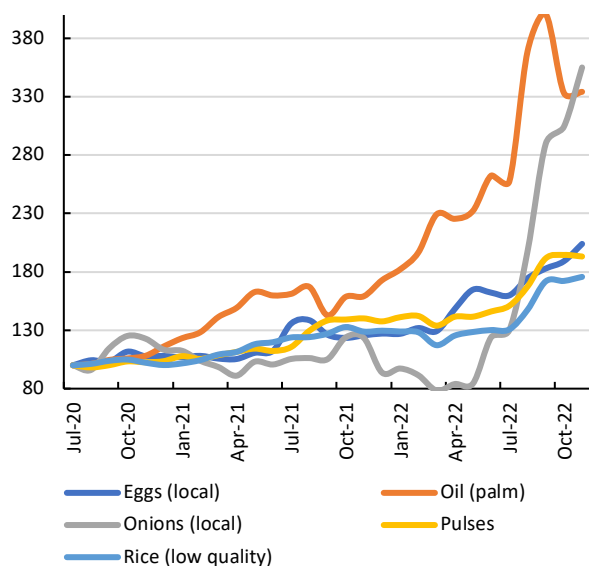
Figure 25: Contributions to non-food inflation



Source: Central Statistical Organization

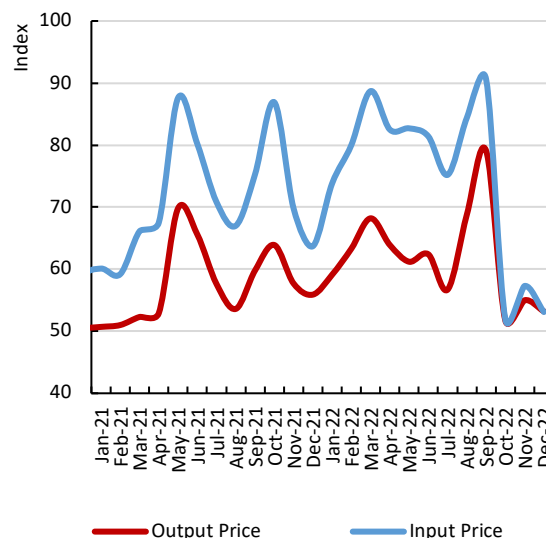
Food prices have continued to rise, with the sharp exchange rate depreciation in July and August corresponding to a noticeable acceleration in the prices of palm oil, rice, and pulses (Figure 26). However, WFP data indicate that rice and pulses prices appear to have stabilized more recently, and palm oil prices have fallen following lower international demand and declining international prices. Conflict, logistics and supply chain disruptions, and differential patterns of production mean that there is still substantial variation of prices at the state and region level.

Figure 26: Basic food prices (Index July 2020 =100)



Source: World Food Programme

Figure 27: Purchasing Managers' Index (PMI) input and output prices



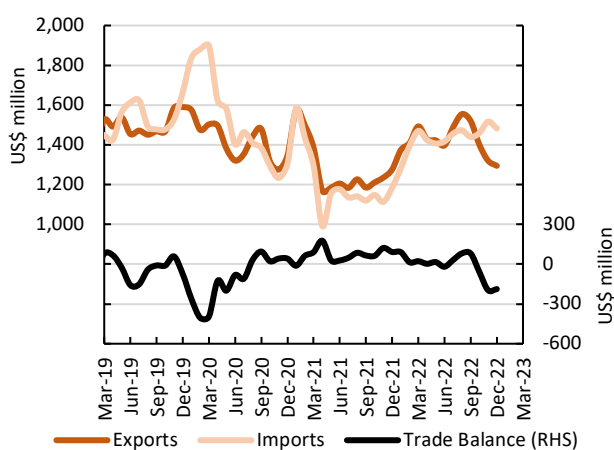
Source: IHS Markit

Manufacturing PMI price indices show that a large proportion of manufacturing businesses have experienced increased input prices over the past two years. Almost all surveyed firms reported higher input prices in September 2022, with most passing those through to output prices (Figure 27). However, the indices show that both input price and output price inflation have eased since October as the kyat stabilized.

D. Trade has been relatively resilient⁶

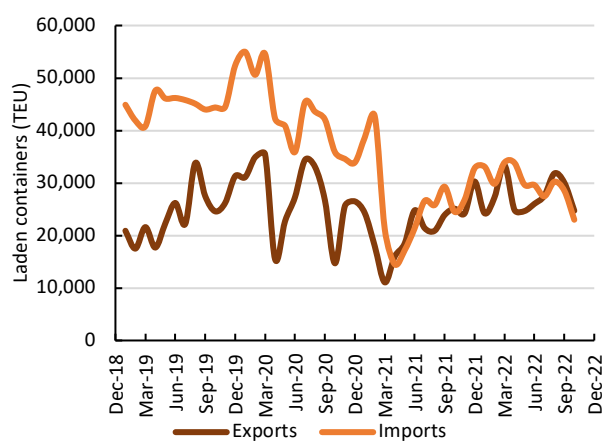
Despite trade and foreign exchange restrictions, Myanmar's international trade remained resilient overall in the second half of 2022, though the value of exports has declined since September.⁷ Compared with the same period last year, exports and imports increased by 14 percent and 27 percent, respectively, in the second half of 2022 (that is, July to December; Figure 28). Trade by sea has been relatively stable at around pre-pandemic levels in 2022, broadly consistent with trends in the shipping of laden containers (Figure 29). Trade over land borders increased by 23 percent in H2 2022 compared with the same period last year, despite continued land border disruptions. Since June, imports have gradually trended upwards while exports have declined after peaking in September.

Figure 28: Trade flows



Sources: CEIC; Ministry of Commerce
 Note: Data reflects a 3-month moving average.

Figure 29: Exports and imports of laden containers



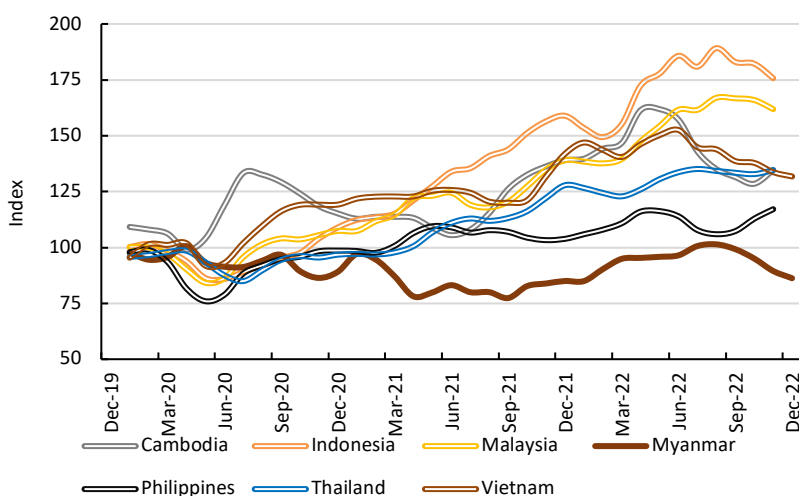
Source: Shipping operators
 Note: Laden container data is available up to October 2022.

While goods exports have risen from 2021 levels, Myanmar's export performance has been well below other countries in the region (Figure 30). Since 2019, both manufacturing and agricultural exports (which, respectively, account for around a half and a quarter of overall exports) have fluctuated from month to month without showing a clear upward trend. In the other countries in the region, exports have risen to well above pre-pandemic levels, supporting overall economic growth.

⁶ All figures related to trade in this section are from CEIC and the Ministry of Commerce (MOC). Monthly figures up to July 2022 are from CEIC, and figures from August 2022 to December 2022 are from the MOC's website—which gathers data from the Customs Department under the Ministry of Planning and Finance (MOPF). Monthly figures from August to December 2022 are extracted from weekly cumulative figures—which could result in slight variances to the data published in the Selected Monthly Economic Indicators of the CSO.

⁷ The first half of 2022 (H1 2022) represents the period between January and June 2022, and the second half of 2022 (H2 2022) represents the period between July and December 2022.

Figure 30: Myanmar's goods exports in comparison with regional peers (2019 average = 100)



Sources: WB Staff calculations using data from CEIC; Ministry of Commerce
 Note: Goods export values are seasonally adjusted.
 Data reflects a 3-month moving average.

However, mirror data suggest a possibility that Myanmar exports could be understated in the official trade data.⁸ In particular, while Myanmar’s recorded exports to China have remained stable at relatively low levels over much of the past two years, China’s recorded imports from Myanmar have been much higher and significantly more volatile (Figure 31). In November 2022, the gap was around US\$ 1 billion, and China’s recorded imports from Myanmar rose even higher in December (to almost US\$ 2 billion). The gap between the two measures, which has gradually trended higher since early 2021, could reflect an increase in informal or illicit exports which are recorded by China as imports but not by Myanmar. These could include rare earths, gold, or precious stones, among others. Between May 2017 and October 2021, Myanmar reportedly exported more than 140,000 tons of rare earth deposits to China, worth more than U.S. \$1 billion.⁹ On the other hand, the difference between Myanmar’s reported exports to Thailand and Thailand’s reported imports from Myanmar has remained relatively contained over the same period (Figure 32).

⁸ World Bank (2022), “[Myanmar Trade & Investment Update](#)”, April – September 2022.

⁹ Radio Free Asia. 2022. “[China-led rare earth mining in Myanmar fuels rights abuses, pollution: Report](#).” August 9, 2022.

Figure 31: Myanmar’s exports to China

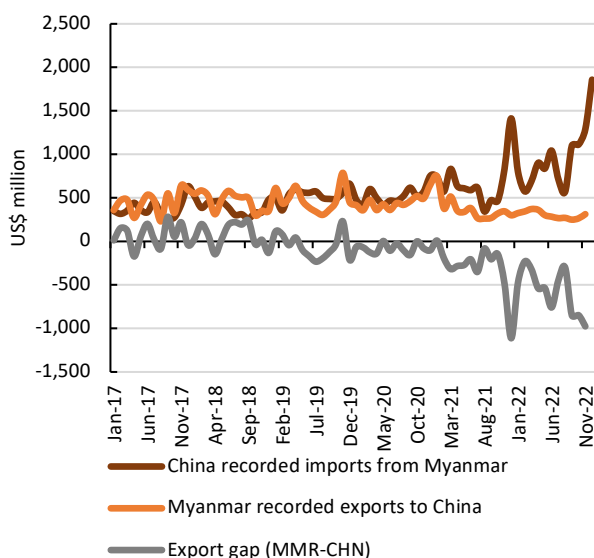
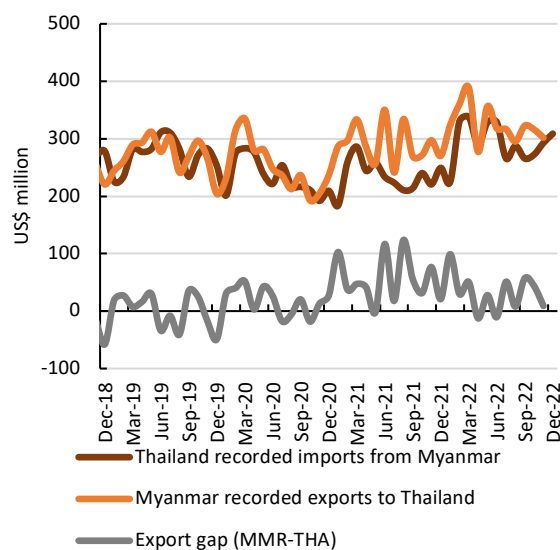


Figure 32: Myanmar’s exports to Thailand



Sources: The General Customs Department of China, the Ministry of Commerce of Thailand, the Central Statistical Organization of Myanmar, and the Ministry of Commerce of Myanmar
 Note: Myanmar’s data is available up to November 2022.

