



Overview: External Sector In Myanmar

**Introductory Workshop to
Financial Programming and Policies
Yangon, Myanmar
January 19–23, 2015**

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IMF-TAOLAM training activities are supported by funding of the Government of Japan

Outline

- I. **External Sector Overview**
- II. Useful Concepts & Indicators
- III. Balance of Payments Developments
in Myanmar
- IV. External Sector Considerations

External Sector Overview

Basic structure of Balance of Payments

Above the line

Current Account

Capital and Financial Account

Errors and omissions

Overall Balance

Below the line

Financing

External Sector Overview

Basic Structure of current account balance (real transactions)

Trade Balance (Goods) = Exports - Imports

Trade Balance (Services) = Exports - Imports

Net Income (e.g., Interest, Profit Repatriation)

Net Transfers (Official, Private)

Current Account Balance

External Sector Overview

Basic Structure of capital and financial account balance (financial transactions)

Capital Account (*e.g., Debt forgiveness*)

Financial Account

Direct Investment

Portfolio Investment

*Other Investment (e.g., net loans—disbursements minus repayment;
currency and deposits)*

Financial and Capital Account Balance

External Sector Overview

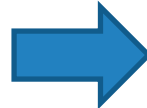
Basic structure: financing

Flows

**-Overall Balance
= Financing**

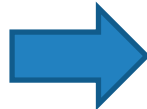


**Change in Net Financial
Reserves**



Foreign Reserve Levels

Change in Arrears

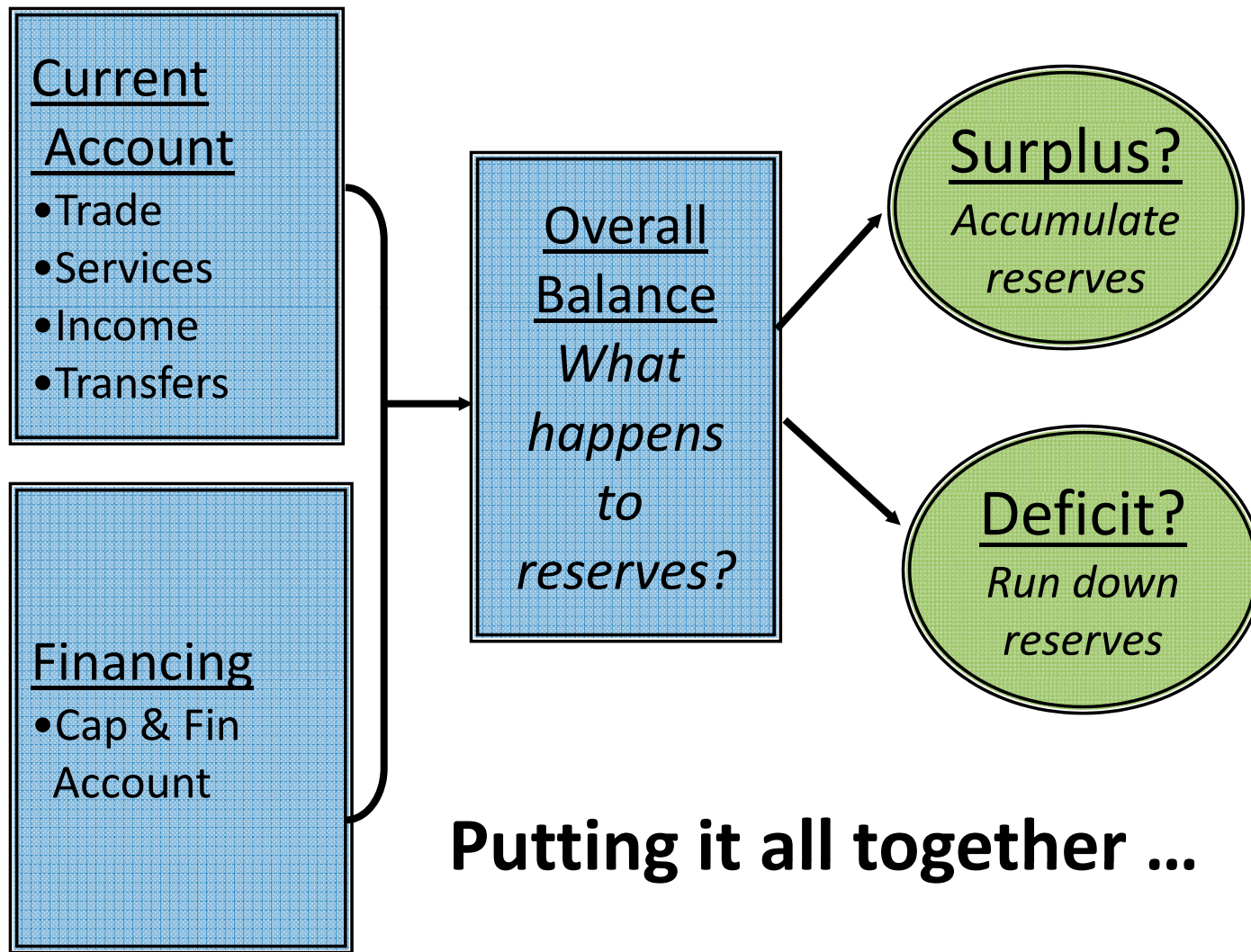


Stock of Arrears

Exceptional Financing

Stocks

External Sector Overview



Outline

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Useful Concepts & Indicators

The exchange rate

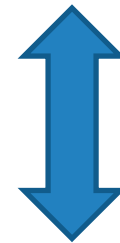
Kyat-US dollar
exchange rate:

- Devaluation
- Appreciation

What determines the
exchange rate?

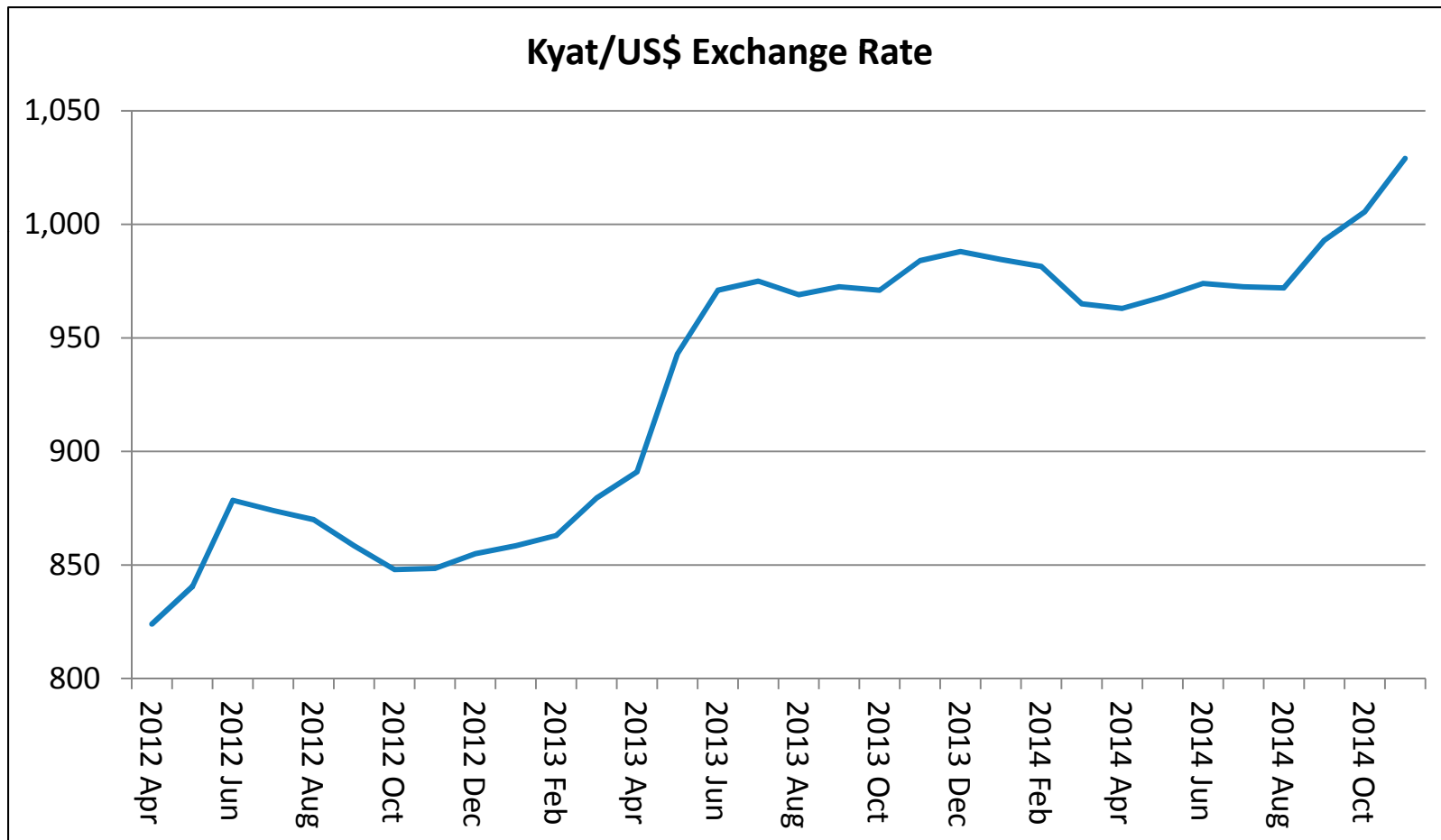
For what does the
exchange rate matter?

