INTERNATIONAL MONETARY FUND

MYANMAR

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATIONS—DEBT SUSTAINABILITY ANALYSIS

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Myanmar is assessed to remain at low risk of debt distress.[1][2][3] *Under the baseline scenario, public and publicly guaranteed (PPG) external debt burden indicators remain well below their indicative thresholds. Similarly, total public debt will also remain below the benchmark, even as it will rise over the long term. While Myanmar's risk of debt distress is characterized as low, it requires close monitoring, in particular because there is potential for both domestic and external downside risks to materialize that may adversely affect the level of debt. On the domestic front these risks include fiscal slippages from the authorities' current target of below 5 percent of GDP and lower growth. On the external side, shocks include further declines in gas prices and depreciation of the kyat. While these shocks do not lead to breaches of the indicative thresholds or benchmarks in the medium term,*[4] *keeping a low risk of debt distress will require prudent fiscal policy, sound public financial management and increasing use of concessional finance while limiting nonconcessional borrowing to viable and growth-enhancing projects.*

[1] External public and publicly guaranteed (PPG) debt and public domestic debt dynamics are assessed using the LIC DSA framework, which recognizes that better policies and institutions allow countries to manage higher levels of debt, and thus the threshold levels are policy-dependent. The quality of a country's policies and institutions are normally measured by the World Bank's Country Policy and Institutional Assessment (CPIA). The most conservative thresholds are applied for the purposes of this DSA based on the average CPIA index of the last two years which indicate a weak rating.

[2] The DSA was jointly prepared by the IMF and the World Bank.

[3] This risk rating is unchanged from the previous DSA which had incorporated the resolution of the external arrears with the Paris Club, the World Bank and the Asian Development Bank.

[4] These are standard shock scenarios in the DSA template.

BACKGROUND

1. **The external and public debt sustainability analyses are based on the standard LIC DSA framework**. The DSA framework presents the projected path of Myanmar's external and public sector debt burden indicators, and draws conclusions on the sustainability of debt.

2. **The underlying macroeconomic assumptions remain broadly unchanged compared with the last DSA but updates have been made taking into account several changes in both the external and domestic environment since the last Article IV consultation.** Main changes in the estimates and projections are below:

- In 2014/15, the real GDP growth was 8.5 percent reflecting robust investment in productive sectors including manufacturing and services, particularly in telecommunications. It is expected that the average medium-term GDP growth rate will remain strong at 8.1 percent as production in the special export zones also picks up. Accordingly, growth has been revised slightly upward over the longer term, taking into account that many of these new investment projects could help raise long-term growth.[5][6]

- Inflation in 2014/15 increased to over 7.5 percent (end of period) and is projected to be higher in the medium term compared to the last DSA mainly due to expected kyat depreciation and higher inflationary expectations. However, it will converge back to the almost the same long-term trend as in the previous DSA.

- In 2014/15, the fiscal deficit was 2.9 percent of GDP, benefiting from considerable windfall gains from telecommunications and oil and gas licenses (which will be spread over a few years). In the medium term, the fiscal deficit is expected to increase to 4.5 percent of GDP due to structural increases in expenditure, including in the public sector wage bill. Revenues, however, have been revised downward both in the medium and long-term due to lower projected State-owned Economic Enterprises' (SEEs) revenues. As a result, the fiscal deficit is projected to rise to 4.2 percent of GDP in the long-term.

- The current account deficit widened in 2014/15, driven primarily by an increase in import demand. Given the downward revision in gas prices (expected to be 20 percent lower in 2015/16 compared with 2014/15), it is expected that the current account deficit will widen significantly in the medium-term compared to the last DSA.

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[5] The staff of the World Bank and the IMF, while strong supporters of the overall reform effort, reserve some caution given the newness of the reform program. In addition, there are possible downside risks stemming from the international environment.

[6] The long-term growth projections were also underpinned by growth diagnostics conducted by IMF staff f in 2014/15 DSA which based projections on age-specific population growth and sectoral level productivity based on the experience of similar countries. The final results were based on consultation with the World Bank.

Key Macroeconomic Assumptions Underlying the DSA for the Baseline Scenario (FY2015/16-35/36)				
	Current DSA		Previous DSA	
	Medium Term	Long Term	Medium Term	Long Term
	2015/16-2020/21	2021/22-2035/36	2014/15-2019/20	2020/21-2034/35
Real GDP Growth (in percent)	8.1	6.8	8.1	6.6
Inflation (in percent)	9.1	4.7	6.3	4.0
Overall fiscal balance (in percent of GDP)	-4.5	-4.2	-4.6	-3.8
Noninterest current account (in percent of GDP)	-7.3	-4.4	-4.7	-3.3
Revenue (nonfinancial public sector; in percent of GDP)	21.3	23.8	24	25
Source: IMF staff estimates				

3. As in the previous DSA, this analysis incorporates the resolution of Myanmar's arrears with its multilateral and bilateral creditors completed in 2013/14. In late-January 2013, the Paris Club reached an agreement with the Myanmar authorities on a debt treatment to be completed in early 2014. Paris Club members agreed to write off 50 percent of all arrears and reschedule the remaining arrears over 15 years with a 7-year grace period. The treatment was phased, with 25 percent of the write-off occurring immediately and 75 percent on the successful completion of a staff-monitored program with the IMF. Furthermore, Myanmar resolved its arrears to the World Bank and the Asian Development Bank in January 2013, with the help of bridge financing from Japan.

4. Myanmar is also expected to gradually reduce its reliance on external nonconcessional financing over the medium term, as assumed in the previous DSA. With the resolution of its arrears and the re-engagement with traditional donors, Myanmar is expected to gradually regain access to concessional resources. In particular, after the resolution of arrears with its multilateral creditors (the World Bank and the Asian development Bank), Myanmar has begun to receive concessional financing from these two institutions. Myanmar's current largest bilateral creditors are Japan and China. It is expected that as the Paris Club donors re-engage with Myanmar, and gradually identify suitable projects, the share of nonconcessional financing will decline over the medium term. The average new disbursements from the non-Paris Club members in the past few years were around 90 percent of total disbursements. We assume that this number will decrease by more than 50 percent in the medium-term, but it will gradually increase over the long-term as Myanmar becomes more developed and will be able to access financial markets.

DEBT SUSTAINABILITY ANALYSIS

5. Recent developments have kept the stock of external debt at relatively low levels.

- The resolution of the arrears in 2013/14 after the successful completion of the Staff Monitored Program had helped reduce the external debt stock (this was also incorporated in the last DSA);
- Furthermore, the valuation effect of recent exchange rate changes has resulted in a reduction of the stock of external debt at end 2014/15.[7]
- Finally, there has been only modest external borrowing in 2014/15.

[7] The kyat (reference rate) appreciated against a basket of currencies in which Myanmar's external debt is denominated.

6. Debt sustainability analysis shows that public and publically guaranteed external debt will remain well below the indicative thresholds throughout the project period. Several of the standard stress tests reflect downside risks currently faced by Myanmar. In particular, these include a reduction in the value of exports (in Myanmar this may be caused by a further drop in gas price), and a depreciation of the exchange rate. Although the standard stress tests indicate that no thresholds will be breached,[8] there can be an increase in debt service (for example, a one-time depreciation increases the debt service to revenue ratio in Figure f in the Panel Chart 1a). It will, therefore, be important to exercise prudence in external borrowing in a volatile international environment where exchange rate changes can have a large impact –either positive or negative – on the debt burden. Furthermore, continued strong performance of the external sector is critical, including by maintaining high export growth in manufacturing and agriculture, in addition to gas, attracting FDI to fund investment projects and obtaining more concessional financing.