The official data show that manufacturing exports rose sharply in the September quarter, likely driven by garment demand, but this increase was subsequently unwound (Figure 33). Manufacturing exports increased by 48 percent in H2 2022 compared to the same period last year, and by 17 percent compared to the same period in 2019. Garments drove the overall increase in manufacturing exports which peaked in September (Figure 34), supported by strong demand from the European Union (EU), Japan and Korea (Figure 35), which together account for three-quarters of Myanmar's total garment exports. Reports suggest that demand for winter jackets from Myanmar was particularly strong. However, declining demand from the major partners later in 2022 is likely to have affected Myanmar's garment exports over the same period. Some garment factories have closed temporarily or reduced their operating hours as orders for spring clothing from Japan, Korea, and the EU have been either reduced or not yet received.¹⁰ Weaker export demand is likely to at least in part reflect slowing growth in the global economy more broadly. Myanmar garment exporters also face other sources of uncertainty, with Primark¹¹ and Marks & Spencer (M&S)¹² recently announcing intentions to halt sourcing from Myanmar in response to a report by the Ethical Trade Initiative (ETI) published in September 2022.

Natural gas exports also contributed to the overall increase in export values. Mirror data suggests that the US dollar value of Myanmar's gas exports to China has increased since the June quarter of 2022, while the

¹⁰ Irrawaddy. September 24, 2022. “Some factories in Yangon shut down due to no orders.”
¹¹ YarnsandFibers News Bureau. September 20, 2022. “Primark to halt Myanmar sourcing on ETI guidance”
¹² Marks and Spencer. October 11, 2022. “M&S Statement on the Myanmar Enhanced Due Diligence Sectoral Assessment”

volume of gas exports to Thailand remained relatively stable (Figure 34). Increases in US dollar values likely reflect rising prices given that other data indicates that the volume of overall exports has been broadly stable.

Figure 33: Major exports by product groups

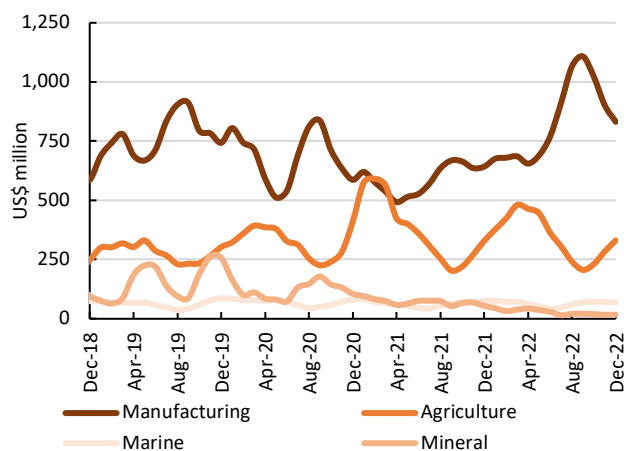
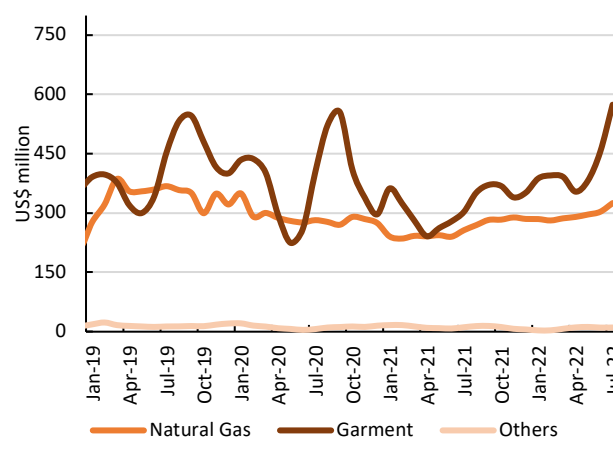


Figure 34: Manufacturing exports by products



Sources: CEIC; Ministry of Commerce

Note: Data reflects a 3-month moving average. Data for manufacturing exports by products is available up to July 2022.

Figure 35: Total garment imports by the EU, Japan, and Korea

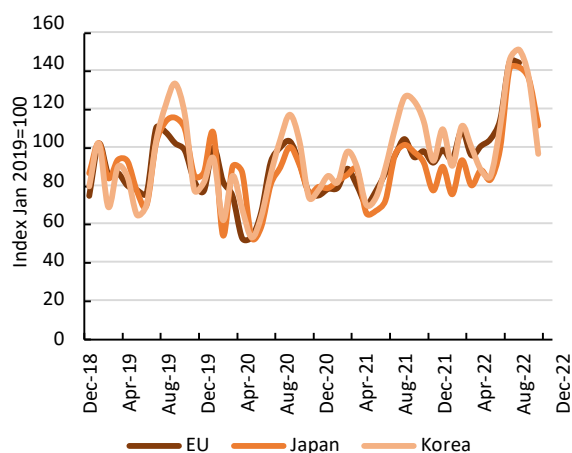
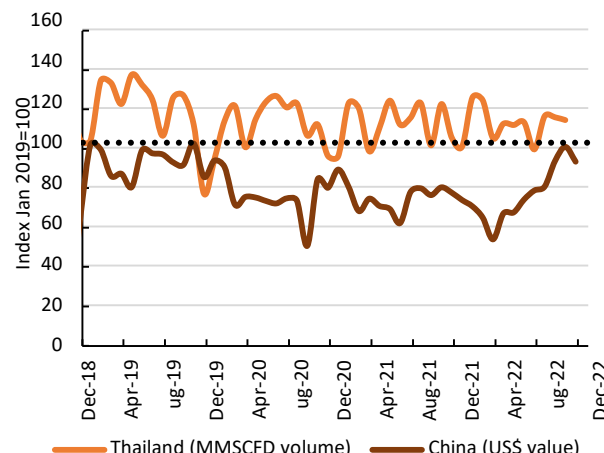


Figure 36: Myanmar's natural gas exports to Thailand and China



Source: CEIC

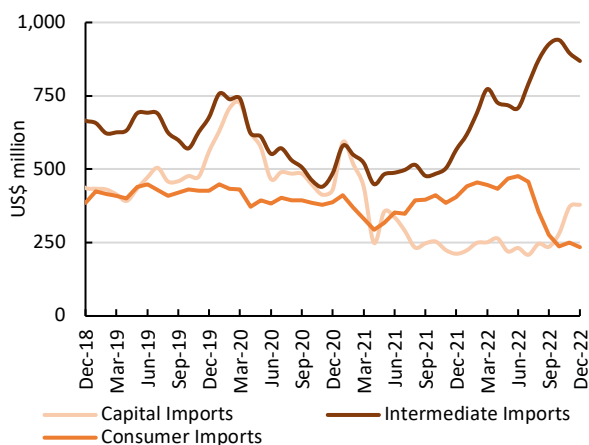
Note: Data represents the total garment imports of the EU, Japan, and Korea (not just imports from Myanmar). Data for the EU is available up to September 2022, and data for Japan and Korea is available up to November 2022.

Sources: China's General Administration of Customs and Thailand's Energy Policy and Planning Office (EPPO).

Note: Data available up to December 2022 for China and November 2022 for Thailand. Data is mirrored using gas imports reported by China and Thailand to proxy Myanmar's gas exports to partners with the most updated data. Given a unit difference between gas exports to China and Thailand, data is indexed at Jan 2019=100. Natural gas imports reported by China and Thailand are available in value (US\$) and volume (million standard cubic feet per day–MMSCFD), respectively. Given that imports from Myanmar reported by China are unavailable at HS 6-digit level, HS 4-digit level (HS 2711) is used to proxy natural gas (HS 271111).

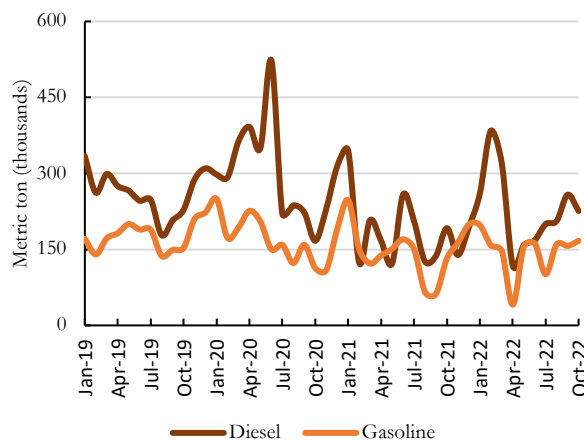
Agricultural exports showed a seasonal recovery in the December quarter (Figure 33). Historical trends suggests that agricultural exports tend to decline in the September quarter with major crops, including monsoon rice, in the growing and sowing stages. But as major crops have entered the harvesting season, agricultural exports have increased since October 2022. Looking through the seasonality, agricultural exports (in US dollar terms) in H2 2022 increased by only 1 percent compared to the same period last year and remained 16 percent lower than the 2020 level.

Figure 37: Imports by product groups



Sources: CEIC; Ministry of Commerce
Note: Data reflects a 3-month moving average.