But first, two different
ways of measuring the
exchange rate ...



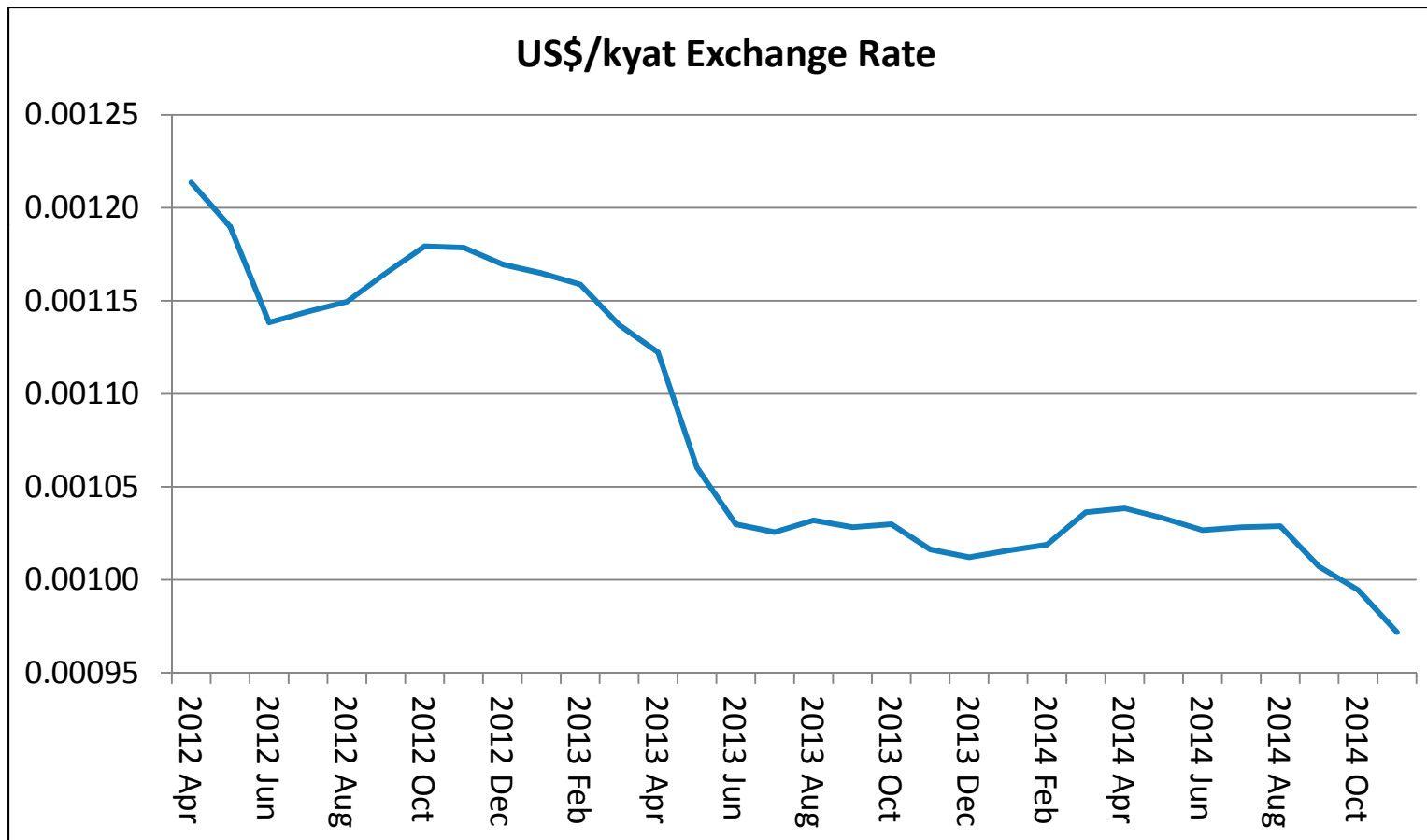
Useful Concepts & Indicators

Measuring the Exchange Rate as Kyat/US\$ Rate



Useful Concepts & Indicators

Measuring the Exchange Rate as US\$/Kyat Rate



Useful Concepts & Indicators

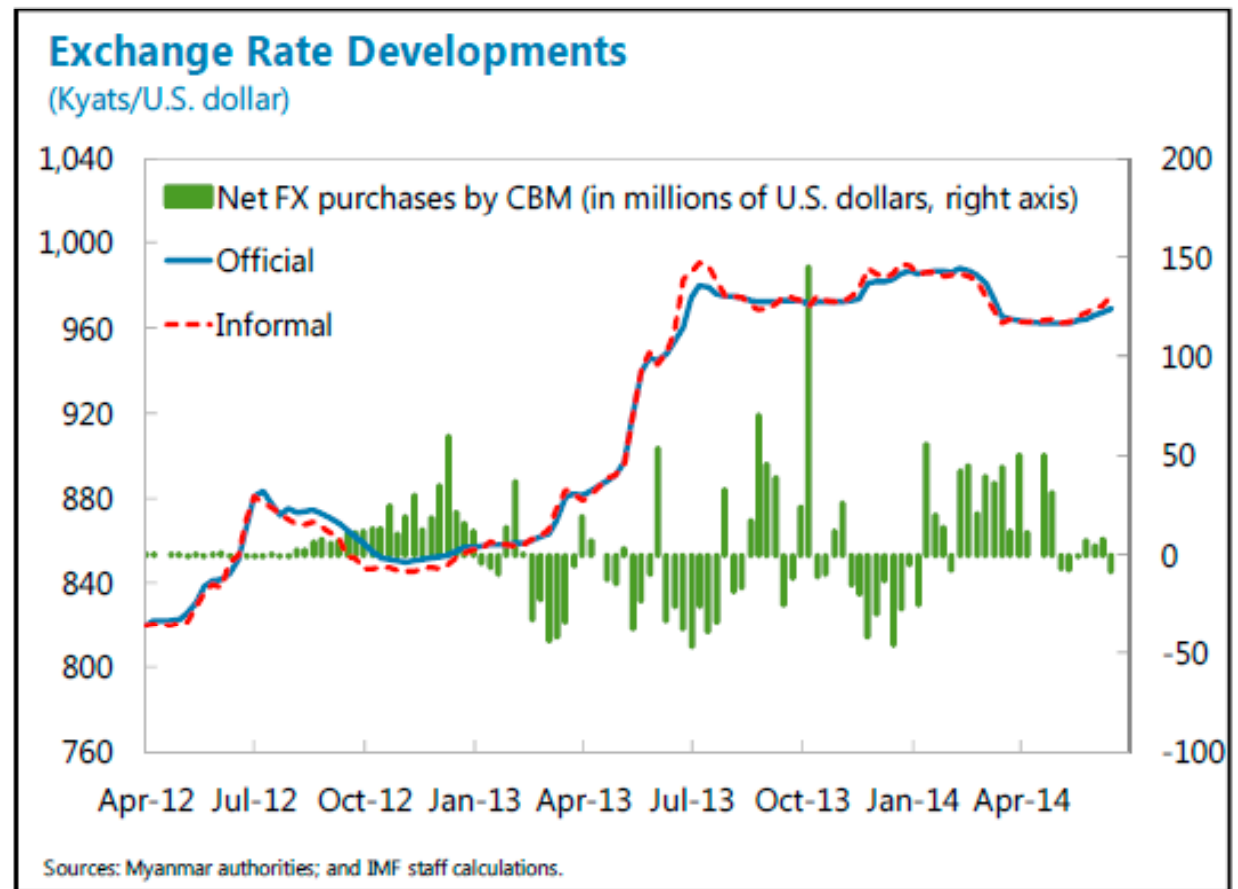
What determines the exchange rate?