7. Total public sector debt will also remain below the indicative benchmark under the baseline scenario but is vulnerable to shocks. The present value of total public debt as a percentage of GDP remains below the indicative benchmark throughout the projection period but it continues to rise over the long-term. This trajectory reflects the significant development needs of Myanmar and the associated overall fiscal deficits assumed in the baseline scenario. This level of debt can give rise to vulnerabilities including a high debt service burden. Overall, the standard stress tests show that public debt sustainability is vulnerable to lower real GDP growth and fiscal slippages.[9] Risks are somewhat mitigated as the authorities aim to use their borrowing to only finance economically viable projects in priority sectors. The authorities plan to keep the fiscal deficit below 5 percent of GDP in the medium term. Based on DSA simulations, however, staff advised the authorities to lower the deficit target to 4½ percent, which would help keep public debt below the indicative benchmark in the long run. The authorities' 5 percent target could lead to a breach of the benchmark in the long run.

8. Myanmar will need to maintain fiscal discipline to ensure debt sustainability. Public finances are dependent on natural resource revenues. Tax revenues are very low and the tax base remains narrow, in part due to widespread exemptions. In addition, transfers to sub-national governments without devolving spending responsibilities will increase the overall public sector deficit. It is expected that in 2015/16, the balance of the aggregate SEEs will turn negative underscoring the need to implement reforms that increase SEEs efficiency. Furthermore, only prudent borrowing by the policy banks[10] should be allowed as guarantees for the policy banks could pose risks to debt control and complicate fiscal management. It is imperative to improve the collection of statistics on these institutions.

9. Fiscal risks can be mitigated by taking several steps, some of which are already under consideration by the authorities. Higher revenue is needed to provide a solid foundation for financing development. To this end, introducing a value added tax (VAT) and reducing tax incentives are key steps. Fiscal decentralization and reforms of SEEs finances need to be carefully planned and implemented to

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[8] The typical historical scenario is not shown in this analysis. In the case of Myanmar, the historical scenario would imply an unlikely return to pre-reform policies: low noninterest current account deficits (consistent with binding international sanctions) and sustained real exchange rate pressures.

[9] In the present value of total public debt to GDP ratio, the most extreme shock is the growth shock which causes a breach in the indicative benchmark in 2023/34 while fixing the primary balance causes a breach in 2033/34.

[10] Policy banks in Myanmar are financial institutions in which the government has an ownership stake and which carry. out functions that are associated with policies of the government.

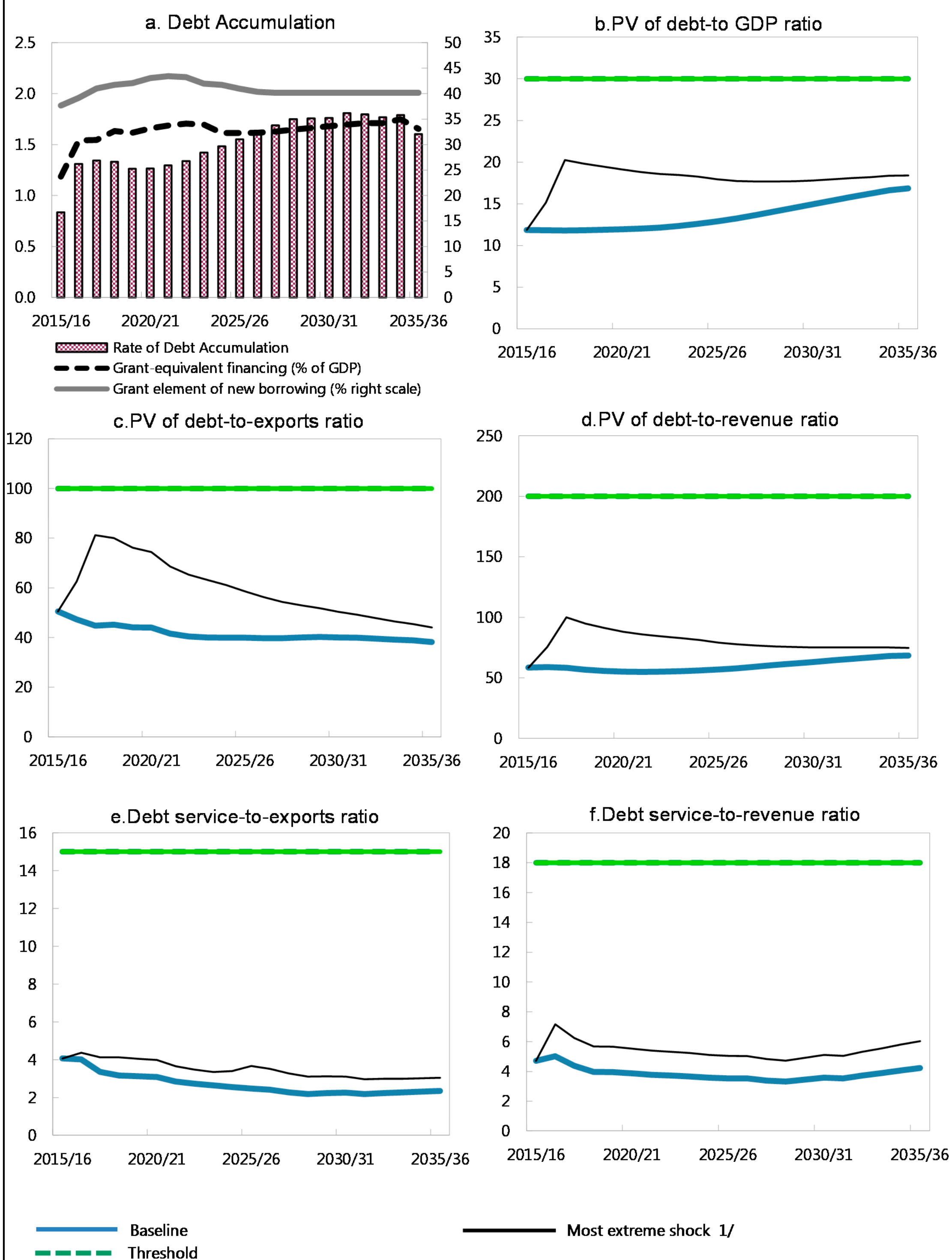
safeguard fiscal sustainability. Proper use of windfall revenues—such as those from oil and gas exploration—can also help strong the fiscal position, especially in the context of a medium-term fiscal framework.

STAFF ASSESSMENT

10. Myanmar is assessed to be at low risk of debt distress, but prudent macroeconomic policies and sound debt management will be required to keep debt sustainable. Under the baseline scenario, all indicators for the external debt are below their indicative thresholds and standard stress tests show that shocks will not cause breaches although shocks such as a one-time depreciation can cause debt service (expressed as a ratio of revenue) to increase. Under the baseline scenario, the total public debt also remains below the benchmark although it rises throughout the projection period and is vulnerable to fiscal slippages and low real GDP growth. Preventing total public debt vulnerability from increasing will require prudent fiscal policy, improvements in revenue performance and public financial management, limiting contingent liabilities by improving the performance of SEEs as well as prudent borrowing by policy banks, and increasing use of concessional finance.