Figure 38: Refined mineral oil imports by product



Source: Shipping operators

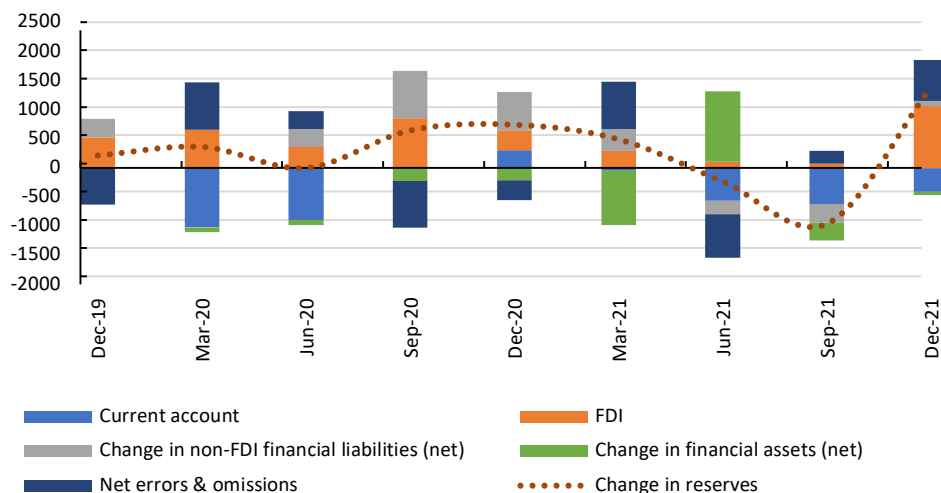
Intermediate imports remained the main driver of overall import growth in the second half of 2022 (Figure 37). Compared to the same period last year, the value of intermediate imports was 72 percent higher in H2 2022, primarily driven by increases in import prices, including fuel (Figure 38) and fertilizers, as well as increases in cut-make-pack (CMP) imports (inputs for garment production). Consumer product imports have weakened considerably since mid-2022, with the kyat depreciation further reducing affordability in a context of already weak demand for consumer products. In addition, import license requirements and bans on certain imports through land borders (including beverages, soap and toothpaste, motorcycles) may have contributed to this decline. On the other hand, capital imports picked up noticeably in the December 2022 quarter to reach their highest level since early 2021. This could partly be attributable to the relaxation of import license requirements for a range of agricultural machinery items in August 2022, and/or may provide an early indication that investment appetite is recovering more broadly.

E. The exchange rate has been volatile

The latest publicly available data indicate that balance of payments pressures were contained through the 2021 calendar year, with FDI inflows picking up in the December quarter (Figure 39). The current account deficit narrowed in the December quarter 2021 due to a declining goods trade deficit, which more than offset a reduction in remittance receipts. Pressures on the financial account eased with foreign direct investment (FDI) flows rebounding, after remaining very low through most of 2021. However, more recent data shows that FDI commitments have in general remained weak compared to 2019 and 2020 levels, despite

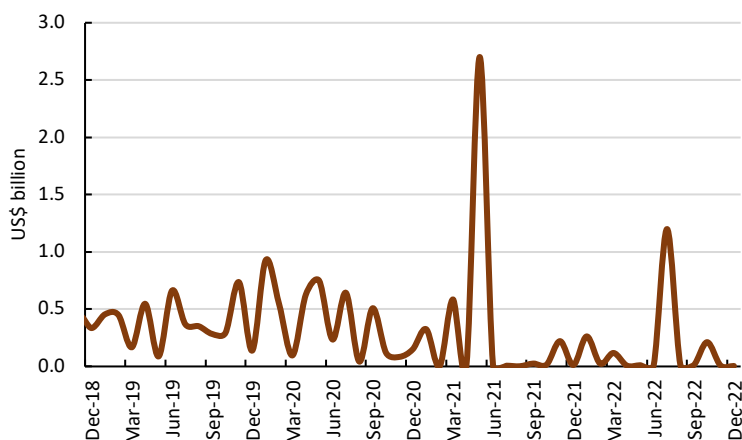
a spike in July 2022 (Figure 40). Total FDI commitments were about US\$1.46 billion in the second half of 2022, with July 2022 alone accounting for 83 percent of this total. The commitments in July 2022 came from six Singaporean solar power firms, another Singaporean firm developing ports and stores to provide services for the offshore drilling industry, and a Chinese garment manufacturing firm.¹³

Figure 39: Balance of payments (USD, millions)



Source: Central Bank

Figure 40: FDI commitments



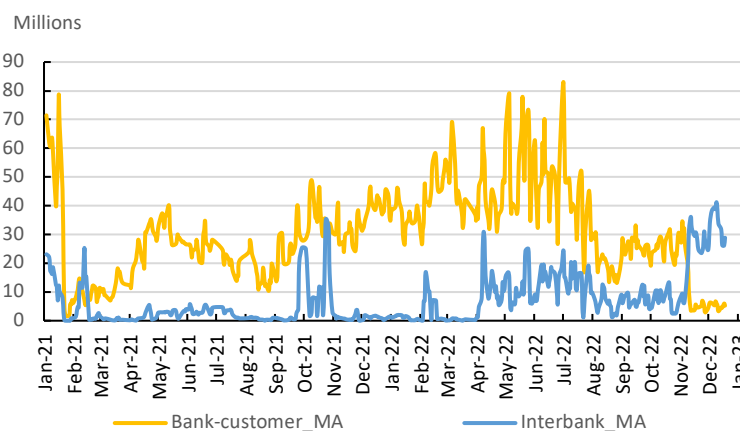
Source: DICA

¹³ Irrawaddy. August 1, 2022. [“Myanmar civilian government warns foreign firms investing under junta.”](#)

Over the full year to December 2021, a balance of payments surplus was recorded, consistent with an increase in foreign exchange reserves. A balance of payments surplus of USD 1.4 billion (that is, accounting for both current and financial account flows) was recorded in the December quarter of 2021, following a deficit of USD 1 billion in the previous quarter. The data is consistent with an increase in reserves of almost US\$700 million over the full 2021 calendar year.¹⁴ This implies that net foreign exchange inflows – FDI and other investment flows in particular, given the current account was in deficit throughout 2021 – were more than sufficient to offset the CBM’s explicit market interventions to support the value of the kyat (by way of sales of FX reserves) that took place through much of 2021. However, it is not clear the extent to which the official balance of payments data captures trade and capital flows on informal or unregulated markets, which have likely increased over the past two years, in part to circumvent increasing restrictions on trade and foreign exchange.

Despite the balance of payments surplus recorded in 2021, the persistent exchange rate depreciation experienced over most of the past two years indicates that demand for foreign currency has exceeded supply. CBM auctions of foreign exchange were discontinued in March 2022. Rather than using reserves to support the exchange rate, since that point the authorities have relied on administrative trade and foreign exchange restrictions to keep foreign currency within the country and under the control of the central bank (Part III places these measures in historical context). Over the same period, bank to customer transactions in US dollars have fallen to very low levels (Figure 41). This lack of explicit intervention activity since March 2022 – with the exception of the \$200 million loan that was reportedly issued in August – may be at least in part due to the inaccessibility of some portion of the central bank’s foreign reserve holdings (including the US\$1 billion held at the U.S. Federal Reserve).

Figure 41: US dollar transactions



Source: Central Bank

After a particularly sharp depreciation in July and August, the kyat has stabilized in recent months. Between the beginning of July and the end of August, the kyat lost about half of its value against the US dollar

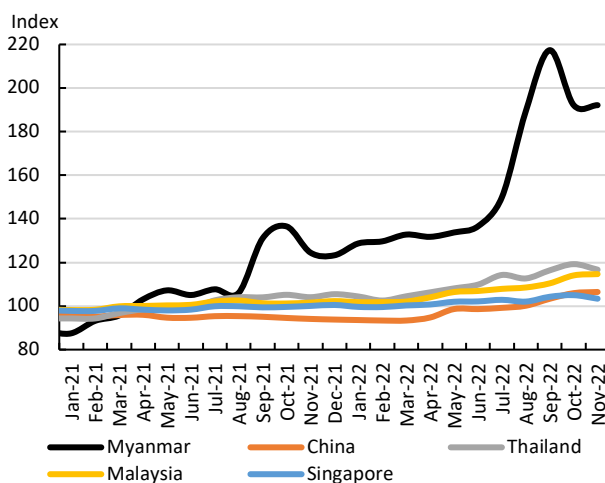
¹⁴ Foreign exchange reserves held at the CBM were last estimated to total around US\$6.8 billion as at September 2020, or around 4.7 months of imports.

(Figure 42). This episode appeared to be triggered by a reduction in the supply of US dollars from the CBM to importers (at the official rate), which drove importers to the parallel market, resulting in panic buying and exacerbating foreign currency shortages. The kyat subsequently recovered in September and as of end-December, it had stabilized at just over 2800 kyat to the US dollar.

The stabilization occurred after the authorities introduced measures that allowed a greater supply of dollars in parallel markets, partially unwinding previously imposed restrictions. In August, the foreign currency surrender requirements that were introduced in April were eased. Exporters are currently required to convert 65 percent of their export earnings into kyat at the official reference rate (2100 kyat to the US dollar) rather than 100 percent as previously. The remaining 35 percent can be sold at market rates, adding to the supply of foreign currency available to those who cannot access US dollars at the reference rate (the reference rate is reportedly available to importers of fuel, edible oil, and other essential items). Remittances have also been allowed to trade at rates above the reference rate and closer to the market rate, attracting greater inflows. The CBM injected US\$200 million into the market (reportedly as a loan or swap facility) to facilitate the import of fuel and other essential commodities as prices soared. More recently, in December, companies which are more than 35 percent foreign owned were exempted from the surrender requirements altogether. At the same time, non-trade related outward payments of US dollars remain heavily restricted and businesses continue to be instructed to reschedule foreign loan repayments (principal and interest). The authorities have increasingly permitted the use of the Chinese yuan and Thai baht to make trade-related payments, reducing the pressure on the US dollar market. To fund their purchase of imports, traders can only access a restricted pool of foreign exchange (earnings from exports or remittances), reducing pressure on informal markets and meaning that these ‘exempted foreign earnings’ are trading at a slightly higher rate than the informal rate.

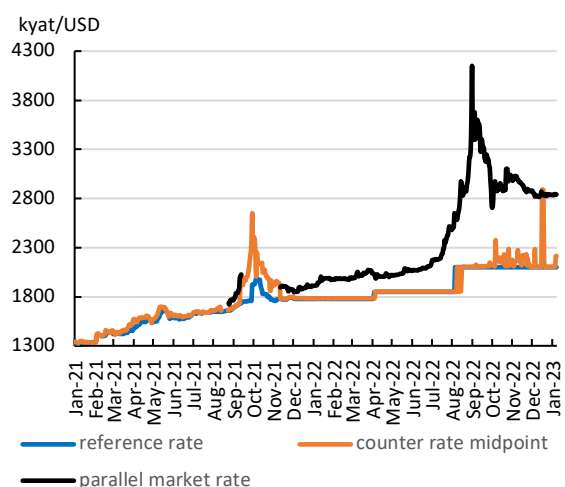
Notwithstanding recent stability in the kyat, exchange rate developments continue to be highly disruptive to the overall economy. As of end December the kyat had depreciated by around a quarter since the beginning of July, resulting in significant price pressures which continue to filter through the economy. The magnitude of this depreciation has been significantly worse than what has been experienced in most other countries in the region (Figure 43). At the same time, despite various interventions from the authorities, foreign currency shortages persist, while surrender requirements continue to impose a substantial tax on many exporters. Together with the need to apply for import licenses and navigate other constraints on trade, the increased cost and limited supply of foreign currency has resulted in many imported products becoming scarcer and more expensive, including basic food items, fuel, and medicines. At the same time, the institution of strict capital controls and the emergence of multiple exchange rates has obscured the price signal that a unified market-determined exchange rate would provide, resulting in inefficiencies in the allocation of resources and opportunities for rent-seeking. It has also severely complicated the operating environment for businesses, increasing regulatory uncertainty and compliance costs.

