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**Myanmar's Economic Future after the April 1 Elections** by Bradley O. Babson

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In recent months, there has been increasing attention to Myanmar's economic potential. There has also been growing recognition that shaping economic development so that it is broadly inclusive, based on sensible economic reforms, and supported by good macroeconomic management and institution-building, will be critical to a sustainable political reform and national reconciliation process.

The visits of political leaders and business delegations to Myanmar in recent months have fed a heightened expectation that after the April elections — assuming they are judged to be satisfactory in the eyes of domestic contenders and international community — there will be significant lifting of economic sanctions by the US and European Union. Lifting sanctions, even if partial, would most likely be accompanied by increased willingness of donors to provide official development assistance and readiness of private investors to ramp up foreign direct investment. In anticipation, the UN has announced it will organize a first donor's pledging conference, Japan has said it is ready to move ahead with new loans, and many private investors are already on the prowl.

Expectations of increased aid and investment flows may be well founded, but they are also overly optimistic. One risk is that any perceptions that the US or EU respond to the elections by moving the goal post of needed actions on the part of the government to justify lifting of sanctions, could boomerang on pro-reform elements of the government and empower hard-line elements, making progress on meaningful economic reforms even more difficult.

Moreover, because the absorptive capacity of the Myanmar civil service and private sector is still very weak and transparency poor, rapid infusion of funds without careful preparation could result in delays in projects or misuse of funds, leading to disappointment internally and externally.

Also, while the inflow of capital can boost the Myanmar economy, any delay in a robust and committed economic reform program will limit the impacts of investments and could have negative side effects.

One of the most important strategic issues for Myanmar is engineering a process of reforming while growing. Like Vietnam, Myanmar faces the prospect of attracting high levels of foreign aid and foreign direct investment at the same time, so the resources to sustain high economic growth rates are likely to be available. Getting the right sequence of economic reforms and investing in capacity building in the civil administration, legal system and financial system will also be key ingredients.

Much has been learned about best practices in country-led economic development, poverty alleviation and economic development in conflicted areas. Myanmar can start fresh in establishing economic development strategies, aid coordination mechanisms, and domestic policy priorities that will optimize its potential for economic growth, poverty reduction, and integration in the regional and global economy.

A key question for both the government and international community is whether Myanmar has the technocratic leadership and internal policy coordination and implementation organization to take full advantage of its strategic opportunity. Vested interests within the government and military could undermine the high-level policy coordination on economic reform and prioritization of investments that is needed.

Here are several metrics that will determine whether Myanmar is getting its economic policy house in order:

- *2012/2013 Budget.* The government's proposed budget includes a quadrupling of health and doubling of education spending. This is a positive signal, even though the base is very low and both sectors need substantial investment to rebuild Myanmar's badly depleted human capital. The share of military spending has been reduced to 14.9 percent of the budget from 23.6 percent last year, which is also on the surface a positive sign. The World Bank is planning a public expenditure review and this useful assessment can guide dialogue on budget priorities.
- *Exchange Rate Unification.* The IMF has been working with the government on the technical issues involved in unifying the exchange rate and reducing distortions in public accounting. This is critical for bringing transparency to the government budget and state enterprise reform.
- *Financial System Reforms.* The government seems committed to improving the financial system to support agriculture and private sector development. Progress in designing and implementing specific measures will be important for real change in the economy.
- *Large Infrastructure Projects.* Infrastructure investments, especially in transport and power supply, are important for Myanmar's economic growth. The selection of projects and their timing need to be scrutinized and integrated into an overall development strategy. There are also environmental and social impact issues that have been ignored. Two important indicators of responsible economic planning will be

the rationale for investments and assessment of environmental and social mitigation measures needed to make large projects domestically and internationally acceptable.

- *Privatization of State-Owned Enterprises.* The role of crony capitalists who have privileged access to state assets is potentially very sensitive. This could give the US and EU reason to hold onto some sanctions in force. As the country creates opportunities for private sector development, it will be necessary to level the playing field between state-owned enterprises and private companies, improve transparency, and put in place incentives for efficiency improvements in state-owned and private enterprises.

- *Military Role in the Economy.* The gorilla in the closet of Myanmar's economic future is control by the military over economic assets and lucrative foreign exchange earning companies. Also, military interests in extractive natural resource industries and large infrastructure projects in ethnic minority homeland areas, militates against the national reconciliation efforts and local control over local economic development. Coming to grips with the military's role in the economy is the most important bellwether of reform in Myanmar.

Finally, there are two aspects of US economic sanctions that are important to highlight:

- First, if the world is ready to move forward with aid, trade, and investment in Myanmar after the April 1 elections, retaining sanctions will mainly serve to deny opportunities for Myanmar companies that want to forge business and social relations with the US. Retaining sanctions will also put US companies in a competitive disadvantage. A trade agreement with Myanmar that addresses the role of the military in the economy, the quality of foreign investment in job creation, and deepening domestic value-added, while expanding bilateral economic relations, is worth exploring.

- Second, financial sanctions that forbid transactions using US banks are likely to have distorting effects on Myanmar's economic development. If there is a significant ramping up of aid, trade, and investment with the international community generally, US banks should be able to play their normal role and reduce risk of over-reliance on less transparent mechanisms for financial flows in and out of the country.

Myanmar's economic future after the April 1 elections is potentially rosy but there could be continuing divisiveness and a growing wealth gap between those with privileged military connections and the largely rural agrarian population. The US and the international community need to pay attention to the dynamics of economic change in Myanmar and its impact on political development and the national reconciliation process. How the US handles the removal of sanctions and shaping its economic relationship can make a difference. This should be a central part of the diplomatic agenda going forward.

*PacNet commentaries and responses represent the views of the respective authors. Alternative viewpoints are always welcomed.*

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