11. The authorities broadly agreed with these conclusions and with the thrust of the analysis. They concurred with staff on the need to be cautious on nonconcessional borrowing and reconfirmed their intention to use nonconcessional external borrowing only to finance economically viable projects in priority sectors, at levels consistent with low risk of debt distress. In order to limit the use of nonconcessional financing, the authorities reiterated their aim to keep the fiscal deficit below 5 percent of GDP over the medium term.

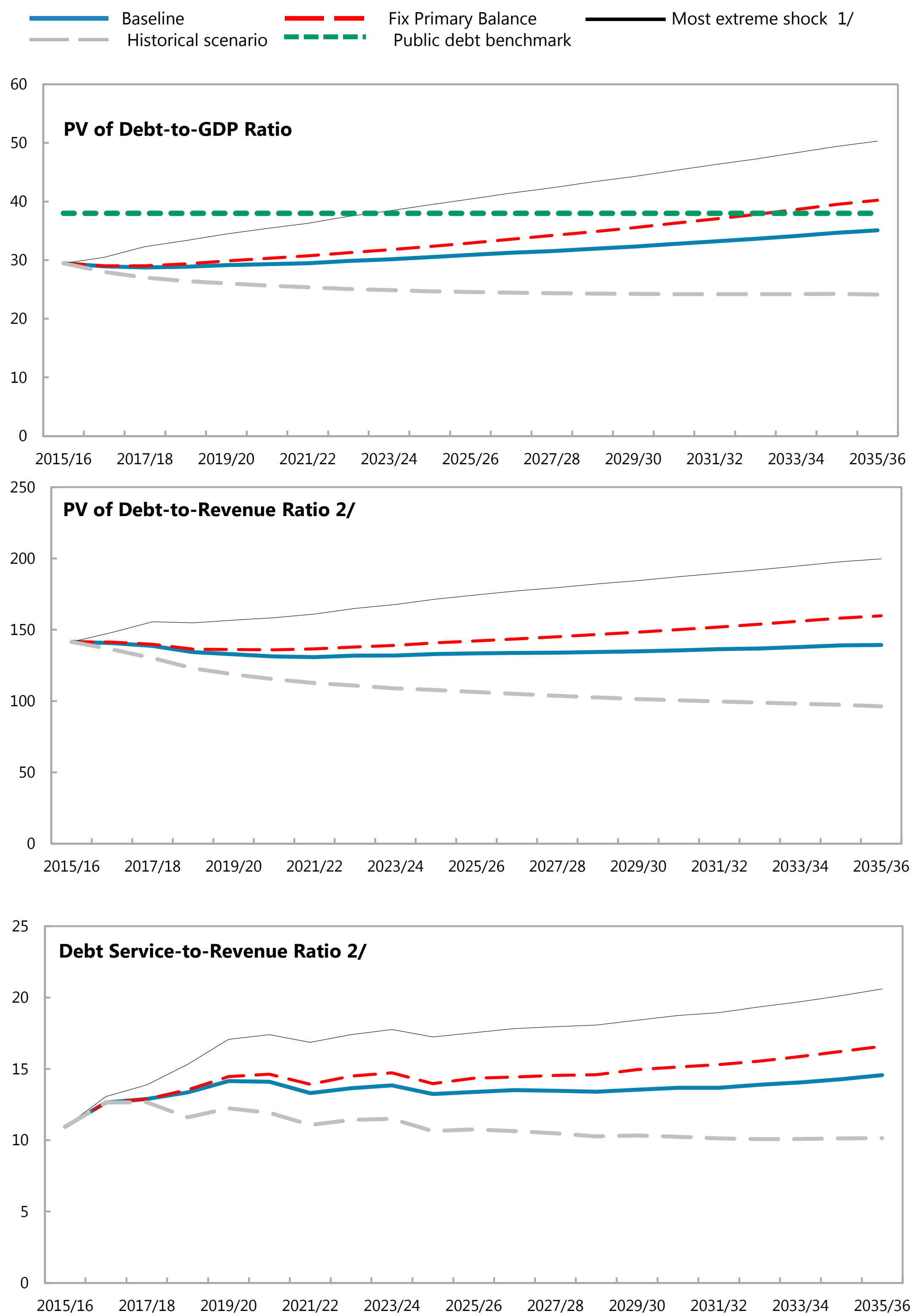
Figure 1a. Myanmar: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2015/16-2035/36 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025. In figure b. it corresponds to a Combination shock; in c. to a Combination shock; in d. to a Combination shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Figure 1b.Myanmar: Indicators of Public Debt Under Alternative Scenarios, 2015/16-2035/36 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025.
In all three figures above, the most extreme shock is the growth shock.

2/ Revenues are defined inclusive of grants.