Figure 42: Asian currencies per US dollar (index, January 2019 = 100)



Source: exchange-rates.org

Figure 43: Myanmar kyat/USD (Reference rate, counter rate, parallel market rate)



Source: Central Bank of Myanmar; Money Exchangers

F. Financial institutions are facing a range of operational issues

Banks and MFIs in Myanmar continue to experience a range of operational issues and challenges.

These include liquidity stress, a reduction in asset quality, and increased delays and scrutiny in the processing of trade and remittances payments and in the handling of other foreign currency services. A survey of MFIs conducted in August and September 2022 by the Myanmar Microfinance Association indicates that non-performing loans have risen dramatically since 2019, increasing from less than 1 percent of MFIs’ total loan portfolio in 2019, to 9.6 percent in December 2020 due to pandemic-related disruptions, and then to 28 percent in June 2022. Branch security and profitability were also reported as key concerns.

In October 2022 the Financial Action Task Force (FATF) blacklisted Myanmar for “failing to address a large number of strategic deficiencies in its anti-money laundering and counter terrorist-financing systems”, highlighting concerns around illicit financial flows. FATF has called for countries to apply enhanced due diligence for financial transactions involving Myanmar, while noting that this enhanced due diligence must not negatively impact humanitarian assistance. The blacklisting has the potential to increase the time and costs involved in moving money into and out of the country, including for trade and remittance payments. This could mean further shifts toward informal unregulated channels for international payments, and toward the use of bank accounts set up outside Myanmar.

The CBM has issued a range of directives that require additional provision of information. In August, banks were subject to additional reporting requirements on foreign exchange transactions. In September, the CBM announced that users of digital payment platforms would be subject to increased requirements around

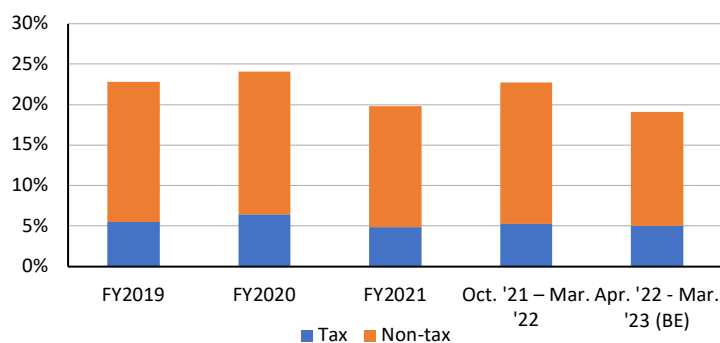
the provision of personal information. These requirements may reduce incentives to use these systems and could similarly drive a shift toward informal methods of transferring funds.

In response to high inflation, the CBM has tightened the monetary policy stance by adjusting reserve requirements. Specifically, the portion of the 3 percent minimum reserve requirement that is required to be deposited at the CBM has increased to 2.5 percent from 2.25 percent, in attempt to reduce the volume of currency in circulation and to control inflation (the remaining cash reserve requirement was correspondingly lowered from 0.75 percent to 0.5 percent). Interest will be paid on additional cash deposits beyond these requirements.

G. The fiscal position has strengthened

Aggregate revenue collection improved in the six months to March 2022.¹⁵ An increase in the income of energy State Economic Enterprises (SEEs) was the main contributor, while tax collections also improved. On an annualized basis, revenues in this period were around 3 percentage points of GDP higher than in the preceding year, while nominal revenue collection rose rapidly due to significant price inflation (Figure 44).¹⁶

Figure 44. Revenue 2019–2023 (% of GDP)



Source: MOPF; WB staff estimates.

Note: BE = Budget Estimate; Data for the period between October 2021 and March 2022 is annualized to enable historic comparison. Non-tax revenue includes revenue from State Economic Enterprises.

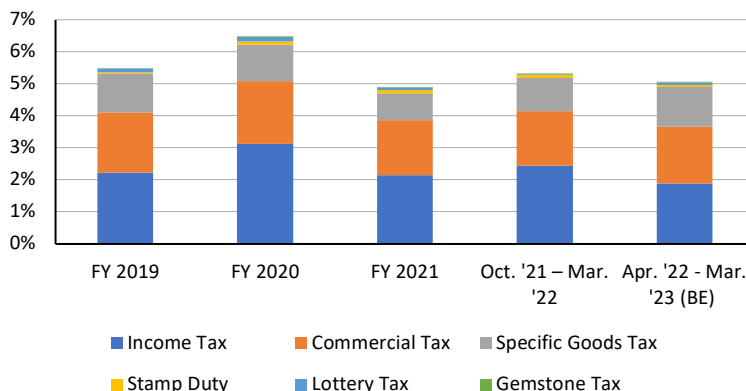
In annualized terms, tax revenue has rebounded to 5.3 percent of GDP in the six months to March 2022 (Figure 45). The rebound in tax collection was broad-based across the different tax lines: income tax,

¹⁵ This was a six-month mini-budget period as the budget year was subsequently changed from an October – September year to an April – March year, beginning in the year starting April 2022.

¹⁶ To accommodate historical comparisons, the implied annualized value for the six months ended March 2022 is used to provide a more accurate context for comparison. Implied annualized amounts assume that the expenditure and revenue in the full 12-month fiscal year would be twice as large as those in the 6-month fiscal year.

commercial tax, and Specific Goods Tax (SGT).¹⁷ Recent World Bank firm surveys show that the share of firms paying taxes to the authorities increased between December 2021 and June 2022 (to close to 2020 levels), but then declined in the September quarter.

*Figure 45. MOPF tax collection
(% of GDP)*



Source: MOPF; WB staff estimates.

Note: BE = Budget Estimate; Data for the period between October 2021 and March 2022 is annualized to enable historic comparison.

Non-tax revenues from energy SEEs rose sharply in the six months to March 2022. Non-tax revenue was boosted by higher than projected profits in energy SEEs. During this period, Energy SEEs recorded a profit equivalent to around 0.4 percent of GDP against the authorities’ original estimate of a loss of 0.1 percent of GDP, a significant improvement from the reported loss of 1.2 percent of GDP in FY2021. Overall, the energy SEEs’ revenue amounted to around 4.3 percent of GDP, equivalent to around 38 percent of overall revenue in the six months to March 2022. Most of this comes from the state-owned Myanmar Oil and Gas Enterprise (MOGE), whose revenue is estimated to contribute about 70 percent of all energy SEE revenue.

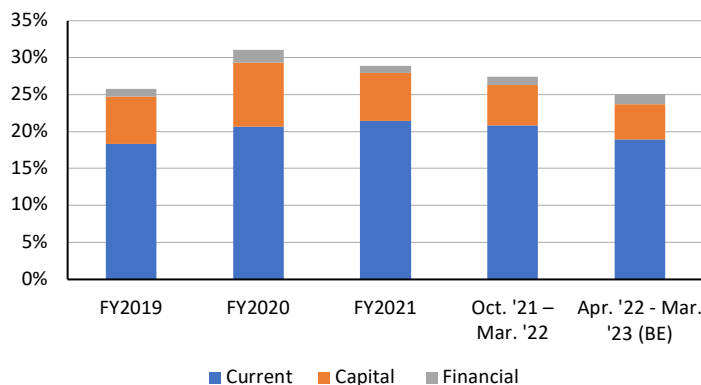
Spending declined in the six months to March 2022. Aggregate spending has decreased to 27 percent of GDP (in annualized terms), down from 31 percent in FY2020 (Figure 46). This has been accompanied by a decrease in capital spending which may have implications for longer-term economic growth.¹⁸ This execution rate (share of budget that has been spent) has improved and is more in line with pre-pandemic trends, after falling markedly in FY2021. However, a large part of the increase in nominal spending over this period was related to the higher prices of goods and services in the economy more generally.

¹⁷ The Specific Goods Tax (SGT) Law replaced commercial tax on a list of specific goods that are imported into Myanmar, manufactured in Myanmar, or exported to a foreign country. The list of specific goods includes products such as cigarettes, tobacco leaves, cigars, wine, beer, as well as natural resource products such as teak, lumber, jade, kerosene, petroleum, diesel and natural gas. The SGT rates range from 5 percent to 60 percent.

¹⁸ See World Bank, “[Myanmar Public Expenditure Review 2017: Fiscal Space for Economic Growth](#)” (Report).

Health and education spending has continued to decline. Combined, they accounted for just 8.5 percent of total spending during the period between October 2021 and March 2022, down from over 10.7 percent in FY2021 and 12.6 percent in FY2020 (Figure 47). Decreases in sector spending appear to be equally driven by reductions in both wage and non-wage expenses.¹⁹ Less than 0.5 percent of spending during FY2022 has been reported under the COVID-19 Economic Recovery Plan (CERP).²⁰ In the six months to March 2022, about 40 percent of spending was undertaken by SEEs, an increase from 33 percent in FY2021.

*Figure 46. Spending estimates
2019–2023 (% of GDP)*



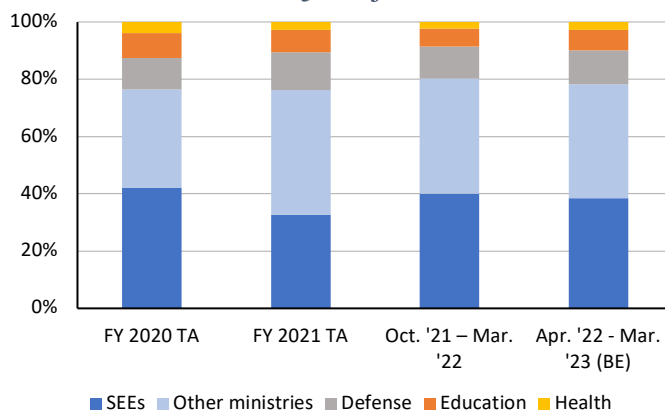
Source: MOPF; WB staff estimates.

Note: BE = Budget Estimate; Data for the period between October 2021 and March 2022 is annualized to enable historic comparison. Financial expenditure predominantly consists of repayment of loans (domestic and external).

¹⁹ For more information on sectoral spending see World Bank, “[Myanmar Budget Brief \(November 2022\)](#)”.

²⁰ The 2020 CERP committed to ambitious plans to mitigate the impacts of the COVID-19 pandemic while establishing foundations to support rapid economic recovery. It articulated 7 goals, 10 strategies, 36 action plans, and 78 actions, covering a broad range of extraordinary fiscal measures, combined with a set of human-focused and commonsense policy responses. The plan did not make budgetary commitments, the cost of CERP was estimated to be between MMK 2.9 and MMK 3.7 trillion (2.5 to 3.2 percent of GDP).