- Availability of foreign exchange

Depends on ...

→ Balance of Payments

→ Central bank intervention



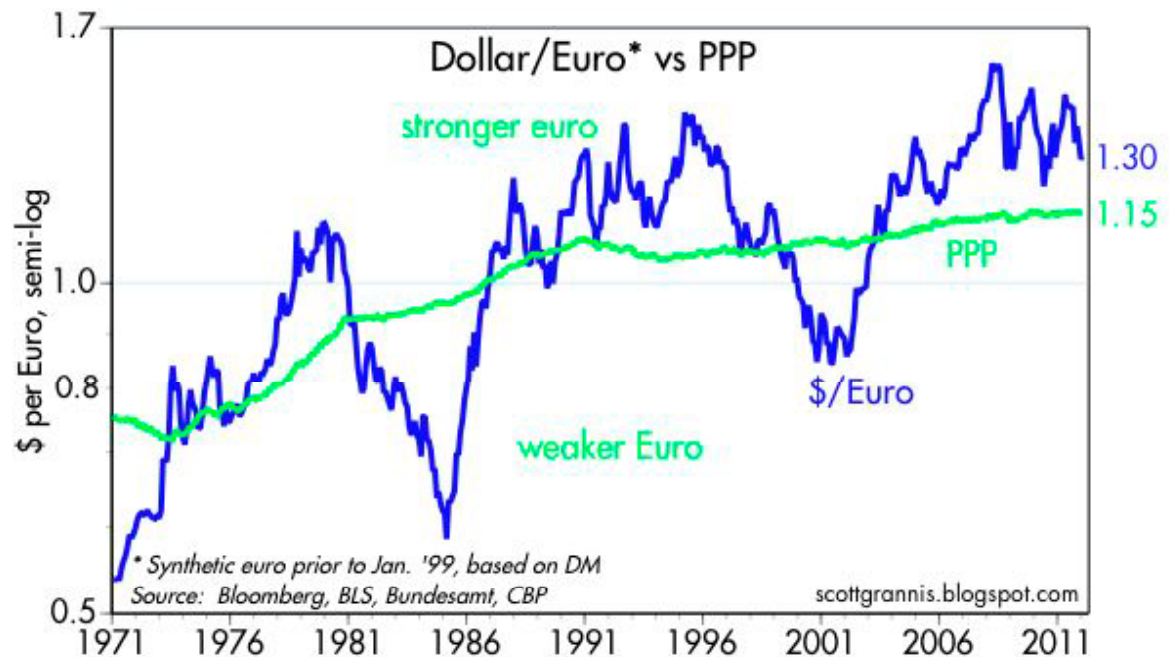
Useful Concepts & Indicators

Fundamental exchange rate factor: price differentials

Similar good in two countries should cost about the same

→ exchange rate corrects for price differential

→ Called 'Purchasing Power Parity'



Useful Concepts & Indicators

Real Exchange Rate

Comparing the price level in Myanmar with that of other countries, all expressed in US\$:

$$RER = \frac{CPI_{Myanmar}^{kyat} \cdot \frac{US\$}{kyat}}{CPI_{USA}^{US\$}} = \frac{CPI_{Myanmar}^{US\$}}{CPI_{USA}^{US\$}}$$

What does it mean if the real exchange rate increases?

- Goods in Myanmar become more expensive relative to their counterparts in the USA
- Kyat becomes more expensive in terms of US dollars

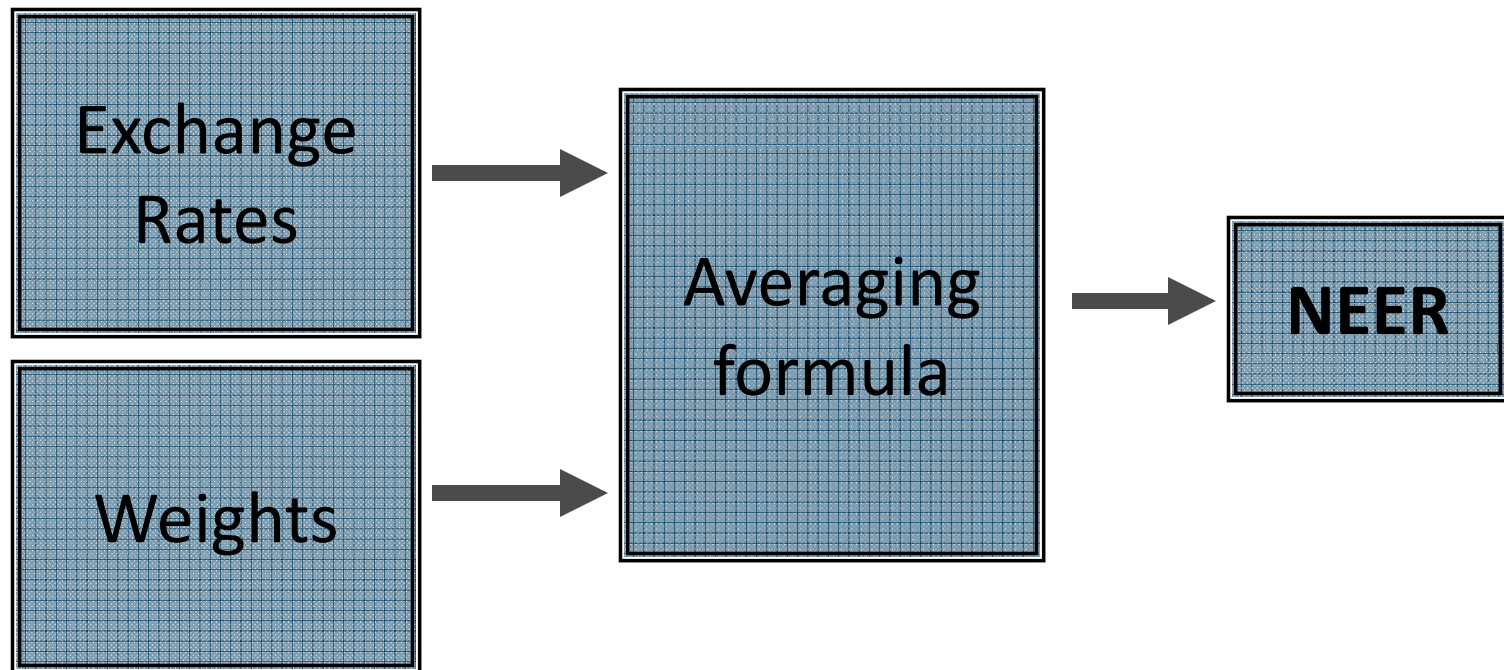
This is called a real appreciation: what do you think is the impact on the economy? (Think in terms of competitiveness ...)