Table 1a .Myanmar: External Debt Sustainability Framework, Baseline Scenario, 2012/13-2035/36 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical [6/]	Standard [6/]	Projections									
	2012/13	2013/14	2014/15	Average	Deviation	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2015/16-2020/21 Average	2025/26	2035/36	2021/22-2035/36 Average
External debt (nominal) 1/	**25.3**	**18.0**	**14.4**			**15.8**	**16.3**	**16.6**	**17.0**	**17.4**	**17.8**		**20.0**	**25.5**	
of which: public and publicly guaranteed (PPG)	25.3	18.0	14.4			15.8	16.3	16.6	17.0	17.4	17.8		20.0	25.5	
Change in external debt	-1.5	-7.3	-3.6			1.4	0.4	0.4	0.4	0.4	0.4		0.5	0.3	
Identified net debt-creating flows	-0.7	0.1	-1.0			2.3	0.6	-0.5	-0.7	-1.1	-1.3		-2.7	-1.9	
Non-interest current account deficit	**4.0**	**4.8**	**5.7**	**0.5**	**4.7**	**8.6**	**7.9**	**7.4**	**7.2**	**6.7**	**6.4**		**4.6**	**4.1**	4.4
Deficit in balance of goods and services	3.9	4.8	6.7			10.1	9.7	8.8	9.0	8.6	8.4		6.4	6.0	
Exports	20.8	22.6	24.2			23.5	25.0	26.3	26.2	27.0	27.2		32.4	44.2	
Imports	24.7	27.4	30.9			33.6	34.7	35.1	35.2	35.7	35.6		38.8	50.2	
Net current transfers (negative = inflow)	-1.0	-1.6	-2.6	-1.1	0.6	-2.8	-2.9	-2.9	-3.0	-2.9	-2.9		-2.6	-2.4	-2.6
of which: official	-0.1	-0.4	-0.5			-0.5	-0.5	-0.5	-0.6	-0.6	-0.6		-0.5	-0.5	
Other current account flows (negative = net inflow)	1.1	1.6	1.7			1.3	1.2	1.5	1.1	1.0	0.9		0.8	0.6	
Net FDI (negative = inflow)	**-5.0**	**-4.6**	**-5.2**	**-3.6**	**1.2**	**-5.5**	**-6.5**	**-6.9**	**-7.0**	**-6.9**	**-6.8**		**-6.3**	**-5.0**	-5.7
Endogenous debt dynamics 2/	**0.4**	**-0.1**	**-1.5**			**-0.8**	**-0.9**	**-0.9**	**-0.9**	**-0.9**	**-0.9**		**-1.0**	**-1.0**	
Contribution from nominal interest rate	0.2	0.4	0.4			0.4	0.4	0.3	0.3	0.3	0.3		0.3	0.3	
Contribution from real GDP growth	-2.0	-2.1	-1.4			-1.2	-1.2	-1.2	-1.2	-1.2	-1.2		-1.3	-1.3	
Contribution from price and exchange rate changes	2.2	1.6	-0.5			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-0.8**	**-7.4**	**-2.6**			**-0.9**	**-0.2**	**0.8**	**1.1**	**1.4**	**1.7**		**3.2**	**2.2**	
of which: exceptional financing	-10.9	-8.5	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	11.0			11.9	11.8	11.8	11.8	11.9	12.0		12.9	16.9	
In percent of exports	...	...	45.4			50.5	47.3	44.8	45.2	44.1	44.0		39.9	38.1	
PV of PPG external debt	**...**	**...**	**11.0**			**11.9**	**11.8**	**11.8**	**11.8**	**11.9**	**12.0**		**12.9**	**16.9**	
In percent of exports	**...**	**...**	**45.4**			**50.5**	**47.3**	**44.8**	**45.2**	**44.1**	**44.0**		**39.9**	**38.1**	
In percent of government revenues	**...**	**...**	**42.5**			**58.4**	**59.0**	**58.2**	**56.7**	**55.7**	**55.1**		**56.9**	**68.4**	
Debt service-to-exports ratio (in percent)	**2.2**	**3.3**	**2.9**			**4.1**	**4.0**	**3.4**	**3.2**	**3.1**	**3.1**		**2.5**	**2.4**	
PPG debt service-to-exports ratio (in percent)	**2.2**	**3.3**	**2.9**			**4.1**	**4.0**	**3.4**	**3.2**	**3.1**	**3.1**		**2.5**	**2.4**	
PPG debt service-to-revenue ratio (in percent)	**2.0**	**3.3**	**2.7**			**4.7**	**5.0**	**4.4**	**4.0**	**4.0**	**3.9**		**3.5**	**4.2**	
Total gross financing need (Billions of U.S. dollars)	-0.2	0.7	0.8			2.7	1.8	1.1	0.9	0.7	0.5		-1.4	0.7	
Non-interest current account deficit that stabilizes debt ratio	5.5	12.1	9.3			7.1	7.5	7.0	6.7	6.3	6.0		4.1	3.8	
Key macroeconomic assumptions															
Real GDP growth (in percent)	7.3	8.4	8.5	8.3	3.5	8.5	8.4	8.3	8.0	7.7	7.7	8.1	7.2	5.7	6.8
GDP deflator in US dollar terms (change in percent)	-7.5	-6.0	2.7	9.9	15.8	-4.0	0.0	2.4	2.5	2.4	2.3	0.9	2.3	2.3	2.3
Effective interest rate (percent) 5/	0.6	1.6	2.2	1.9	0.9	2.6	2.5	2.3	2.1	2.0	1.9	2.2	1.5	1.4	1.5
Growth of exports of G&S (US dollar terms, in percent)	4.9	10.8	19.4	17.6	11.5	1.1	15.2	16.9	10.1	13.6	10.8	11.3	12.6	11.7	12.9
Growth of imports of G&S (US dollar terms, in percent)	17.4	13.0	25.6	24.5	20.6	13.4	11.8	12.3	11.1	11.5	9.9	11.7	12.2	11.4	11.8
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	37.6	39.1	41.0	41.7	42.0	43.0	40.8	41.0	40.2	40.9
Government revenues (excluding grants, in percent of GDP)	23.3	23.1	25.9			20.3	20.1	20.3	20.9	21.4	21.7		22.7	24.7	23.3
Aid flows (in Billions of US dollars) 7/	0.3	0.3	0.6			0.7	1.1	1.4	1.7	1.9	2.2		2.9	6.6	
of which: Grants	0.0	0.2	0.3			0.3	0.4	0.4	0.5	0.6	0.6		0.9	2.0	
of which: Concessional loans	0.3	0.2	0.2			0.4	0.7	1.0	1.2	1.3	1.6		2.1	4.5	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			1.2	1.5	1.5	1.6	1.6	1.7		1.6	1.7	1.7
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			51.1	48.8	50.7	53.1	53.6	54.2		50.2	49.0	50.1
Memorandum items:															
Nominal GDP (Billions of US dollars)	55.6	56.7	63.1			65.8	71.3	79.0	87.5	96.4	106.2		170.9	400.4	
Nominal dollar GDP growth	-0.7	2.0	11.4			4.2	8.4	10.9	10.7	10.2	10.2	9.1	9.7	8.2	9.3
PV of PPG external debt (in Billions of US dollars)			6.7			7.3	8.1	9.1	10.1	11.2	12.5		21.7	67.1	
(PVt-PVt-1)/GDPt-1 (in percent)						0.8	1.3	1.3	1.3	1.3	1.3	1.2	1.6	1.6	1.6
Gross workers' remittances (Billions of US dollars)	0.5	0.7	1.3			1.5	1.7	1.9	2.1	2.3	2.4		3.6	7.7	
PV of PPG external debt (in percent of GDP + remittances)	...	...	10.8			11.6	11.5	11.5	11.6	11.6	11.7		12.6	16.5	
PV of PPG external debt (in percent of exports + remittances)	...	...	41.8			46.0	43.1	41.0	41.4	40.6	40.6		37.5	36.5	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.7			3.7	3.7	3.1	2.9	2.9	2.9		2.3	2.3	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 1b. Myanmar: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2015/16-2035/36

(In percent)

	Projections							
	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	**2025/26**	2035/36
PV of debt-to GDP ratio								
Baseline	12	12	12	12	12	12	**13**	17
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	12	8	6	4	2	1	**1**	1
A2. New public sector loans on less favorable terms in 2015-2035 2	12	12	13	13	14	14	**18**	25
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	12	12	12	12	12	13	**14**	18
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	12	13	15	15	15	15	**15**	17
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	12	12	13	13	13	14	**15**	19
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	12	15	19	19	19	18	**17**	18
B5. Combination of B1-B4 using one-half standard deviation shocks	12	15	20	20	19	19	**18**	18
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	12	16	16	17	17	17	**18**	24
PV of debt-to-exports ratio								
Baseline	50	47	45	45	44	44	**40**	38
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	50	32	21	14	8	4	**2**	2
A2. New public sector loans on less favorable terms in 2015-2035 2	50	48	48	51	51	53	**54**	58
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	50	46	44	44	43	43	**39**	38
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	50	55	69	69	66	65	**55**	47
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	50	46	44	44	43	43	**39**	38
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	50	61	73	72	69	67	**53**	41
B5. Combination of B1-B4 using one-half standard deviation shocks	50	63	81	80	76	74	**59**	44
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	50	46	44	44	43	43	**39**	38
PV of debt-to-revenue ratio								
Baseline	58	59	58	57	56	55	**57**	68
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	58	40	28	18	11	5	**4**	4
A2. New public sector loans on less favorable terms in 2015-2035 2	58	60	63	64	65	66	**78**	103
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	58	59	61	59	58	58	**60**	73
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	58	63	75	72	70	68	**66**	70
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	58	60	65	64	63	62	**65**	79
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	58	76	95	91	87	84	**76**	73
B5. Combination of B1-B4 using one-half standard deviation shocks	58	76	100	95	91	88	**79**	75
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	58	81	81	79	78	77	**80**	97