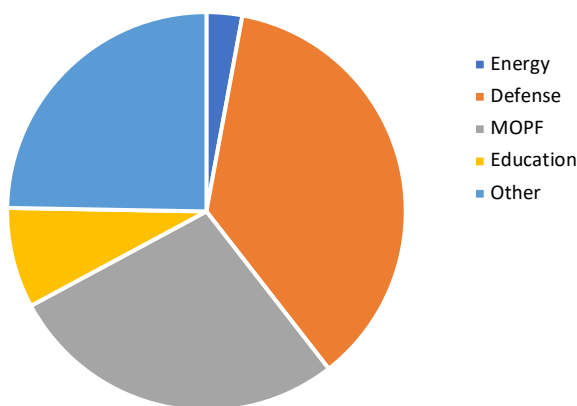
Figure 47. Expenditure by sector/ ministry (% of total)



Source: MOPF; WB staff estimates.
 Note: TA = Temporary Actual; BE = Budget Estimate

In-year budget changes prioritized defense spending. The authorities published the first supplementary budget in December 2022 for the year ended March 2023. This revised budget allocates additional expenditure which accounts to nearly 4 percent of the original budget for this period (which was approved in April 2022). This newly planned spending prioritizes defense expenditure, which accounts for about 37 percent of the total newly approved spending (Figure 48). These new allocations increase the overall defense budget for the period by 18 percent relative to FY2020. The supplementary budget also allocated resources to the Ministry of Planning and Finance (MoPF, 28 percent of the total), education (8 percent), energy (3 percent), and transfers to State and Region governments (Kachin, Rakhine, Yangon, Shan, and Ayeyarwaddy) (1.2 percent). Almost no additional resources were allocated to health.

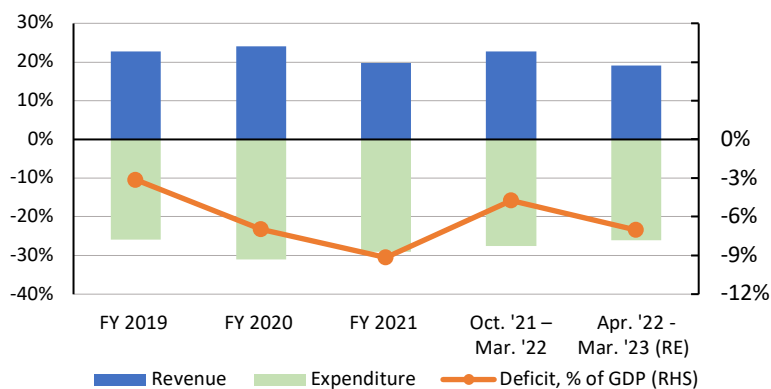
Figure 48. Supplementary budget April 2022 – March 2023 (% of new planned expenditure)



Source: MOPF

The fiscal deficit narrowed in the six months to March 2022 due to improved revenue performance and lower spending (Figure 49). In annualized terms, revenue increased to 22.7 percent of GDP from 19.8 percent in FY2021. During the same period, spending declined from 28.9 to 27.5 percent of GDP, resulting in a fiscal deficit of 4.7 percent of GDP, lower than the 6.9 percent of GDP projected by the authorities at the time of budget approval. The authorities’ budget projections for the year ended March 2023 indicate a deficit of around 7 percent of GDP.

Figure 49. Fiscal aggregates (% of GDP)

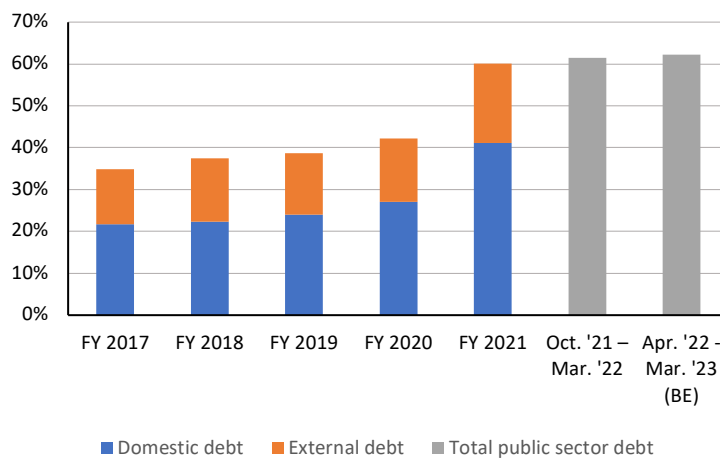


Source: MOPF; WB staff estimates.

Note: RE = Revised Estimate; Data for the period between October 2021 and March 2022 is annualized to enable historic comparison.

Public debt is estimated to have risen above 60 percent of GDP (Figure 51). The public debt to GDP ratio is estimated to have increased by more than 20 percentage points since FY2019, with relatively high fiscal deficits, a significant estimated contraction in GDP in FY2021, and exchange rate valuation effects all contributing to the rise.

*Figure 50. Public sector debt
2017–2023 (% of GDP)*



The use of CBM financing has increased, accompanied by a shift away from T-bills and T-bonds issuance. Since February 2021, the domestic securities market has become a less viable source of financing, and development assistance has declined. Quarterly sales of government securities²¹ have declined since 2020 (Figure 51). The volume of financing from domestic securities has decreased from around MMK 3,500 billion in FY2019 and FY2020 to less than MMK 2,500 billion in FY2021. This means government bonds now finance a much smaller share of the budget deficit – less than 30 percent between October 2021 and March 2022 (Figure 52).²² The authorities are instead relying on other sources of financing, primarily the CBM. According to the authorities’ projections for the 12 months to March 2023, 65 percent of public financing needs are expected to be met by the CBM, with the rest covered by the issuance of T-bills, T-bonds (16 percent) and external debt (19 percent). This marks a significant unwinding of previous efforts to reduce the share of government gross financing needs financed by the CBM, and has the potential to add to inflationary pressures.

²¹ These include the savings bonds, treasury bills and notes

²² Budget deficit does not amount to the gross financing needs, which also include amortization.

Figure 51. Quarterly government securities auction (MMK, billions)

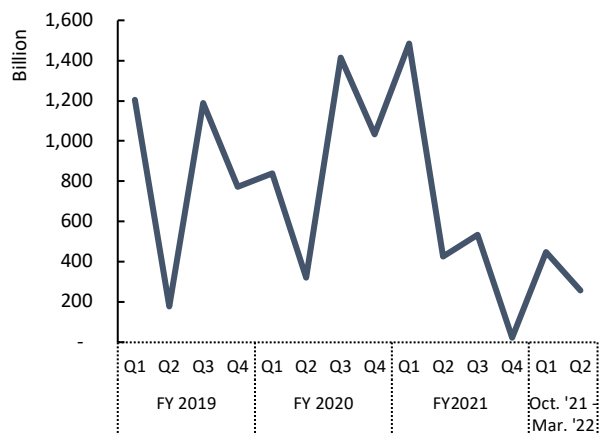
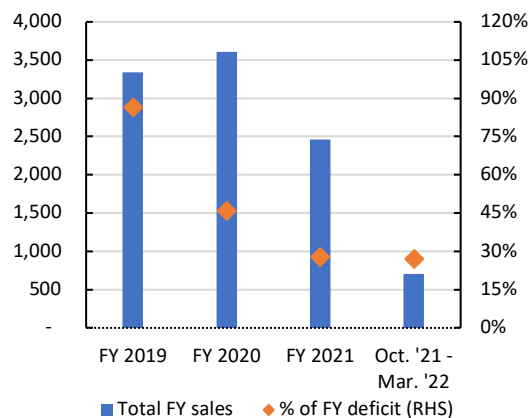


Figure 52. Government securities auction (Total FY sales and % of FY deficit)



Source: Central Statistical Organization; WB staff estimates.

Note: Budget deficit does not amount to gross financing needs, which also include amortization. Sales of government securities relative to the deficit are presented for illustrative purposes to highlight the broader shift away from T-bills and T-bonds issuance.

H. Livelihoods remain under severe pressure

The most recent survey data available indicate that household incomes remain under severe pressure.

In the third round of Myanmar Household Welfare surveys conducted by IFPRI, conducted during July – August 2022, 46 percent of households reported experiencing income losses compared to the previous year, while only 26 percent reported that their income increased.²³ Households earning incomes from casual wages and self-employment were more likely to report reduced incomes than those households benefitting from salaried employment. Income losses also varied across provinces. The largest share of households reporting income contractions over the past year were from Kayah (78.2 percent), Chin (56.9 percent) and Rakhine (50 percent). These regions also rank among the highest in terms of their headcount poverty rate. The observed patterns of income losses are therefore suggestive of continuing adversity among the poorest households and a rising trend in inequality. Reduced working hours and inadequate work are the main challenges experienced by salaried/wage workers, while agricultural producers and non-farm business owners reported high inflation as their main challenge.

Food and nutrition security in Myanmar also deteriorated in 2022. The proportion of households with a low food consumption score (a measure of dietary diversity and food frequency) increased from 9.4 percent at the beginning of the year to 17.2 percent in July-August 2022, with 4 percent of households facing moderate

²³ IFPRI Myanmar Strategy Support Program Working Paper 26, November 2022, “[Findings from the third round of the Myanmar Household Welfare Survey \(July and August 2022\)](#).”

to severe hunger. Insecurity in terms of low food consumption was highest in Kayah (27.5 percent), Chin (46.1 percent), and Magway (25.5 percent). While poor dietary diversity among households has been correlated with higher food prices, households engaged in agricultural production and receiving remittances are able to better cope with risks to food insecurity and dietary diversity.²⁴

Households' use of coping mechanisms reflects these income and food security pressures. In World Bank's surveys conducted in May 2022, 51 percent of households reported reducing non-food consumption, 42 percent reported reducing food consumption and 39 percent reported relying on their savings to cope with economic shocks. IFPRI's surveys conducted in July – August 2022 indicates that these coping mechanisms remain prevalent: about half of all households reported reducing food and non-food consumption while two-thirds of all households fell back on their savings to cope with distress. Rural households were more likely to use these coping mechanisms than urban households. Half of all agricultural households reduced agricultural input expenses, which is likely to affect yields.

Access to schooling improved compared with earlier in the year, but there remains significant regional variation. Over three quarters of children 5 to 14 years old attended school in July-August, up from just over half of children between April and June. But less than half of children in Kayah and Sagaing were enrolled.

²⁴ IFPRI Myanmar Strategy Support Program Working Paper, "[Findings from the third round of the Myanmar Household Welfare Survey \(December 2022\)](#)," 26, November 2022.