Useful Concepts & Indicators

Nominal Effective Exchange Rate (NEER)

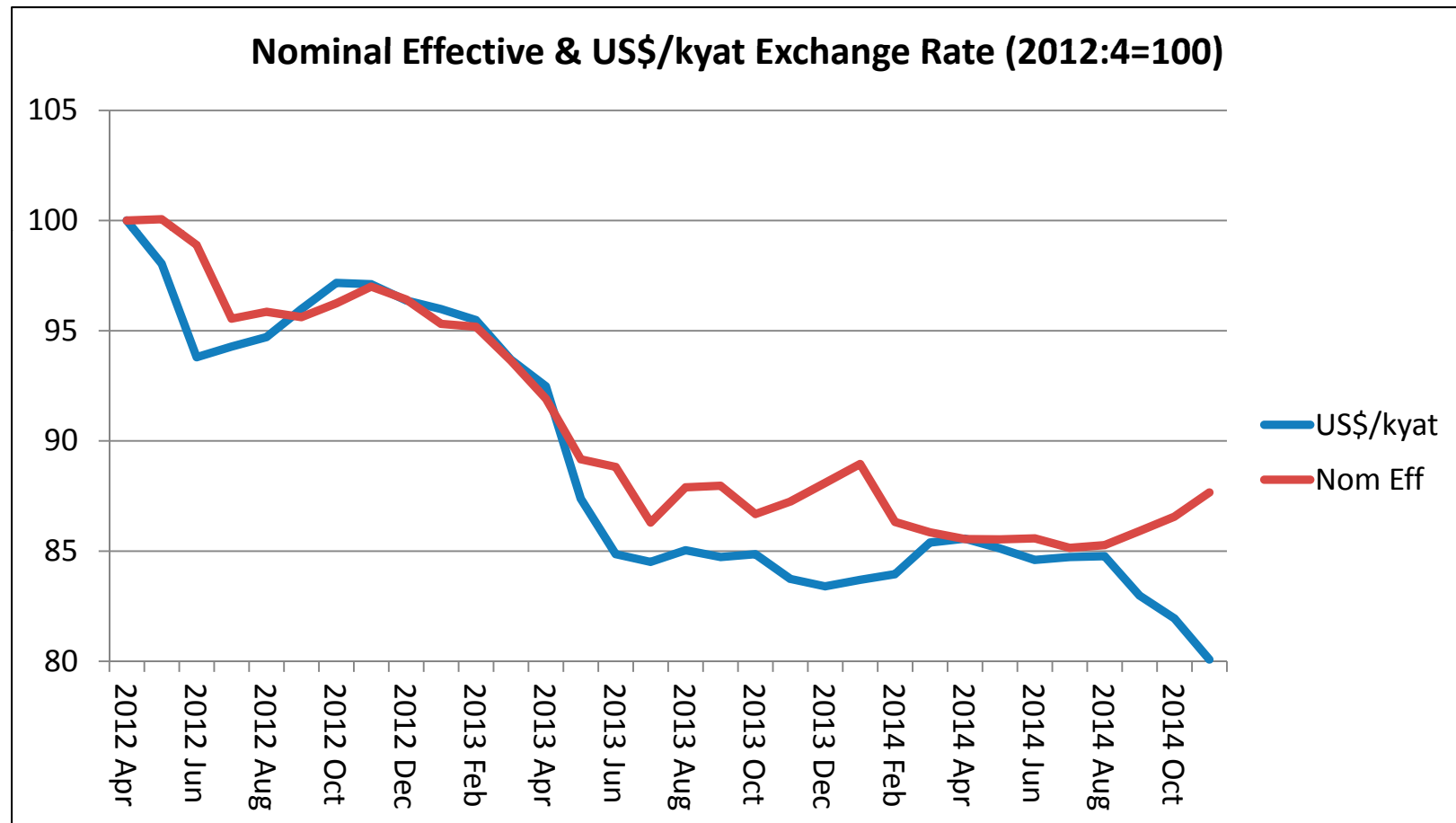
The NEER is a weighted average of indexed nominal bilateral rates

- Bilateral cross rates are expressed in foreign currency per domestic currency and indexed to 100 [note: an increase in US\$/kyat rate means the kyat appreciates against the US dollar]
- The more “important” a competitor, the higher the weight of its currency



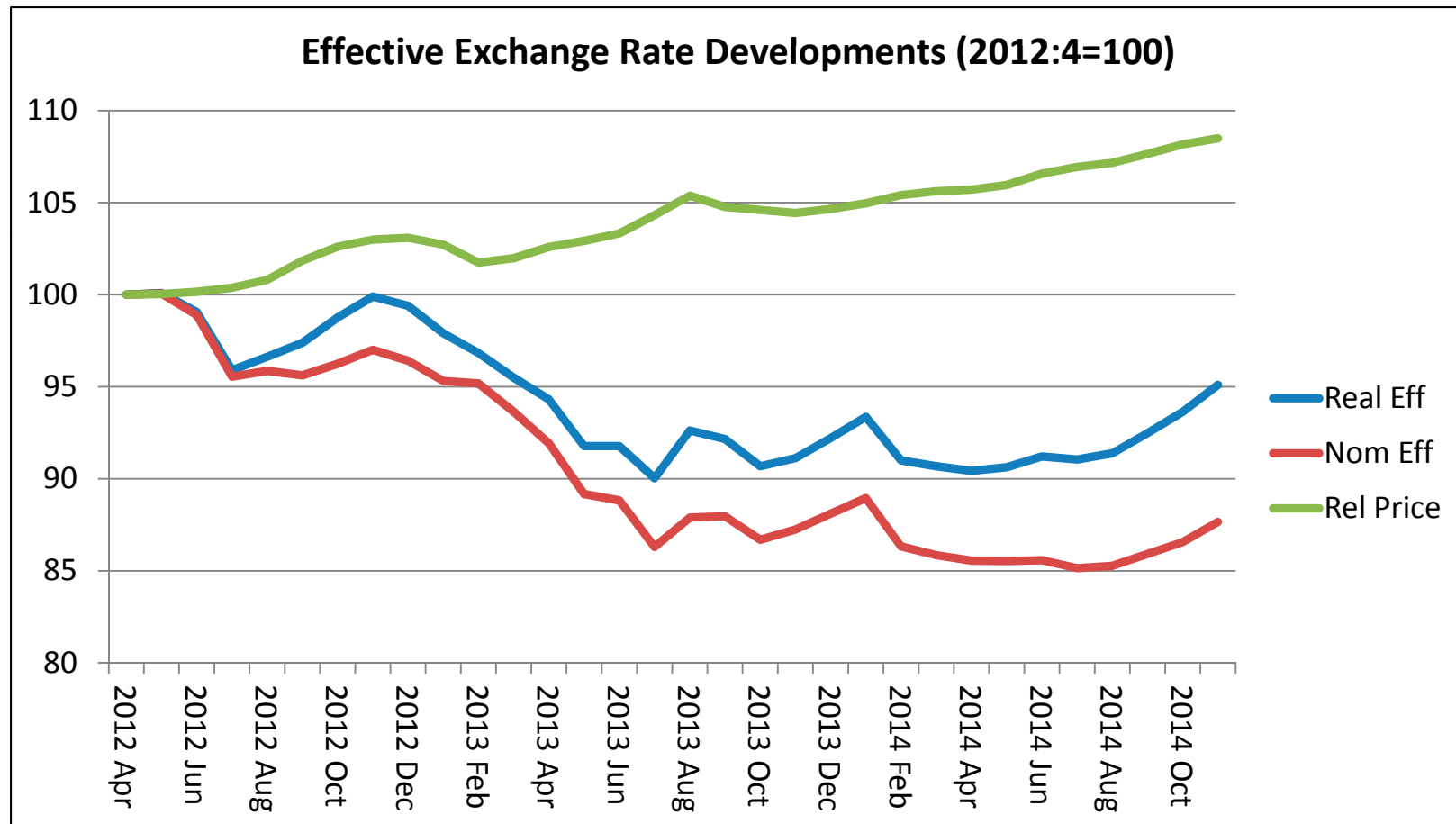
Useful Concepts & Indicators

Myanmar NEER and US\$/kyat Exchange Rate



Useful Concepts & Indicators

Myanmar Real Effective Exchange Rate



Useful Concepts & Indicators

For what does the exchange rate matter?
External competitiveness

$$\text{Export volume} = f(PD/PD^* \cdot ER); YR^*; \dots)$$

Price
effect (-)

Foreign income
effect (+)

where:

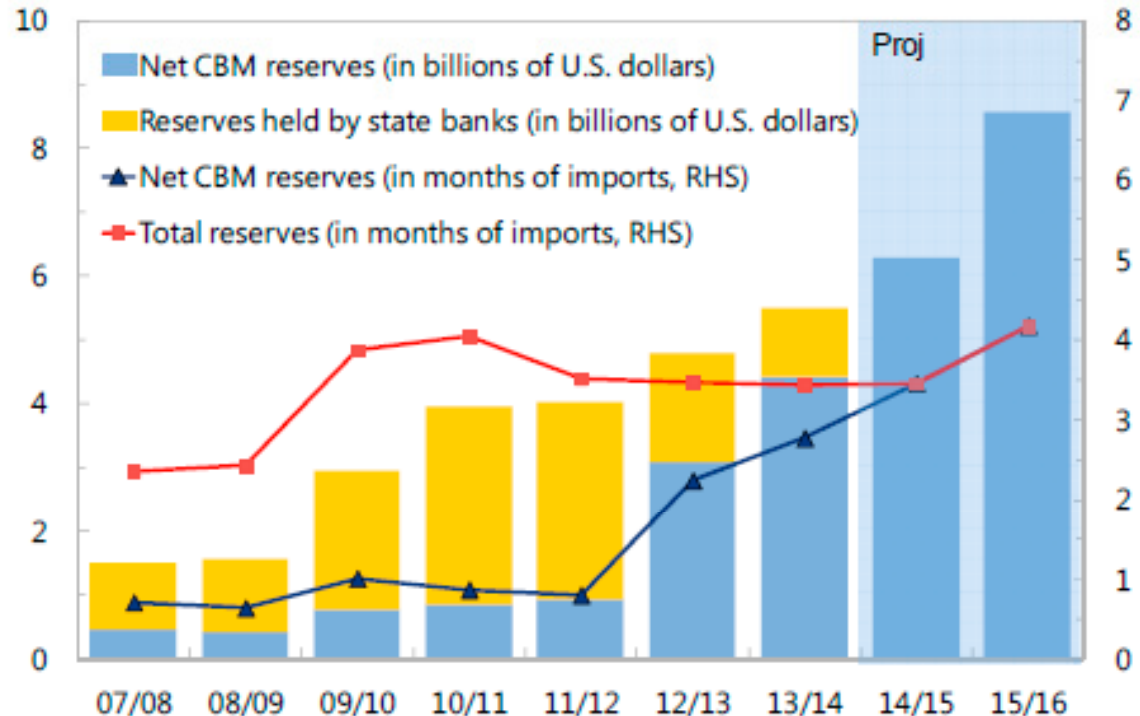
- ER = nominal exchange rate (in home currency per \$)
- PD = domestic price level (in home currency)
- PD* = foreign price level (in \$)
- YR* = foreign income (proxied by real GDP)

Useful Concepts & Indicators

Reserve adequacy

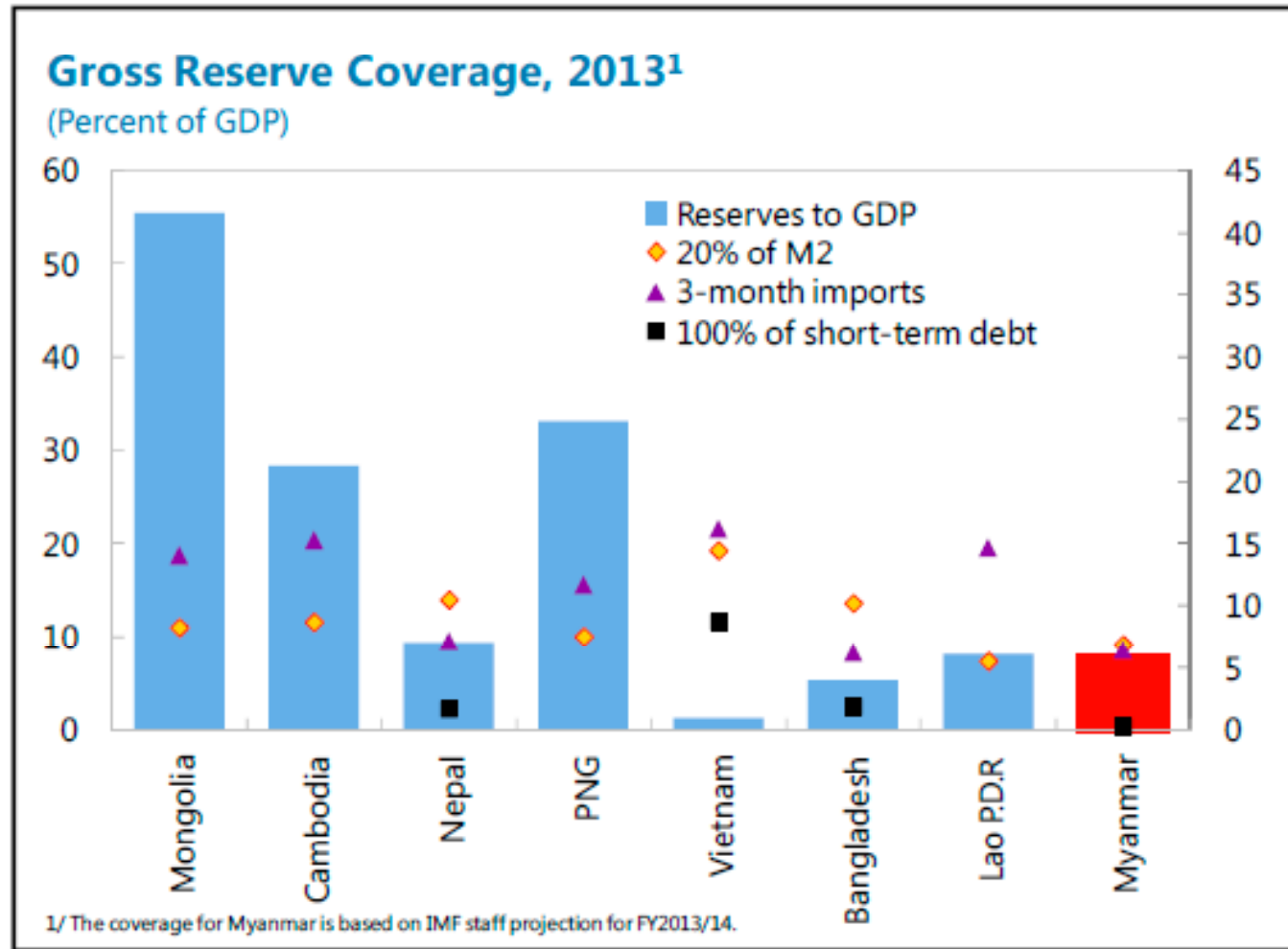
- In relation to trade: import coverage
 - Rule of thumb: reserves should cover 5-6 months of imports (IMF analysis)

Total and Net CBM Reserves



Useful Concepts & Indicators

- In relation to capital flows: vulnerability to sudden capital outflows?



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Balance of Payment Developments in Myanmar

Table 3. Myanmar: Balance of Payments, 2010/11–2015/16

(In millions of US\$, unless otherwise indicated)

	2010/11	2011/12	2012/13	2013/14 Est.	2014/15 Proj.	2015/16
Current account	-617	-1,083	-2,390	-3,090	-3,472	-3,771
Trade balance	645	-195	-2,120	-2,677	-2,473	-3,197
Exports, fob	8,829	10,241	10,344	12,205	14,966	16,666
Of which: Gas	2,523	3,503	3,666	4,206	5,805	6,037
Imports, mostly cif	-8,184	-10,437	-12,464	-14,882	-17,440	-19,863
Nonfactor services, net	-336	-496	-46	-35	52	132
Income, net	-1,156	-882	-757	-1,286	-2,136	-1,992
Of which: Interest due	-306	-560	-94	-220	-219	-240
Transfers, net	231	490	533	907	1,085	1,286
Official	64	41	28	205	229	258
Private	167	449	504	702	857	1,028
Capital and financial account	1,430	2,066	5,110	5,110	5,365	6,116
Direct investment, net	2,249	2,057	2,800	2,621	3,350	3,850
Other investment	114	4	926	555	965	1,516
MLT debt disbursements	500	605	1,085	761	1,200	1,765
Repayments due	-386	-600	-159	-206	-235	-250
Other flows 1/	-933	5	1,384	1,934	1,050	750
Errors and omissions	-1,257	-1,908	-580	-536	0	0
Overall balance	-443	-925	2,140	1,484	1,893	2,344
Financing	443	925	-2,140	-1,484	-1,893	-2,344
Gross official reserves (increase: -)	-84	-72	-2,140	-1,484	-1,893	-2,344
Change in arrears (increase: +)	528	997	-6,056	-4,792	0	0
Exceptional financing (positive: +)	0	0	6,056	4,792	0	0