Table 1b. Myanmar: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2015/16-2035/36 (concluded)

				Debt service-to-exports ratio				
Baseline	4	4	3	3	3	3	**2**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	4	4	3	2	2	2	**1**	0
A2. New public sector loans on less favorable terms in 2015-2035 2	4	4	3	3	3	4	**3**	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	4	4	3	3	3	3	**2**	2
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	4	4	4	4	4	4	**4**	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	4	4	3	3	3	3	**2**	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	4	4	4	4	4	4	**4**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	4	4	4	4	4	4	**4**	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	4	4	3	3	3	3	**2**	2
				Debt service-to-revenue ratio				
Baseline	5	5	4	4	4	4	**4**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	5	5	3	3	2	2	**1**	0
A2. New public sector loans on less favorable terms in 2015-2035 2	5	5	4	4	4	4	**5**	7
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	5	5	5	4	4	4	**4**	5
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	5	5	4	4	4	4	**4**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	5	5	5	5	5	4	**4**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	5	5	5	5	5	4	**5**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	5	5	5	5	5	5	**6**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	5	7	6	6	6	6	**5**	6
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	40	40	40	40	40	40	**40**	40

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming
an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 1c. Myanmar: Public Sector Debt Sustainability Framework, Baseline Scenario, 2012/13-2035/36

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2012/13	2013/14	2014/15	Average 5/	Standard Deviation 5/	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2015/16-2020/21 Average	2025/26	2035/36	2021/22-2035/36 Average
Public sector debt 1/	43.1	34.8	31.6			33.4	33.4	33.6	34.1	34.7	35.1		38.0	43.7	
of which: foreign-currency denominated	25.3	18.0	14.4			15.8	16.3	16.6	17.0	17.4	17.8		20.0	25.5	
Change in public sector debt	-6.2	-8.3	-3.2			1.8	0.0	0.2	0.4	0.6	0.5		0.6	0.4	
Identified debt-creating flows	1.1	-1.6	-0.6			1.8	-0.1	0.2	0.4	0.6	0.4		0.5	0.6	
Primary deficit	0.4	0.2	1.3	1.8	1.2	3.3	3.1	3.1	2.9	2.9	2.8	3.0	2.8	2.4	2.6
Revenue and grants	23.4	23.3	26.4			20.8	20.6	20.8	21.5	22.0	22.3		23.2	25.2	
of which: grants	0.1	0.3	0.5			0.5	0.5	0.5	0.6	0.6	0.6		0.5	0.5	
Primary (noninterest) expenditure	23.8	23.6	27.7			24.1	23.7	23.8	24.4	24.9	25.1		25.9	27.5	
Automatic debt dynamics	0.6	-1.8	-1.8			-1.5	-3.3	-2.9	-2.5	-2.3	-2.3		-2.2	-1.7	
Contribution from interest rate/growth differential	-3.5	-3.4	-2.4			-2.9	-3.0	-2.7	-2.4	-2.2	-2.2		-2.1	-1.6	
of which: contribution from average real interest rate	-0.1	-0.1	0.4			-0.4	-0.4	-0.1	0.1	0.2	0.2		0.4	0.7	
of which: contribution from real GDP growth	-3.4	-3.3	-2.7			-2.5	-2.6	-2.6	-2.5	-2.4	-2.5		-2.5	-2.3	
Contribution from real exchange rate depreciation	4.1	1.6	0.5			1.4	-0.2	-0.2	-0.2	-0.1	-0.1		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-7.3	-6.7	-2.6			0.1	0.1	0.0	0.0	0.0	0.0		0.0	-0.2	
Other Sustainability Indicators															
PV of public sector debt	...	...	28.2			29.4	28.9	28.8	28.9	29.2	29.3		30.9	35.1	
of which: foreign-currency denominated	...	...	11.0			11.9	11.8	11.8	11.8	11.9	12.0		12.9	16.9	
of which: external	...	...	11.0			11.9	11.8	11.8	11.8	11.9	12.0		12.9	16.9	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	3.1	2.5	3.5			5.7	5.8	5.8	5.9	6.1	6.0		5.9	6.1	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	106.9			141.5	140.7	138.6	134.2	132.8	131.4		133.3	139.4	
PV of public sector debt-to-revenue ratio (in percent)	...	...	108.9			145.0	144.2	142.1	138.1	136.6	135.0		136.3	142.2	
of which: external 3/	...	...	42.5			58.4	59.0	58.2	56.7	55.7	55.1		56.9	68.4	
Debt service-to-revenue and grants ratio (in percent) 4/	10.3	8.3	8.1			10.9	12.6	12.9	13.4	14.2	14.1		13.4	14.6	
Debt service-to-revenue ratio (in percent) 4/	10.3	8.4	8.2			11.2	13.0	13.2	13.7	14.5	14.5		13.7	14.9	
Primary deficit that stabilizes the debt-to-GDP ratio	6.7	8.5	4.5			1.5	3.2	2.8	2.5	2.3	2.3		2.2	1.9	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	7.3	8.4	8.5	8.3	3.5	8.5	8.4	8.3	8.0	7.7	7.7	8.1	7.2	5.7	6.8
Average nominal interest rate on forex debt (in percent)	0.6	1.6	2.2	1.9	0.9	2.7	2.5	2.3	2.1	2.0	1.9	2.3	1.5	1.4	1.5
Average real interest rate on domestic debt (in percent)	2.4	1.5	2.7	-4.2	7.4	-3.6	-3.2	-0.9	0.4	1.2	1.5	-0.8	2.8	4.8	3.5
Real exchange rate depreciation (in percent, + indicates depreciation)	17.1	7.1	3.1	-4.7	14.1	10.3	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	2.8	5.7	5.9	10.8	8.0	12.2	11.8	9.2	7.7	7.0	6.6	9.1	5.4	3.5	4.7
Growth of real primary spending (deflated by GDP deflator, in percent)	75.3	7.4	27.2	11.1	24.1	-5.4	6.6	8.9	10.7	9.5	8.6	6.5	7.8	6.2	7.4
Grant element of new external borrowing (in percent)	...	...	...	...	...	37.6	39.1	41.0	41.7	42.0	43.0	40.8	41.0	40.2	...