II. Outlook and Risks

GDP is projected to grow by 3 percent in the year ending September 2023 (Figure 53). The economic recovery from the shocks of COVID-19 and the military coup is expected to remain subdued in the near term, constrained by significant macroeconomic and regulatory uncertainty, persistent conflict, and ongoing electricity outages. The forecast implies that GDP per capita as of September 2023 would still be around 13 percent lower than in 2019 (Figure 54), indicative of the persistent impacts of recent shocks to both the supply and the demand side of the economy. The failure to return to pre-pandemic levels of activity sharply contrasts with the situation in the rest of the East Asia and Pacific region, where GDP in all large countries has already recovered to above 2019 levels (Figure 55).

Compared with FY2022, growth is expected to be more balanced across the different sectors. The baseline forecast for the year ended September 2023 assumes that conflict will remain elevated in the lead-up to planned elections and that export-oriented sectors face an easing of demand due to the projected slowdown in activity in major trading partners. Electricity supply is expected to remain erratic. The services sector is expected to grow by around 2 percent (off a very low base) as inflationary pressures ease, and domestic travel and transport continue to pick up. But with average household incomes and purchasing power remaining well below 2019 levels, domestic consumption will remain weak, and little improvement in international tourism is expected. After a stronger rebound in FY2022, industrial sector growth is expected to slow to about 4 percent, with garment manufacturers and food processors faced with slowing export demand and weak domestic demand respectively. Nevertheless, in the short run food and beverage manufacturers could potentially benefit from substitution to domestically produced products as import prices remain high and import restrictions remain in place. Industrial production will also be supported by a further rise in construction activity, and continued resilience in natural gas production and exports. In contrast to FY2021 and FY2022, the agriculture sector is also expected to grow in the year ended September 2023, reflecting recent signs of resilience in agricultural production, with pressure on key input prices likely to ease through 2023.

Figure 53: Real GDP growth and contributions to real growth by sector (percent, percentage points)

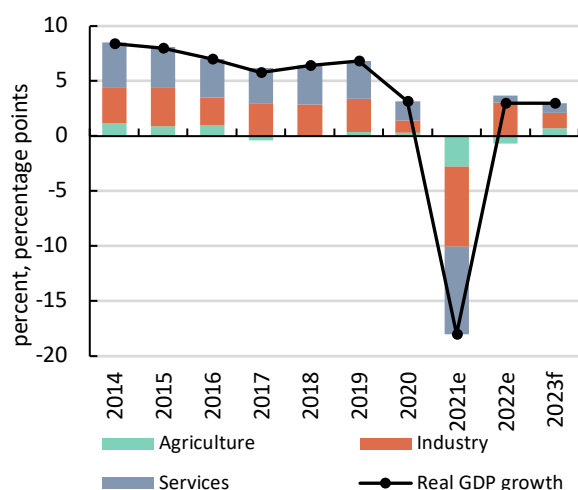
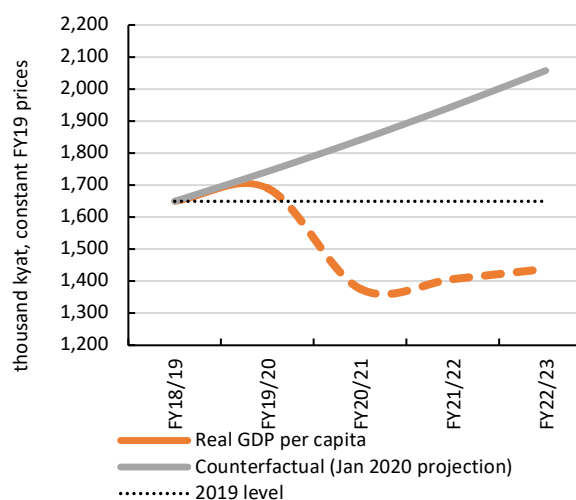
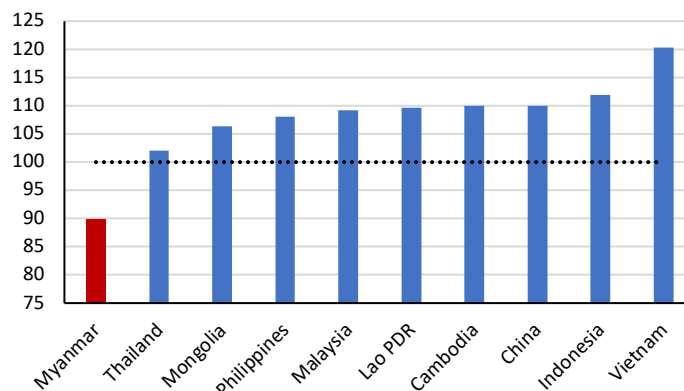


Figure 54: Real GDP per capita



Source: World Bank projections

Figure 55: Forecast real GDP level in 2023 (2019=100)



Source: Global Economic Prospects, January 2023
 Notes: Real GDP level in 2019 is indexed as 100.

Annual average inflation is expected to moderate to 7 percent in FY23, from 16.5 percent in FY22 (revised upwards from 15 percent in the July 2022 MEM) (Figure 56). Energy prices started to decline in the second half of 2022; assuming that the global Brent oil price stabilizes at around 90 USD/bbl over the next nine months (Figure 57), and that the parallel market exchange rate is stable at around Kyat 3,000/USD, average annual inflation for FY23 is expected to moderate to 7 percent from the 16.5 percent in FY22. On the other hand, a further depreciation in the kyat or a renewed pick up in global commodity prices would result in a commensurately higher rate of inflation.

Figure 56: Inflation forecast

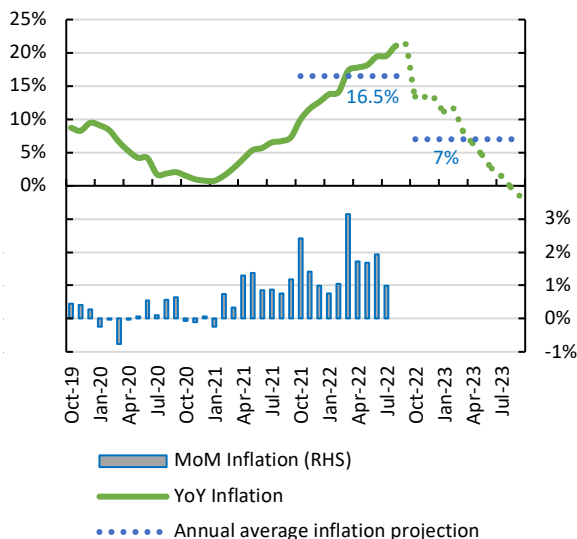
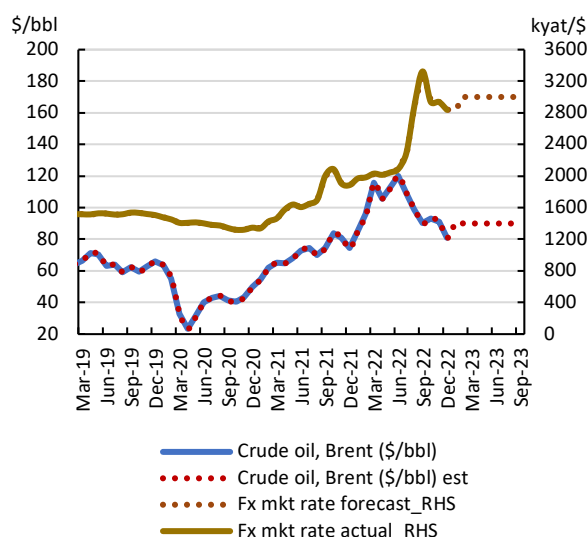


Figure 57: Global oil price and exchange rate assumptions



The current account deficit is expected to widen to 4.7 percent of GDP in FY2022/23. In the six months to December 2022, merchandise imports have increased by 27 percent compared with the same period of last year, while exports have increased by 14 percent. Through the remainder of the year to September 2023, growth in imports of intermediate goods and capital equipment is expected to continue, while growth in exports is likely to ease with the slowing global economy. Exports of tourism related services will provide little support to the current account this year. On the other hand, remittances are expected to increase given the recent change in regulation to allow remittances to be converted into kyat at close-to-market or market rates.

The fiscal deficit is projected to remain elevated in the twelve months to September 2023, with public debt to rise to above 62 percent of GDP. Accounting for the additional spending passed during the in-year supplementary FY2023 budget, the deficit for the year ended September is projected at over MMK 8.2 trillion or around 6.7 percent of estimated GDP (Table 1). Total gross financing requirements – that is, accounting for both the budget deficit and debt amortization – are expected to be around 8.3 percent of GDP. A greater reliance on CBM funding has resulted from the pausing or withdrawal of official sources of foreign finance as well as the lack of appetite from private banks for domestic debt issuance. Continued monetization of the deficit is likely to add to the medium-term pressure on inflation and the exchange rate.

Table 1: Economic data and projections for the year ended September 2023

	FY17/18	FY18/19	FY19/20	FY20/21e	FY21/22e	FY22/23f
Real GDP growth, at constant factor prices	6.4%	6.8%	3.2%	-18%	3%	3%
Agriculture	0.1%	1.6%	1.7%	-12.5%	-3.0%	3.0%
Industry	8.3%	8.4%	3.8%	-20.6%	8.6%	3.7%
Services	8.7%	8.4%	3.4%	-18.4%	1.6%	2.3%
Inflation (CPICPI), year average	5.9%	8.5%	5.8%	3.6%	16.5%	7%
Current Account Balance (% of GDP)	-4.7%	-0.2%	-2.0%	-1.4%	-3.3%	-4.7%
Fiscal Balance (% of GDP)	-2.9%	-3.1%	-7.0%	-9.2%	-4.7%	-6.7%
Public Sector Debt (% of GDP)	38.4%	37.0%	42.2%	60.0%	61.5%	62.3%

Note: To facilitate comparisons over time, the FY22/23 forecast relates to the period October 2022 to September 2023, which differs from the budget fiscal year (April to March). e = estimate; f = forecast.

Downside risks remain elevated. Conflict has the potential to worsen significantly in 2023 in the lead up to scheduled elections. The baseline forecast assumes a moderate increase in conflict this year (from already elevated levels) continuing to affect business confidence and strain logistics and supply chains. However, there is a risk that conflict escalates to levels which have a material impact on firms' ability or willingness to remain open and operate, which would lead to much weaker outcomes for economic activity. Outcomes for the global economy could also be worse than expected, not only because of escalations of geopolitical tensions which could impact both external demand and global commodity prices. On the upside, a stronger than expected recovery in China after the recent roll-back of COVID-19-related restrictions could provide some boost to bilateral trade and investment flows. Myanmar also remains vulnerable to other sources of risk, including a resurgence of COVID-19 or natural disaster, which would severely test the authorities' capacity to respond.