Balance of Payment Developments in Myanmar

Analyze Myanmar's BOP developments both in US dollar terms and in percent of GDP:



**Your
task!**

Balance of Payment Developments in Myanmar

Let's generate a BOP forecast for 2014/15:

We need a BOP forecast both in US dollar terms and in % of GDP:

- The first step is generating a forecast for the kyat/US\$ exchange rate (which we need for computing the GDP ratios): consider the monthly development of the exchange rate and extrapolate it to the end of the fiscal year
- The second step is adding the BOP forecast in US dollar terms: this is complicated and for now we simply use the IMF forecast in the last Article IV report
- What do you see? Consider ...
 - ✓ ... the main developments in 2014/15 projected by the IMF
 - ✓ what does this imply for the build up of reserves?

Outline

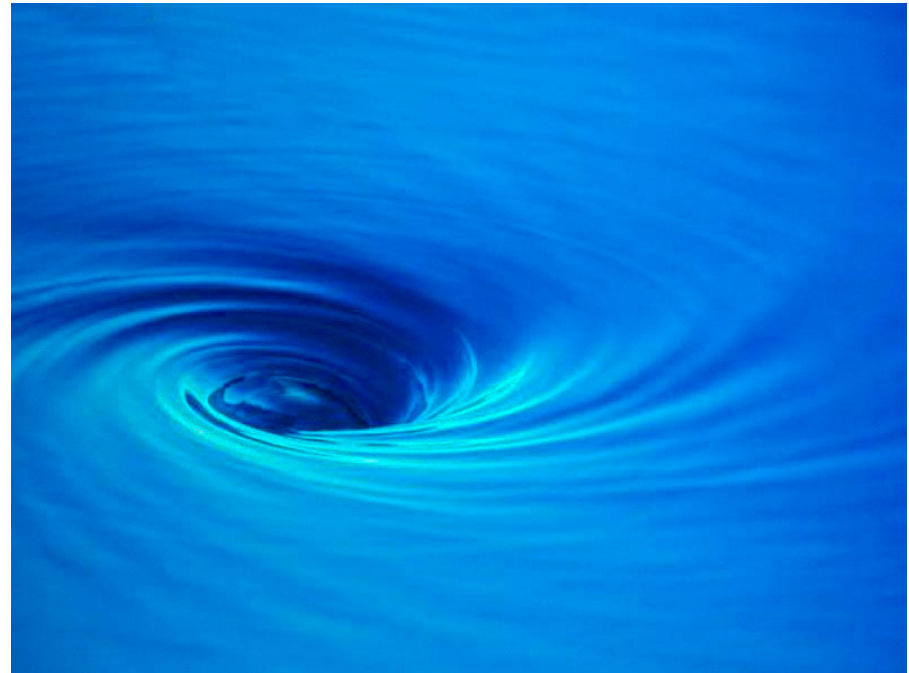
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External Sector Considerations

Main considerations

From a macroeconomic viewpoint, analysis of external sector often focuses on:

- External sustainability
- Growth contribution

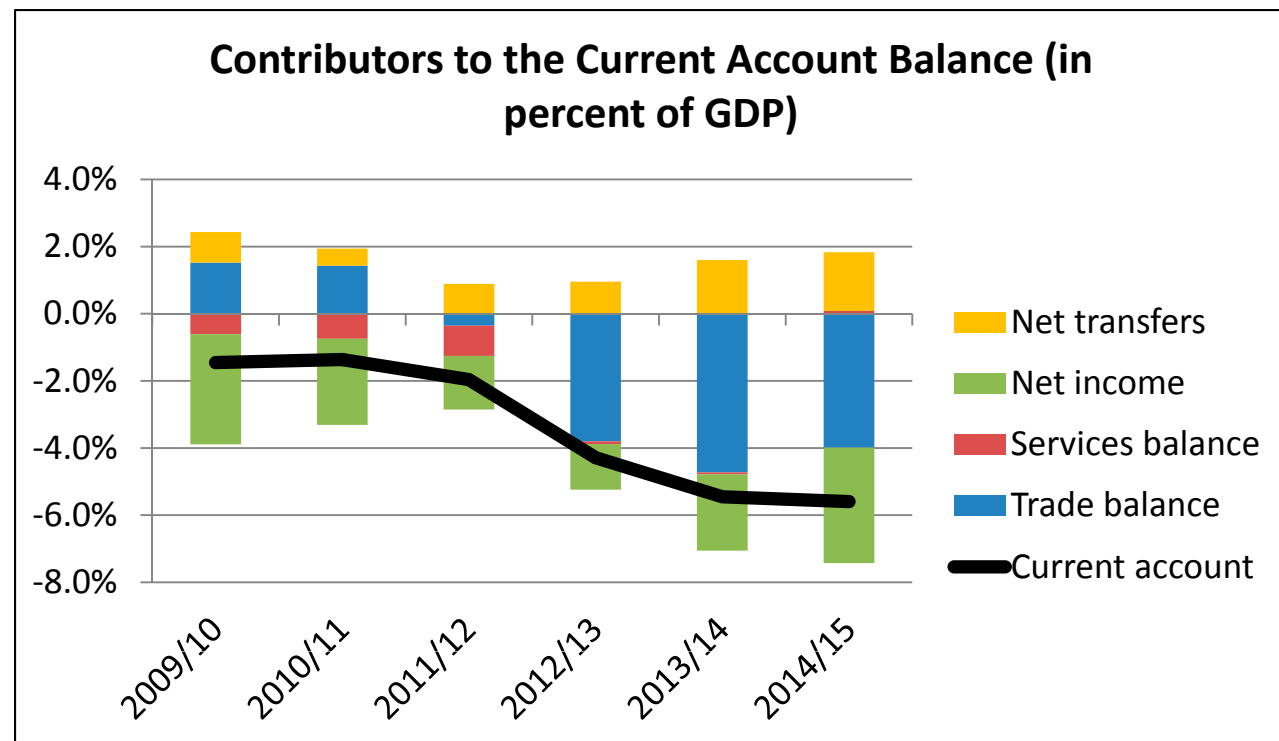


External Sector Considerations

External sustainability

Key question: if country runs **current account deficits**, are they sustainable?

This issue matters for Myanmar!