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 1d. Myanmar: Sensitivity Analysis for Key Indicators of Public Debt 2015/16-2035/36

	Projections							
	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2025/26	2035/36
PV of Debt-to-GDP Ratio								
Baseline	29	29	29	29	29	29	31	35
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	29	28	27	26	26	26	25	24
A2. Primary balance is unchanged from 2015	29	29	29	29	30	30	33	40
A3. Permanently lower GDP growth 1/	29	29	29	30	31	32	38	59
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017	29	30	32	33	34	35	40	50
B2. Primary balance is at historical average minus one standard deviations in 2016-2017	29	29	29	29	29	29	31	35
B3. Combination of B1-B2 using one half standard deviation shocks	29	29	29	29	30	31	35	42
B4. One-time 30 percent real depreciation in 2016	29	34	33	32	32	32	31	34
B5. 10 percent of GDP increase in other debt-creating flows in 2016	29	36	35	34	34	34	34	37
PV of Debt-to-Revenue Ratio 2/								
Baseline	141	141	139	134	133	131	133	139
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	141	136	130	123	119	115	106	96
A2. Primary balance is unchanged from 2015	141	141	140	136	136	136	142	160
A3. Permanently lower GDP growth 1/	141	142	142	140	141	143	165	235
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017	141	148	156	155	157	158	174	200
B2. Primary balance is at historical average minus one standard deviations in 2016-2017	141	140	138	134	132	131	133	139
B3. Combination of B1-B2 using one half standard deviation shocks	141	140	138	137	138	139	150	168
B4. One-time 30 percent real depreciation in 2016	141	164	158	150	145	141	136	135
B5. 10 percent of GDP increase in other debt-creating flows in 2016	141	176	170	160	156	152	148	146
Debt Service-to-Revenue Ratio 2/								
Baseline	11	13	13	13	14	14	13	15
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	11	13	13	12	12	12	11	10
A2. Primary balance is unchanged from 2015	11	13	13	14	14	15	14	17
A3. Permanently lower GDP growth 1/	11	13	13	14	15	15	17	24
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017	11	13	14	15	17	17	18	21
B2. Primary balance is at historical average minus one standard deviations in 2016-2017	11	13	13	13	14	14	13	15
B3. Combination of B1-B2 using one half standard deviation shocks	11	13	13	13	14	15	15	17
B4. One-time 30 percent real depreciation in 2016	11	14	15	16	17	17	16	18
B5. 10 percent of GDP increase in other debt-creating flows in 2016	11	13	15	25	16	17	14	15

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

MYANMAR

August 24, 2015

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION—SUPPLEMENTARY INFORMATION

Prepared by Asia and Pacific Department

1. **This supplement provides preliminary information on the impact of the recent floods in Myanmar since the staff report was finalized in early August.** Staff's assessment is that in the short term the fiscal and current account deficits are likely to be higher, and overall growth this year weaker than previously projected, which may warrant a modest adjustment to the timing and pace at which some of the staff's policy recommendations should be implemented. Paragraph 4 of this supplement forms part of the staff's assessment of the recent developments, and paragraphs 5 and 6 outline the possible recalibration of some of the policy recommendations in the staff appraisal.

2. **Floods triggered by monsoon rains together with Cyclone Komen have caused major casualties and damages since July.** As of mid-August, the floods and associated landslides killed 117 people and affected more than 1 million people (Myanmar's population is estimated to be around 51 million). About 1.4 million acres of farmland are reportedly affected by flooding with about half of the affected totally damaged (around 3 percent of the estimated total sown area), and over 16,000 homes and 3,000 school buildings have been damaged by floods. The authorities are working on preliminary estimates of damages and losses, but it will take some time before an official comprehensive assessment of damages and losses can be completed. Nevertheless, the total damages and losses are expected to be significant. The authorities have requested World Bank assistance to carry out a Post-Disaster Needs Assessment (PDNA).

3. **A state of emergency has been declared in the four worst-hit states and regions in the west of the country and the government has appealed for international assistance.** Food, shelter, clean water and sanitation are in immediate need. The authorities have set up a National Natural Disaster Management Committee headed by a Vice President. Apart from immediate disaster relief, the government is organizing the distribution of seeds and providing support to the use of farm equipment for replanting. Repair of infrastructure, such as bridges and railroads, is already under way. A number of development partners have provided immediate disaster relief and humanitarian assistance. The World Bank and the Asian Development Bank plan to tap into their emergency assistance facilities, as well as to bring forward disbursement of some of the existing resources allocated for Myanmar, to assist the country's recovery and reconstruction efforts. The authorities intend to request Fund assistance under the Rapid Credit Facility.

4. **While an accurate assessment will require a PDNA, staff expects the floods to add significant short-term pressure on inflation, government spending, and the external position.** Some food prices have already experienced a spike, and it is expected that inflation will rise further from already elevated levels. Apart from an increase in spending in the immediate aftermath of the disaster, additional public resources will be needed for recovery and reconstruction through the next fiscal year. The increased spending will contribute to the already rapid growth of imports, and together with the reduced exports of crops, the balance of payments situation is likely to worsen compared with staff's baseline projections. On the other hand, the impact on the private banking sector is expected to be limited, as commercial banks in Myanmar have limited exposure to the agricultural sector, which appears to have borne the brunt of the disaster impact, although some businesses in urban areas may also have been affected by the floods. State-owned banks will likely be more affected as they are more involved in lending to the agricultural sector – losses here will impact on the fiscal position via a deterioration of the state economic enterprise sector balance.

5. **The expected impact of the floods may affect the timing of fiscal consolidation.** The authorities should continue to aim for an early phase-out of CBM financing of the fiscal deficit and scale up Treasury bill auctions, but a temporarily larger fiscal deficit in this and next fiscal year, commensurate with the additional resources needed for recovery and reconstruction, should be accommodated. To the extent that at least part of the additional spending needs will be covered by external assistance, the inflationary impact of moderately higher fiscal deficits will be limited, but a more decisive fiscal consolidation may be necessary in the outer years to preserve the fiscal target and debt sustainability. To this end, the authorities should also aim for grants and concessional loans in seeking external assistance. If external assistance falls short of the need, the authorities should consider further reprioritizing expenditure to protect spending targeted at the vulnerable and poor.

6. **On the monetary front, some short-term adjustment to the monetary policy stance may be required.** The early October target for the full implementation of the recalibrated reserve requirement should be maintained, but the CBM may need to adjust the timing of sterilization operations if pressures on liquidity begin to appear. The CBM's discount window could also be used to meet temporary increases in liquidity demand. However, the CBM should be prepared to resume tightening the monetary stance through increasing the reserve requirement and scaling up deposit auctions if there are signs of a long-lasting effect of higher food prices on aggregate inflation. Staff continues to advise the authorities to maintain exchange rate flexibility, which would help mitigate the impact of the floods on the external position and facilitate economic recovery.

Statement by Ms. Pornvipa Tangcharoenmonkong, Alternate Executive Director and Ms. Nwe Ni Tun, Advisor to the Executive Director
August 28, 2015

Introduction

1. On behalf of the Myanmar authorities, we would like to express our deep appreciation to Mr. Yongzheng Yang and his team for the productive discussions during the 2015 Article IV Consultation and for their comprehensive set of reports.

2. The authorities highly value the Fund's constructive policy advice and technical assistance which significantly complements and contributes to Myanmar's ongoing economic reform agenda. While Myanmar has made substantial achievements in most areas of the economic reform program, the authorities recognize the need to further accelerate the ongoing reform process. The authorities broadly agree with staff's recommendations and recognize the importance of sustaining economic and structural reforms through creating fiscal space to boost public investment, strengthening banking regulation and supervision to maintain financial stability, and improving the business environment to support inclusive growth. Our authorities broadly concur with the staff appraisal and remain fully committed to the economic reform process.