In the absence of such a shock, beyond 2023 the economy is likely to expand slowly at rates well below those observed in the years prior to the pandemic. Constraints to doing business – including higher prices, supply constraints (across a range of inputs), and trade and foreign exchange restrictions – remain severe. On

the other hand, over the past six months there have been some tentative signs of a rise in domestic investment, though FDI remains weak. Import substitution policies may be providing an impetus to domestic activity with previously imported goods (such as processed food products) now being domestically produced. More generally, some firms appear to be adapting to the new set of circumstances, particularly those that are either able to benefit from discretion in the enforcement of frequently changing regulations or find ways of circumventing these rules. But these adjustments are costly and inefficient, and imply a significant decline in productivity across the economy.

Myanmar's potential for inclusive growth over the medium and longer term has been curtailed. Growth is likely to suffer as resources are allocated to activities that are potentially unsuited to local factor endowments and away from more productive and competitive areas. The business environment is unlikely to improve materially while electricity shortages, logistics disruptions, trade and foreign exchange restrictions and regulatory uncertainty persist. Funding to critical health and education services is being curtailed and a lack of trust in the public provision of these services is in any case reducing their use. Lost months of education, together with rapid increases in unemployment and displacement, will reduce already low levels of human capital and productive capacity over the longer term. Migration is reportedly increasing through both formal and informal channels: while this is likely to benefit the migrants and those receiving remittances, it is also leading to increased reports of labor and skills shortages within the country.

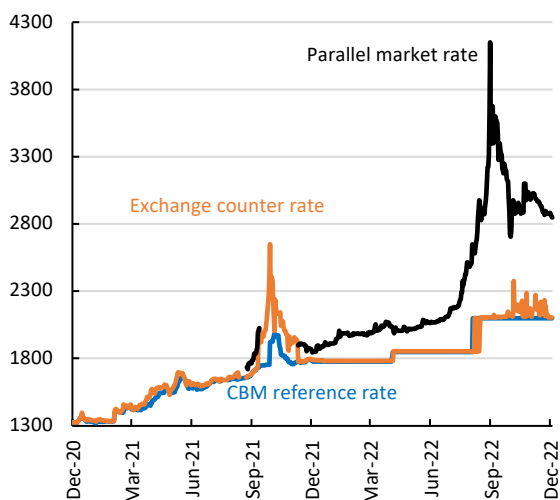
III. Recent exchange rate developments: A historical perspective

The past two years have seen substantial changes in exchange rate management in Myanmar, with a shift away from the previously managed float regime and toward reliance on administrative controls aimed at retaining foreign exchange within the economy. This special topic chapter analyzes recent changes in exchange rate policy and assesses the possibility and potential implications of a return to a unified exchange rate system.

A. Recent changes in exchange rate policy

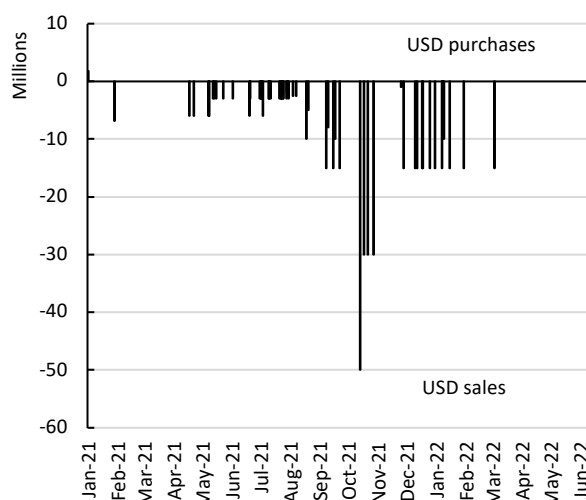
There has been a pronounced depreciation of Myanmar kyat over the past two years (Figure 58). As of end-December 2022, the official CBM kyat reference rate had depreciated by 37 percent against the USD since the end of 2020. A parallel exchange rate emerged in August 2021 after the imposition of restrictions on the official foreign exchange trading band, with the market value of the kyat more than 50 percent lower against the US dollar as at end-December 2022 compared with two years ago. Only a relatively small part of the kyat depreciation can be attributed to the general strengthening of the US dollar against other currencies: the US dollar index had appreciated by 15 percent over the two years to end-2022.

Figure 58: Myanmar kyat/USD



Source: The Central Bank of Myanmar; Money Exchangers

Figure 59: USD sales in FX auctions

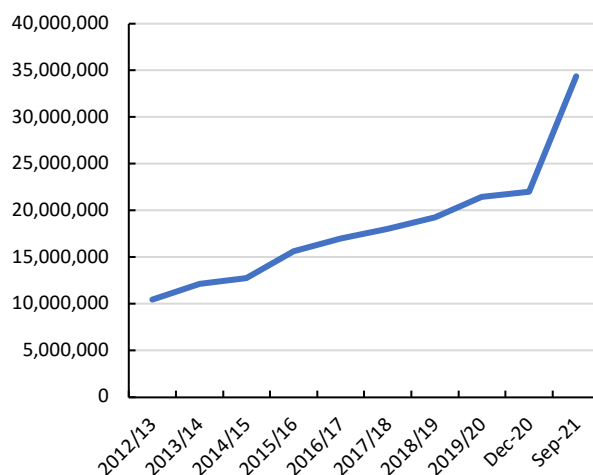


Source: The Central Bank of Myanmar

Monetary expansion may have contributed to the exchange rate depreciation. The latest publicly available data indicate that narrow money supply (M0) increased by 56 percent in the nine months between December 2020 and September 2021 and may have increased further since (Figure 60). Money creation

(primarily driven by the fiscal dominance of the central bank) has been one of the primary drivers of the depreciation of the kyat over the past several decades (Box 2).

Figure 60: Narrow Money Supply (M0), 2012-2021 (MMK. millions)



Source: Central Bank of Myanmar, Quarterly Financial Statistics Bulletin, 2021, Volume III, p.19

The CBM has abandoned the previous managed float exchange rate regime and fixed the official rate at an overvalued level. The reference rate has been effectively fixed at around 1780 kyat per USD with a tight exchange trading band of +/- 0.5 percent since November 2021. The CBM fixed the reference rate of 1,850 kyat per US dollar in April 2022 and adjusted it to 2,100 kyat per US dollar in August 2022. The CBM stopped intervening in the FX market through US dollar auctions to support the official exchange rate after March 2022 (Figure 59). The authorities have been instead imposing administrative measures which forced exporters to convert their FX earnings into kyat and reduce importers' access to FX.

The regulated official exchange rate has been misaligned, with a widening spread between official and parallel exchange rates. The official reference rate – which is only available to selected importers – is not reflective of the supply and demand for foreign currency, resulting in persistent shortages of US dollars and the emergence of a substantial gap between the parallel and reference rates. The spread between parallel and reference exchange rates widened dramatically, with parallel market kyat/US dollar exchange rates about half of the official exchange rate at the end of August 2022. Despite declining after August, the spread between parallel and reference rates is still significant and around 25 percent at end December 2022 (Figure 58).

Box 2: A longer-run perspective on Myanmar’s exchange rate

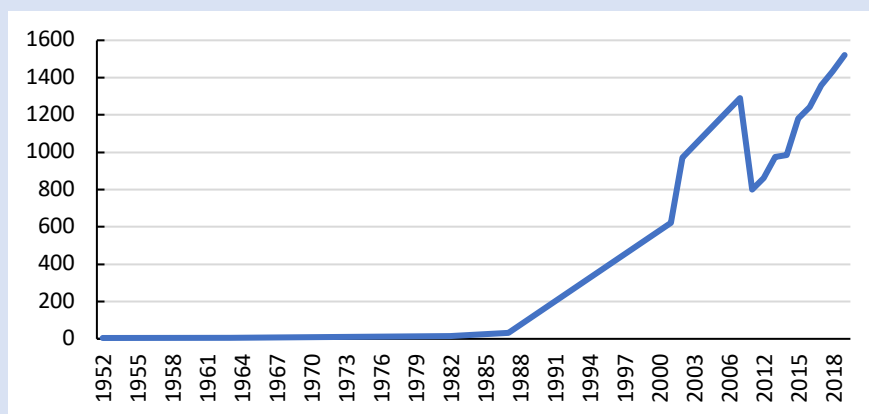
Myanmar has experienced depreciation of its currency for most of the last 60 years (see Figure B 1). In general, the weakening of the kyat over this period was driven by weak export performance – leading to substantial current account deficits – and substantial money creation. Since the mid-2000s, however, capital inflows have mitigated some of this downward pressure on the exchange rate.

Depreciation of the kyat parallel market exchange rate was significant during the 1960s and 1970s, losing around two-thirds of its value over these two decades.¹ Depreciation continued in the 1980s, halving in value between the early 1980s and 1987, and by 1987 1 USD traded for around 30 kyat in the parallel market, compared to the official rate of 1 USD = 6.7 kyat.¹ Factors behind exchange rate depreciation during the 1970s and 1980s included weak export performance and high domestic inflation arising from increased money supply via soft loans to SOEs.¹

Depreciation accelerated in the 1990s and much of the 2000s, with the parallel exchange rate peaking at around 1 USD = 1300 kyat in 2007,¹ equating to a loss of around 98 percent of its value over the two decades since 1987. The depreciation of the 1990s and early-to-mid 2000s occurred partly due to Myanmar's general failure to promote exports aside from a few basic primary products and large-scale central bank financing of budget deficits that caused high rates of domestic inflation (typically 20-40% per annum).¹

In the late 2000s and early 2010s the parallel exchange rate appreciated, rising from 1 USD = 1300 kyat in 2007 to around 1 USD = 800 kyat in 2011.¹ This appreciation of the exchange rate during this period was due to several reasons, including increased exports of natural gas, jade, and gems; a fire-sale of state-owned assets in 2010-11, which all had to be paid for in kyat; informal flows of capital attracted by high-interest rates on deposits and an expectation that MMK would continue appreciating. Increased informal flows of capital used to purchase real estate and rising remittances from Myanmar migrant workers¹ also contributed.

Figure B 1: Market-Determined Nominal USD-MMK Exchange Rate, 1950s-2010s



Sources: Diehl, Alexandra Diehl, *The Burma Currency Board* (Baltimore, 2017), p.8; “[The Burma Currency Board](#)” (Baltimore, 2017), p.8; 'Treasury Reporting Rates of Exchange as of March 31, 1963' report, available at: <https://www.govinfo.gov>; Hal Hill, 'Industrialization in Burma in Historical Perspective', p.146; Kubo, *Sources of Fluctuations in Parallel Exchange Rates and Policy Reform in Myanmar*, p.1; David Dapice and others, *The Myanmar Exchange Rate: A Barrier to National Strength*, p.5; World Bank dataset.

Note: This is the market-determined rate and from the 1960s until early 2012 it differs from the official rate. Between 1964 and 2011 we only have occasional data on the market-determined rate, taken from the sources mentioned above – we have these observations only for the years 1982, 1987, 2001, 2002, 2007, 2011. From May 2012 to Dec 2019 data is inputted yearly as the average of the monthly average in each month of that year, taken from World Bank data.