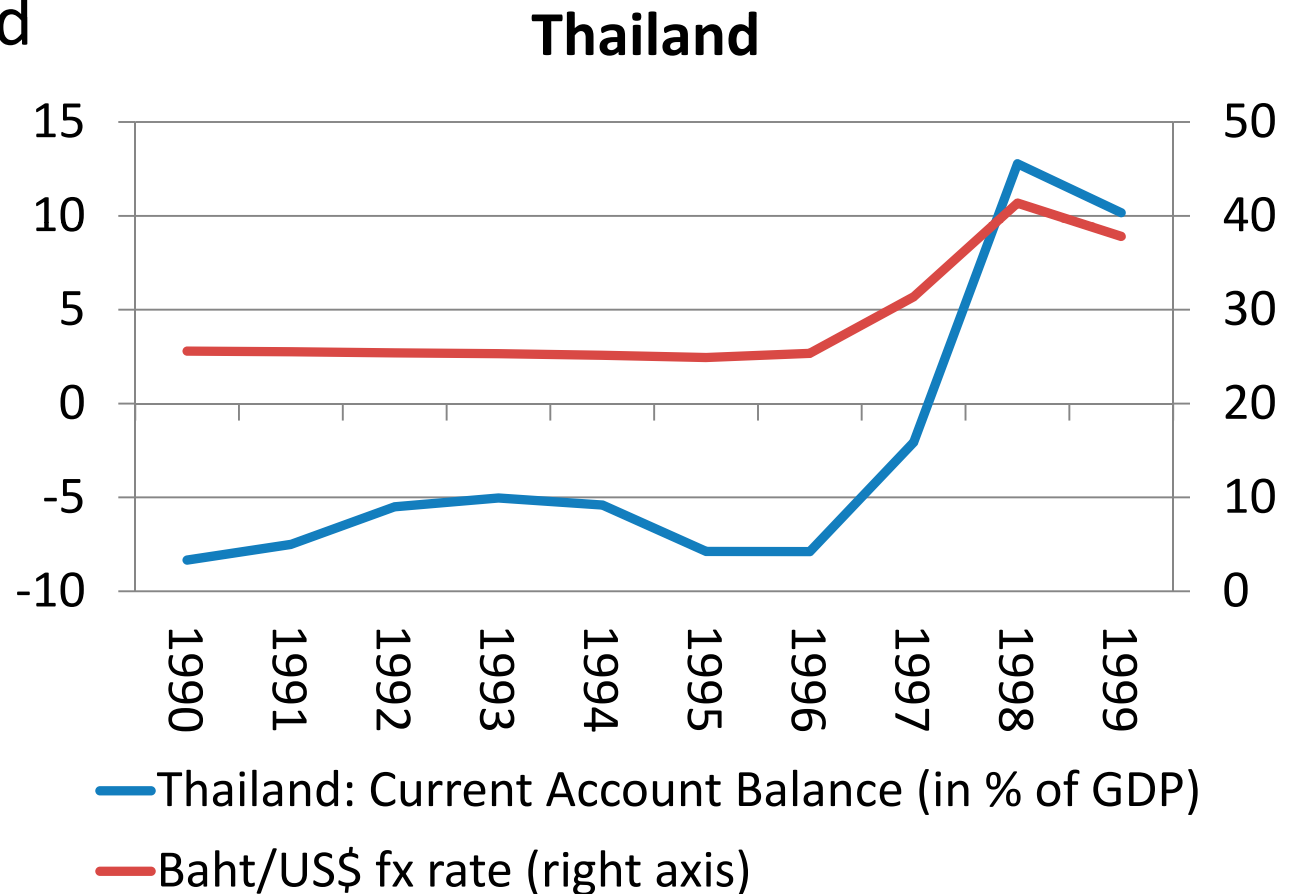


External Sector Considerations

External sustainability

Consider Thailand crisis:

- Large deficits prior to crisis
- Inability to finance deficits was critical cause of crisis
- ... and led to currency crisis

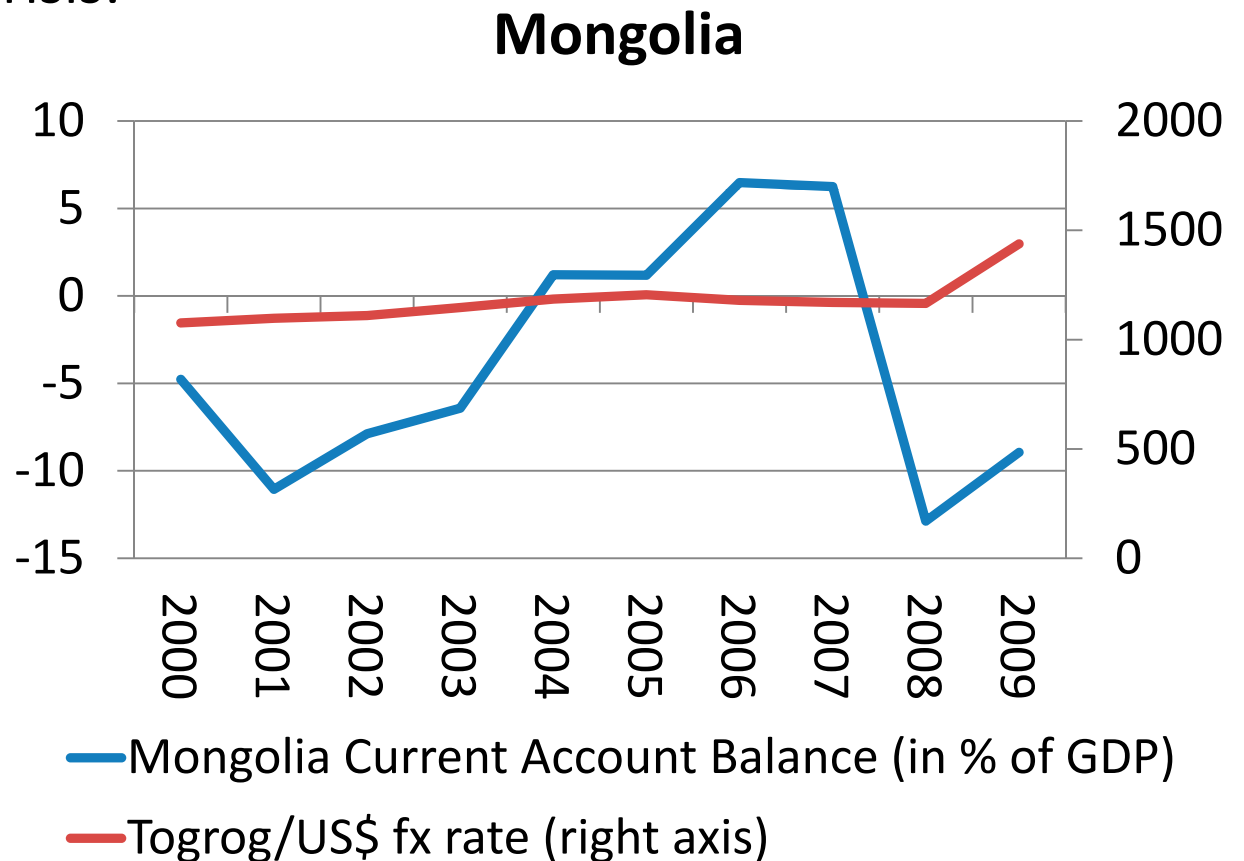


External Sector Considerations

External sustainability

Consider Mongolia crisis:

- Mongolia has large natural resource exports
- Current account surplus prior to crisis
- Sharp drop in international commodity prices during GFC led to current account and currency crisis