Recent Economic Developments and Outlook

3. In line with the objectives under the Framework for Economic and Social Reform (FESR)[1], Myanmar has continued its growth momentum over the years. In fiscal year[2] (FY) 2014/15 – the fourth year of the authorities' Five-Year National Development Plan (Five-Year Plan) - real GDP growth is estimated to grow at 8.5 percent[3], similar to 8.4 percent recorded in FY 2013/2014. The *services and other sector* is the largest contributor to GDP, with a share of 37.7 percent, followed by *the industry sector* (34.4 percent), and the *agricultural, livestock, fishery and forestry sector* (27.9 percent). The average CPI inflation, which increased slightly to 5.9 percent in FY 2014/15 (FY 2013/14: 5.7 percent), is expected to rise further as a result of strong domestic demand from expansionary fiscal policy and rapid growth in private sector credit. The severe flooding in several parts of Myanmar in July which has affected about 1.3 million people and destroyed large areas of rice fields could pose an upside risk to inflation in FY 2015/16.

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[1] The Framework for Economic and Social Reform (FESR) was developed to set the government's policy priorities for 2012- 2015 in order to achieve the long-term goals of the 20-year National Comprehensive Development Plan 2011-2031.

[2] The fiscal year (FY) starts April 1and ends March 31.

[3] Staff's estimation.

4. The current account deficit is estimated to widen to around 6 percent of GDP in FY 2014/15 (FY 2013/14: 5 percent of GDP) due mainly to the higher trade deficit, reflecting strong import growth. Gross international reserves held by the Central Bank of Myanmar (CBM) increased to US$ 5.12 billion, which is sufficient to finance about three months of imports.

5. Credit to the private sector is estimated to expand by 35.5 percent in FY 2014/15 (FY 2013/14: 52.5 percent), in light of increased government expenditure and better access to credit by the private sector, increased business opportunities, and the development of credit facilities to Small and Medium Enterprises (SMEs).

6. The authorities are in broad agreement with staff's assessment on the economic outlook. Medium-to long-term growth prospects remain favorable. However, the authorities' real GDP growth estimate for FY 2014/15 and projection for FY 2015/16 are 9.1 percent and 9.3 percent respectively, slightly higher than staff's projections. For FY 2015/16, the authorities expect to achieve a higher growth rate in the agriculture, livestock and fishery, energy, construction and transportation sectors, which are likely to receive a boost from reform measures that were implemented over the first four years of Myanmar's Five-Year Plan. Notably, reform measures targeted improvements in electricity and water supply, job creation and development in agriculture, tourism, trade and investment, and the financial sector.

Fiscal Policy

7. In line with the policy priorities and objectives of the FESR – a credible, responsive and transparent planning and budget process – the medium term fiscal framework for FY 2015/16 to 2017/18 has been laid out in order to achieve higher budget credibility, enhance fiscal discipline and improve strategic resource allocation.

8. The authorities have gradually tightened fiscal policy and remain committed to reducing central bank deficit financing. The authorities will ensure fiscal sustainability through greater revenue mobilization and expenditure re-prioritization. In addition, the government continues to scrutinize wage and salary increases and reduce non-productive expenditure.

9. The authorities are committed to the Public Finance Management (PFM) reform to strengthen budget formulation and fiscal discipline, control expenditure, as well as improve fiscal accounting and reporting processes. The authorities continue to focus on maintaining fiscal discipline in order to ensure debt sustainability and create the fiscal space needed. With the assistance of the World Bank and other development partners, the Myanmar Modernization of Public Finance Management Project is being implemented to

support efficient, accountable and responsive delivery of public services through Myanmar's PFM systems as well as to strengthen institutional capacity.

10. In order to develop cash and debt management operations, the authorities have established the Treasury Department under the Ministry of Finance (MoF). The Treasury bill auction was introduced in January 2015 to reduce central bank deficit financing and to access financial resources of the private sector. To develop a more effective market with market-determined interest rates and sufficient volume of bids, the authorities plan to issue Treasury bills with different maturities, on top of the existing 3-month bill, lower the minimum face amount of bids, and switch from single to multiple pricing auctions for government securities.

11. Under the fiscal reform program, the authorities have underscored the importance of increasing tax revenue by broadening the tax base and improving tax administration. Continuous efforts have been made to introduce the value-added tax and property tax, simplify the tax system, develop the legal and administrative framework, and implement the Extractive Industries Transparency Initiative (EITI)[4]. Thus far, the establishment of the Large Taxpayer Office (LTO) in 2014 has been effective in improving tax compliance and tax administration while the ongoing Internal Revenue Department (IRD) reform program will continue to help to improve the efficiency and effectiveness of the IRD and move it closer to international standards of tax administration.

12. On the expenditure side, the authorities will prioritize infrastructure development, socio-economic development, rural development and poverty alleviation. The authorities are committed to ensure the efficiency of spending in these priority areas.

Monetary and Exchange Rate Policy

13. The authorities have made significant progress in the area of monetary and exchange rate policies, including moving towards a managed float exchange rate system, enacting the new Central Bank Law, and introducing the deposit auction and Treasury bill auction after the CBM was granted its autonomy in July, 2013.

14. The authorities concur with staff's recommendations in various areas regarding the monetary sector. The authorities recognize the risk of increasing inflation as a result of rapid credit growth to the private sector and expansion of government expenditure. Accordingly, the authorities continue to maintain a tight monetary policy stance in line with the monetary target which is reviewed frequently. Substantial progress has also been made in improving the liquidity management framework. The deposit auction introduced in 2013 allows market driven interest rates and more terms of deposits with greater participation by commercial banks and greater flexibility for the CBM to target specific

[4] EITI is a global standard to promote open and accountable management of natural resources.

types of banks in the deposit auctions. In addition, the authorities have also introduced a new reserve requirement for banks and financial institutions in April 2015, with full compliance required by October 2, 2015.

15. In addition, the introduction of Treasury bill auctions in January 2015, in close cooperation with the MoF and with technical assistance from the Fund, has reduced central bank financing of the fiscal deficit, thereby decreasing inflationary pressures stemming from fiscal expansion.

16. To develop the government securities market, the Securities Steering Group and Working Group, which include senior officials from CBM and MoF, have been established to implement the development plans in this area. The authorities plan to introduce Treasury bond auctions in the near future to further promote the development of the Treasury bond market. This will further promote market-determined interest rate and attract investor participation in the Treasury bond market. Allowing the purchase of government securities by foreign banks would be the next step when all prerequisites are met.

17. The authorities have also taken note of staff's recommendation to tighten the access to the CBM discount window to prevent the use of the discount window as a de facto revolving credit facility. In this regard, the authorities plan to abolish the CBM discount window facility and replace it with the overnight window when the CBM Net system[5] can be fully implemented in 2016.

18. On the exchange rate regime, in line with staff's recommendation, the authorities have taken steps to reduce the divergence between the official reference rate and market rate as well as to abolish multiple exchange rates starting from July 13, 2015. As a result, the divergence between the CBM reference rate and the market rate has narrowed and will be unified in the near future. This will help deepen the foreign exchange interbank market, paving the way for completion of the remaining obligations under Article VIII.