FX shortages at the overvalued official rate created economic inefficiencies. Since April 2022, importers' access to foreign exchange at the official rate has been rationed by the newly created Foreign Exchange Supervisory Committee (FESC). A few favored parties are allowed preferential access to foreign exchange, including importers of military supplies, fuel, and palm oil, but reportedly only 50-60 percent of their total import need is met – leaving the importers to return to relying on the informal channel with parallel foreign exchange rate. The authorities have applied different exchange rates for different purposes. For instance, the CBM offers a parallel market rate plus 30 kyat for sailors' remittance transfers, while it offers fuel and edible importers the reference rate. Foreign direct investment has been discouraged with a continued suspension of operations by international firms in part due to concerns about accessing FX and an expectation of a sharp depreciation in the future. Businesses that need imported inputs have been disrupted because of less reliable access to FX. Frequent changes in regulations and foreign currency restrictions have increased uncertainty and the burden of compliance.

Import restrictions combined with FX shortages reduced the availability of imports. Imports declined sharply after the coup in February 2021. Despite picking up from late 2021, imports have been much lower than in 2020, due to kyat depreciation, subdued domestic demand, limited access to US dollars at the overvalued official exchange rate, and import restrictions, including the institution of import trade license requirements and import bans and quotas. Imports have been further constrained in recent months, as importers have been required to use the parallel exchange rate to purchase FX and only importers of strategic items (after a long application process) are able to access the reference rate.

Surrender requirements reduced the competitiveness of exports. With several exemptions and amendments being issued, exporters are now required to convert 65 percent of their earnings into kyat within one business day at an unfavorable fixed exchange rate, with the remaining 35 percent must be converted into kyat if exporters do not use it within 30 days.²⁵ The requirements have acted as a tax on exporters (who were previously able to convert foreign exchange earnings at the market rate), squeezing margins even further given the rise in kyat-denominated costs facing most businesses. At end-December 2022, official and parallel market exchange rates, these surrender requirements are equivalent to an export tax of nearly 20 percent. This already appears to have impacted the price competitiveness of some exports.²⁶

There are several parallels between the multiple exchange rate system that emerged in 2021-2022 and Myanmar's exchange rate management in the 1990s and 2000s (Box 3). In both instances, the official exchange rate was overvalued, which led to foreign currency shortages and rationing at this rate (with implications for the availability of imports), reduced price competitiveness of (official) exports, and significant movement toward informal markets. Furthermore, depreciation continued on parallel markets despite efforts by the authorities to impose controls on foreign exchange flows and retain foreign currency within Myanmar. Several of the controls imposed today (such as the "export first" policy) have historical precedents.

²⁵ Companies with more than 35 percent of foreign ownership do not need to convert their foreign currency into kyat.

²⁶ World Bank. "[Myanmar Economic Monitor: Reforms Reversed](#)". July 2022.

Box 3: Exchange rate management in Myanmar through history

From the mid-1960s to 1988, there was a state monopoly on international trade. The official exchange rate was overvalued (the spread between the official and unofficial rates widened over this period and by 1987 had reached 350%) and export performance was weak. This led to large shortages and rationing of foreign currency, which in turn meant that many SOEs not being able to access the imported inputs they needed to carry out their production plans. Moreover, from the late 1970s until 1988 state entities that made a profit from exporting had to surrender half of the profits earned above a profit margin of 10-12%, with surrendered foreign exchange redistributed to other state agencies. Unofficial (*bmaung hkeo*) traders – whose trade may have exceeded official trade in the 1980s – bought and sold foreign exchange on unofficial markets, at a market-determined parallel rate. However, it should be noted that the rate paid for foreign currency on unofficial markets may have been inflated by this market being insulated from official exports.

International trade was liberalized and Myanmar opened up to foreign investment in the late 1980s and early 1990s, but the increasingly overvalued official exchange rate continued to create distortions. The highly overvalued official exchange rate created rent-seeking opportunities (for instance, on selling of fx and imports obtained at the official rate) for those able to access foreign currency at that rate, including certain SOEs, government departments, and military-owned companies. It also granted a high level of effective protection for those entities, privileging them over potential competitors. Nevertheless, there was not enough foreign currency to meet the needs of state entities, and SOEs frequently resorted to buying imported inputs from private Myanmar importers, and therefore implicitly paying the unofficial exchange rate. Exporters were not required to surrender any of their export earnings, and were *de facto* permitted to sell some or all their export earnings to other businesses and currency traders at the market rate.

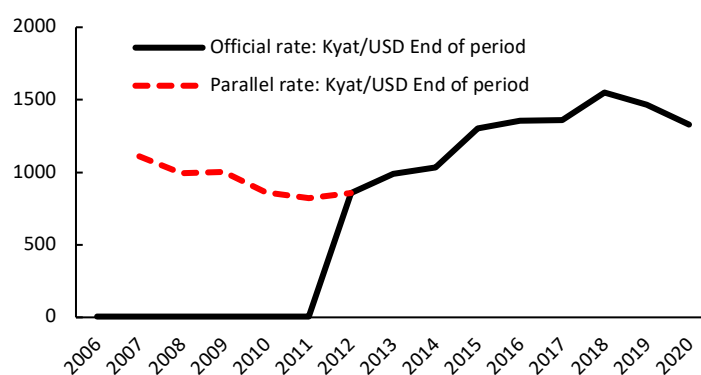
New foreign exchange restrictions introduced in the late 1990s and early 2000s created additional problems for sectors in which profit margins are low and international price competitiveness is particularly important – such as light manufacturing – perpetuating Myanmar’s dependence on natural resource exports. Between 1997 and early 2012, exporters were required to surrender 10 percent of their export earnings to the state as a proxy income tax. Importers also faced additional restrictions on accessing foreign exchange. In 1997, an ‘export-first’ policy was introduced, which required official importers to fund their imports via previously completed exports. In practice, large-scale unofficial importing of licit goods took place to bypass these restrictions. While this was tolerated to a considerable degree, importing unofficially did create costs and risks for businesses, and there were occasional crackdowns on foreign currency traders.

B. The potential for exchange rate unification

Previous experiences – in Myanmar and other countries – provide examples of potential gains from exchange rate reunification and how it might be achieved. Just over a decade ago in Myanmar, a substantial devaluation of the official exchange rate was allowed to unify official and parallel exchange rates. On April 1, 2012, the authorities replaced the official peg to the SDR with a managed float, which effectively unified the FX market at the parallel market rate (Figure 61). As a result, the official exchange rate was devalued from 5.6

kyat per USD in March 2012 to 824 kyat per USD in April 2012.²⁷ Pass-through to inflation was limited, largely because most of the economy already operated using the parallel exchange rate, except for a few entities with privileged access to the official rate.²⁸

Figure 61: Unification of official and parallel exchange rates in 2012



Source: CEIC data, IMF Article IV reports

The authorities implemented a range of supportive measures during exchange rate reunification that contributed to its success. First, the central bank was made an autonomous institution and no longer obliged to monetize deficits.²⁹ The authorities' efforts to consolidate the fiscal position and control central bank financing helped to support the exchange rate. Second, tightly regulated sectors in the economy were opened to foreign investment, including telecoms and manufacturing, and trade license requirements were removed. These reforms saw Myanmar reintegrate into international markets, with trade and foreign investment both increasing rapidly.

Examples from other countries also suggest that fiscal and monetary discipline is essential to support a unified market exchange rate. In Egypt, where the official and parallel exchange rates were successfully unified in late 2016, a three-year fiscal consolidation program was launched to decrease the persistently high fiscal deficits. Growth in central bank financing rapidly stabilized and turned negative in 2018. The policy rate was preemptively tightened before unification and continued to be tightened for more than a year afterward: even so, inflation continued to rise for almost a year after unification before it reversed course. On the other hand, in Sudan, the parallel exchange rate continued to depreciate after attempted unification in late 2018 due to the absence of fiscal reform and a continuation of high central bank financing. As a result, inflation continued to accelerate, rising from 68 percent in October 2018 to 230 percent in October 2020.

²⁷ According to “Official Rate: End of Period: National Currency per USD” in CEIC database.

²⁸ Gray, Simon. 2021. IMF working paper, February 2021.

²⁹ World Bank, “[Myanmar Economic Monitor: Progress Threatened; Resilience Tested](#)”. July 2021.

The unification of the exchange rate regime resolved problems caused by the multiple exchange rate system that had been in place previously. Importers had easy access to foreign exchange at the unified official rate, and there were no surrender requirements imposed on exporters. The liberalization ended foreign exchange shortages and rationing for both state entities and the private sector, helped to improve competition and reduce rent-seeking behavior; and contributed to the diversification and modernization of Myanmar's economy.

Combined other macroeconomic and structural reforms, exchange rate unification paved the way for Myanmar's economic revival during 2010s. Between 2011 and 2019, GDP grew by an average of 6.3 percent per year, putting Myanmar among the fastest-growing countries in the world over that period. While deficit financing continued, causing inflationary and depreciatory pressures, this was on a smaller scale than in the 1990s and 2000s. And although Myanmar ran a current account deficit in every year of the 2010s, this was primarily offset by official FDI inflows and to a lesser extent, foreign aid. This meant that while the exchange rate continued to lose value through much of this period, the depreciation was much slower than during the 1990s and early 2000s. Moreover, foreign exchange reserves trended upward after the reunification, from less than a month of imports in 2011/12 to almost four months in 2014/15. Myanmar began, for the first time, to export significant values of higher value-added goods and services (primarily garments and tourism), rather than only exporting primary commodities, as in earlier periods. Further, a large proportion of the imports driving the current account deficit were capital goods which helped Myanmar to increase its long-run productivity and modernize its economy.

Myanmar's history hence offers a cautionary tale about the distortions caused by poor exchange rate management, while also demonstrating the potential gains from unifying and liberalizing the exchange rate. Historical attempts to fix the official exchange rate at an overvalued level and rely on trade and foreign exchange restrictions to keep foreign currency within the country resulted in substantial economic costs. These included foreign exchange shortages and rationing, an increase in trade and financial transactions through less efficient unofficial channels, distortions in resource allocations (across and within industries), and greater potential for rent-seeking behavior. On the other hand, the liberalization and unification of Myanmar's exchange rate during 2012–19 helped to stabilize the economy and reduce market distortions. Together with other reforms, this helped drive a period of low inflation, increased trade and foreign investment, and strong economic growth. Lessons from Myanmar and other countries indicate that efforts to unify a multiple exchange rate regime are more likely to be successful if fiscal and monetary discipline is maintained to mitigate potential inflationary impacts and reduce the potential for further disruptive depreciation. At the same time, openness to trade and foreign investment flows allows the economy to realize the full benefits of a single market-determined exchange rate.

MYANMAR ECONOMIC MONITOR | JAN 2023