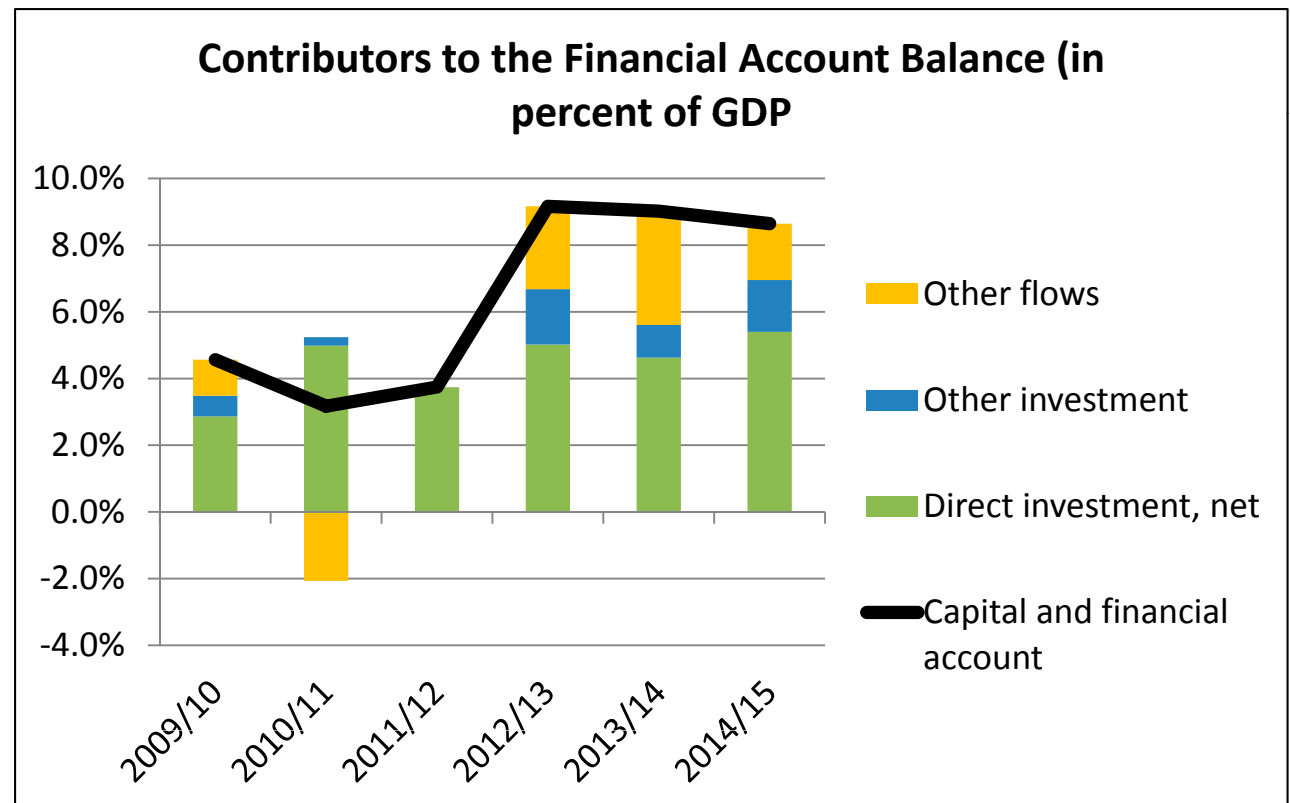


External Sector Considerations

External sustainability

Important factor for sustainability of current account deficits is how they are financed:

- Stable financing source lowers risk of crisis
- FDI is a fairly stable financing source
- This is (mostly) good news for Myanmar!



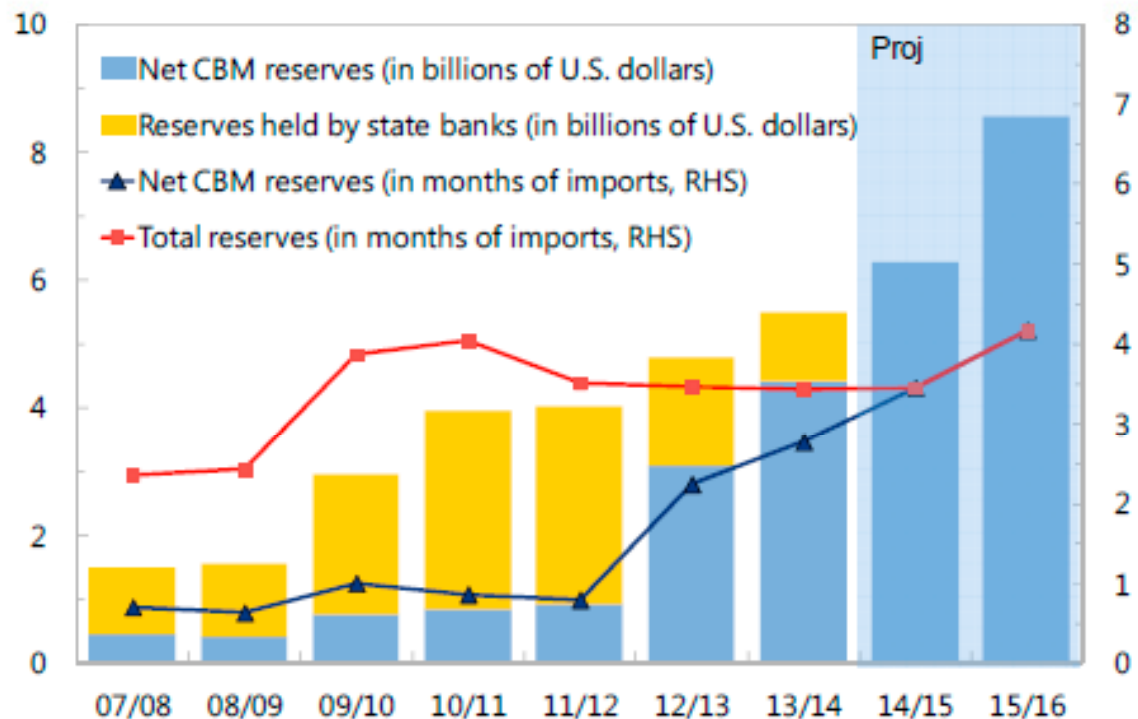
External Sector Considerations

External sustainability

Another important factor for sustainability of current account deficits is levels of foreign exchange reserves:

- They serve as a buffer in case of a crisis
- Does Myanmar have sufficient reserves?

Total and Net CBM Reserves



External Sector Considerations

Growth contribution

Large expansion of manufacturing sector was key driver of growth in Asia!

- Export-driven growth strategy
- Manufacturing-related FDI inflows
- External competitiveness is key for this strategy to work

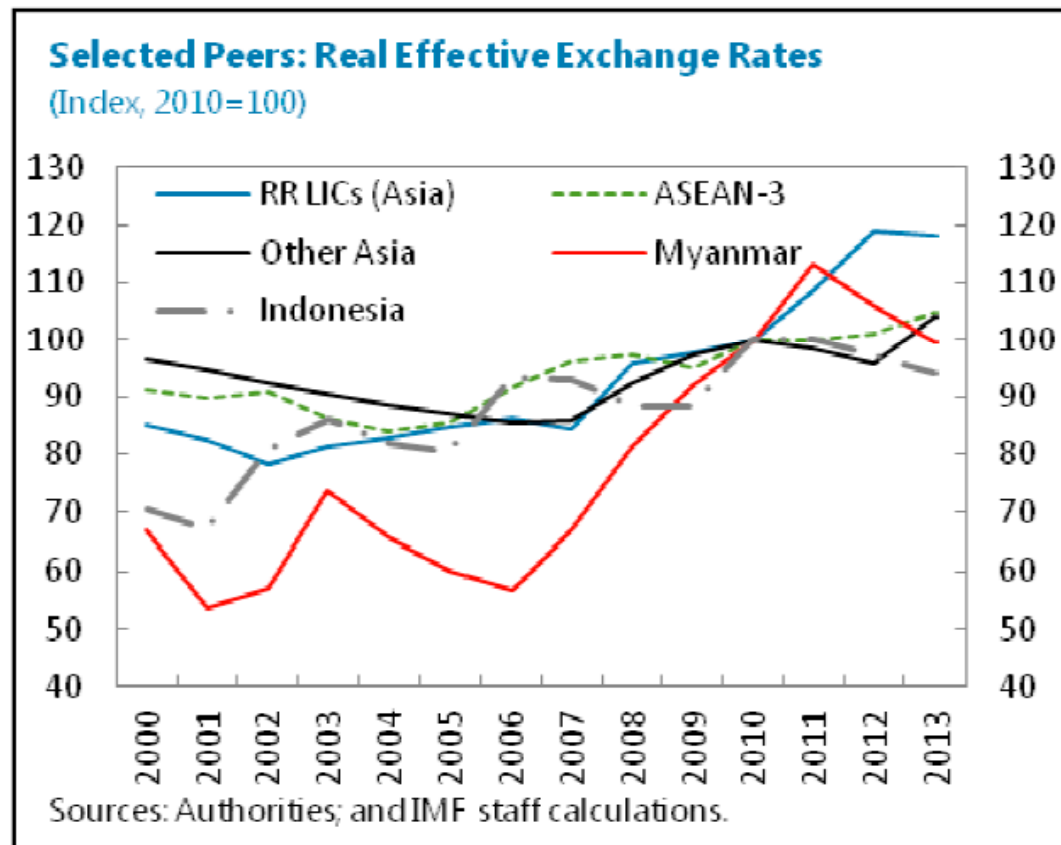


External Sector Considerations

Growth contribution

Real exchange is common indicator for external competitiveness

- Real appreciation undermines external competitiveness
- Is Myanmar's real appreciation since mid-2000s a problem?



Outlook

Next, we will explore in more detail ...

- ... the monetary sector, which helps with analyzing inflation and the exchange rate.