19. Due to the strengthening of the US dollar and strong demand in the domestic market, the volatility in the foreign exchange market has increased towards the end of 2014, resulting in a shortage of foreign currencies. This in turn led to the depreciation of the Kyat. In response, the CBM started sales of foreign currencies to major importers by using CBM's foreign exchange reserves and was able to keep the Kyat broadly in line with medium-term fundamentals. Amidst the unfavorable external environment, potentially lower rice exports as a result of the recent flooding may put further pressure

[5] The CBM is implementing the project of "Modernizing the Funds, Payment and Securities Settlement Systems" by Japan International Cooperation Agency (JICA) since February 2014 which is a grant aid program. This project includes Real Time Gross Settlement System (RTGS), Securities Settlement System and Mechanized Clearing House System (MCH).

on the Kyat. Although the use of CBM's reserves has helped to meet the demand for foreign exchange and to smooth exchange rate fluctuations at this juncture, the authorities see the need to accumulate more reserves and are cognizant that adjusting macroeconomic policies are of the utmost importance in the longer term.

20. The authorities underscore their commitment to become an Article VIII member country and have made significant progress towards eliminating most of the Article XIV restrictions. The authorities are also taking active steps to address gaps that are preventing them from fully eliminating the present multiple currency practice. In this regard, the authorities have phased out foreign exchange certificates and the Foreign Exchange Management Law and accompanying regulations were enacted in August 2012 and September 2014, respectively.

21. Nevertheless, due to the absence of a mechanism in the multiple price foreign currency auction that would prevent exchange rates of accepted bids from deviating by more than 2 percent, the authorities would like to request the Fund's approval for Myanmar to retain the multiple currency practice under Article VIII, Section 3 until August 27, 2016 or the conclusion of the next Article IV consultation with Myanmar, whichever is earlier.

Financial Sector Developments

22. With the growing economy, Myanmar's financial sector is rapidly expanding. In ensuring that the financial sector remains supportive of growth without undermining financial sector stability, the authorities are highly committed to strengthening the regulatory and supervisory framework. Private sector credit growth, although remains elevated, has started to moderate. Progress has been made in strengthening the supervisory framework, including upgrading prudential regulations, revising supervisory framework, developing supervisory techniques in line with international standards, and enhancing the capacity of the supervisors through training and seminars with the assistance of international institutions, regional organizations and other development partners. The CBM has allocated its most qualified staff to work closely with the Fund to further enhance the supervisory framework.

23. In order to achieve greater access to international markets, the CBM, on October 1, 2014, granted preliminary approval to nine foreign banks to begin preparations to commence banking operations in Myanmar. Thus far, the CBM has issued final licenses to eight of the nine foreign banks, enabling them to begin their operations. In this regard, the authorities are concurrently strengthening the capacity of supervisors to supervise and regulate foreign banks. The presence of foreign bank operations will also help to promote greater use of technology and encourage international standard practices in the banking industry.

24. The authorities have made significant progress in improving the financial infrastructure to strengthen the financial system and to modernize its financial framework. Several laws and related regulations have been enacted, namely, the new Foreign Exchange Management Law (August 2012), the new Central Bank of Myanmar Law (July 2013), the Securities Exchange Law (July 2013) and the regulations of Foreign Exchange Management Law (September 2014). The enacting of a new Financial Institutions of Myanmar Law (FIML) and CBM rules and regulations are in the final stages. In particular, the rules and regulations under the FIML are expected to further modernize financial institutions.

25. The Anti-money Laundering and Counter Terrorism (AML/CFT) Law was enacted in March 2014 and its accompanying regulations are currently being drafted with high priority. A number of supervisory tools were developed under the IMF TA project with the objective of assisting the CBM to strengthen its overall AML/CFT legal framework and bring it in line with the Financial Action Task Force (FATF) Recommendations. As a result, the CBM has issued a Risk Management Guidance Note for banks on January 27, 2015. Moreover, to address concerns of the FATF identified in the Public Statement, the updated risk based CDD Directive has been prepared with the assistance of IMF and will be issued soon.

26. The enactment of the Securities Exchange Law in July 2013 was a major milestone as it enabled the establishment of the Securities Exchange Commission (SEC) to supervise and manage the securities market and also paved the way for further capital market development. The authorities have also adopted a concrete plan to establish a stock exchange in late 2015.

27. To develop greater financial access and promote a more inclusive financial system, the authorities have taken steps to expand the branch network of the banking system, encourage microfinance, and enhance innovations in ATMs, point-of-sale systems and mobile banking. In addition, the payment and settlement systems will be further enhanced with the establishment of the CBM Net system.

28. In addition, the Interbank Market Steering Committee will undertake continued and extensive efforts towards the establishment of a functioning and active interbank FX market and money market.

29. The authorities also place great importance on strengthening institutional foundation and capacity. Some programs are still ongoing and include, among others, introducing the "Modernizing the Funds, Payment and Securities Settlement Systems" project, developing the interbank foreign exchange market and money market, implementing new accounting standards and preparing a financial sector development master plan with the technical assistance from the regional and international community.

Macroeconomic and Structural Reforms

30. Comprehensive macroeconomic reforms are critical to maintaining economic stability, promoting sustainable growth and reducing poverty. In addition to the ambitious reforms in fiscal, monetary and exchange rate as well as financial sector policies, key reforms in business and trade sectors remain on track.

31. Recognizing the importance of creating a conducive investment climate and positive business environment to attract foreign direct investment (FDI), some laws relating to investments have been enacted while existing laws are being revised. Notably, the enacting of the new Foreign Investment Law (2012) has helped to attract more FDI by providing foreign companies access to a wide range of new businesses, longer term leases, favorable tax incentives with various tax and customs duty exemptions, and improving transparency of the foreign investment regulations and implementations. The establishment of Special Economic Zones (SEZs), with a new SEZs law (January 2014), will also help to promote local and foreign investment. Further, to support export development and competitiveness, the authorities are developing the National Export Strategy (NES) in cooperation with the International Trade Centre (ITC) and Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ).

32. The restructuring and privatization of state enterprises are crucial for sustained growth. In this regard, some state economic enterprises (SEEs) have been privatized, especially in the industrial and manufacturing sectors. This has also helped to reduce the fiscal deficit. To strengthen SMEs, the authorities have placed a strong emphasis on improving the legal framework and funding for SMEs. Various laws relating to the industrial sectors have also been enacted with the aim to transform Myanmar into an industrialized economy.

33. To enhance overall socio-economic development, the authorities have affirmed the development of the telecommunication sector as part of its economic reforms. In this regard, progress has been made in issuing telecom licenses to foreign companies. The authorities also underscore their commitment to promote inclusive growth through improving health and education services. The authorities recognize the importance of timely macroeconomic statistics for macroeconomic surveillance and have committed to undertake further efforts in this area.

34. The authorities deeply appreciate the Fund's constructive policy advice and technical assistance. However, given the vast challenges that Myanmar is facing and with TAs available only to some reform areas, the economy continues to face significant difficulties in expediting the comprehensive reforms.

Conclusion

35. Myanmar is undergoing a major economic transition towards a market oriented economy. Despite its positive economic growth performance over the years, Myanmar still faces significant challenges in implementing the economic reform agenda given the constraints in human capital, institutions and infrastructure. The authorities remain committed to continuing efforts in those needed areas under the ongoing reform agenda. In this regard, the authorities firmly believe that the technical assistance, capacity building and valuable advice from regional partners and the international community will enable Myanmar to overcome the remaining challenges and ultimately achieve its long-term economic development goals.

36. Finally, the authorities would like to express their gratitude to the Fund as well as to the World Bank and the ADB, for their unwavering support and valuable policy recommendations over the years. The authorities look forward to continuous support and cooperation as they press ahead with the ongoing economic reform agenda.