ECONOMIC REFORM AND GROWTH DYNAMICS DISCUSSION PAPER SERIES

In 2013 the United States Agency for International Development commissioned a set of discussion papers to review Myanmar's economic status, benchmark its performance relative to other countries, and identify priority policy reforms and institutional innovations to place the country on an inclusive growth path. This effort has been led by Nathan Associates under the Private Sector Development Activity and the ASEAN Connectivity through Trade and Investment Project.

Nathan Associates has a long history of providing economic analysis of the Myanmar economy. In 1953, Nathan Associates, along with Knappen, Tippetts, Abbett McCarthy, Stratton and Porter, Management, delivered to the U Nu Government an 8-year economic and social development program. Unfortunately, what the report called a "golden opportunity" for rapid growth was lost. The present set of discussion papers is designed to revive the initiative begun more than 60 years ago, providing a careful analysis of conditions in Myanmar and recommendations for delivering growth and prosperity to all of the people of the country.

USAID
FROM THE AMERICAN PEOPLE

BANKING AND FINANCE IN MYANMAR

PRESENT REALITIES, FUTURE POSSIBILITIES

JANUARY 2014
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In 2015, as Myanmar prepared for new elections, the United States Agency for International Development (USAID) commissioned a set of discussion papers to review Myanmar's economic status, benchmark its performance relative to other countries, and identify priority policy reforms, investments, and institutional innovations to re-establish the country on a new, inclusive growth path. This effort has been led by Nathan Associates under the Private Sector Development Activity (PSDA) and the Association of Southeast Asian Nations (ASEAN) Connectivity through Trade and Investment project Economic Reform through ASEAN Integration program.

Nathan Associates has a long history of providing economic analysis of the Myanmar economy. Originally headed by the economist Robert R. Nathan, who helped develop the United States' first national accounts in the U.S. Department of Commerce, Nathan Associates was founded in 1946 to provide applied economic analysis services to clients in the United States and around the globe and started working in Burma in 1951 at the request of the U Nu government. The latter sought "advice with respect to various important aspects of the country's economy and engineering problems and assistance in solving practical operating difficulties." Nathan Associates worked in Burma until 1959 with two U.S. engineering firms to deliver this advice, initially with funding from the U.S. Technical Cooperation Administration (a predecessor to USAID) and later with direct support from the Burmese government.

In 1953, Nathan Associates, along with the firms of Knappen Tippetts Abbett McCarthy Engineers and Pierce Management, delivered to the U Nu government an 8-year economic and social development program. The comprehensive plan, "Economic and Engineering Development of Burma," laid out a strategy of economic and administrative policies to stimulate growth in agriculture and irrigation, transportation, telecommunications, power, and industry, along with an analysis of the country's macroeconomic conditions. Unfortunately, what the report called a "golden opportunity" for rapid growth was lost, as many of the recommendations were set aside due to political developments in the late 1950s and early 1960s.

The present set of discussion papers is designed to revive the initiative begun more than 60 years ago, providing a careful analysis of conditions in Myanmar and recommendations on how the country can accelerate its integration into the global economy and deliver growth and prosperity to all of the people of the country.

Lynn Salinger, Principal Associate at Nathan Associates, has wled the design and implementation of the discussion paper series in collaboration with Steve Parker, Chief of Party of the Private Sector Development Activity, and Tim Buehrer, Chief of Party of the ASEAN Connectivity through Trade and Investment Project. Daniel Swift has supervised the effort from the U.S. Agency for International Development Mission to Burma.

LIST OF ACRONYMS

AGD	Asia Green Development Bank
AML	Anti-money laundering
ANZ	Australia and New Zealand Banking Group
APG	Asia/Pacific Group on Money Laundering
ASEAN	Association of Southeast Asian Nations
ATM	Automatic teller machine
AYB	Ayeyarwady Bank
CB	Co-operative Bank
CBM	Central Bank of Myanmar
CFT	Combatting the financing of terrorism
CHDB	Construction and Housing Development Bank
DFID	Department for International Development (U.K.)
FATF	Financial Action Task Force (OECD)
FDB	Farmers Development Bank
FIL	Financial Institutions Law
FIML	Financial Institutions of Myanmar Law
FIND	Financial Inclusion for National Development (World Bank)
FMI	First Myanmar Investment
FPB	First Private Bank
FRD	Financial Regulatory Department, Ministry of Finance
FY	Fiscal year
GDP	Gross domestic product
GIZ	*Deutsche Gesellschaft für Internationale Zusammenarbeit*
GoM	Government of Myanmar
GTB	Global Treasure Bank
IBSB	Insurance Business Supervisory Board
IFC	International Finance Corporation
IMF	International Monetary Fund
IT	Information technology
K	Myanmar kyat
KBZ	Kanbawza Bank
LIFT	Livelihoods and Food Security Trust Fund
MAB	Myanmar Apex Bank
MADB	Myanmar Agricultural Development Bank
MAP	Making Access Possible
MAPCO	Myanmar Agribusiness Public Corporation
MCB	Myanmar Citizens Bank
MEB	Myanmar Economic Bank
MEC	Myanmar Economic Corporation
MEHL	Myanmar Economic Holdings Limited
MFI	Microfinance institution
MFL	Microfinance Business Law
MFSP	Mobile financial service providers
MFTB	Myanmar Foreign Trade Bank
MICB	Myanmar Investment and Commercial Bank

MMB	Myanmar Microfinance Bank
MOB	Myanmar Oriental Bank
MP	Member of Parliament
MSEC	Myanmar Securities Exchange Center
MSLE	Myanmar Small Loans Enterprise
MUFJ	Mitsubishi UFJ
NBFI	Nonbank financial institution
NGO	Nongovernmental organization
NLD	National League for Democracy
OECD	Organization for Economic Cooperation and Development
PBUB	Peoples' Bank of the Union of Myanmar
PGMF	Pact Global Microfinance Fund
POS	Point-of-Sale
PSDA	Private Sector Development Activity
RDB	Rural Development Bank
REER	Real effective exchange rate
ROSCA	Rotating Credit and Savings Associations
S	Section
SAMB	State Agricultural Marketing Board
SDN	Specially Designated National
SEL	Securities Exchange Law
SEZ	Special economic zone
SLCM	Sohan Lal Commodity Management
SEE	State economic enterprise
SME	Small and medium enterprise
SPDC	State Peace and Development Council
TFB	Tun Foundation Bank
UAB	United Amara Bank
UNDP	United Nations Development Program
UOB	United Overseas Bank (Singapore)
USAID	United States Agency for International Development
USDP	Union Solidarity and Development Party
YSX	Yangon Stock Exchange

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1. INTRODUCTION

Mobilizing Myanmar's financial resources, while expanding financial inclusion, is an indispensable component of the country's reform process. Notwithstanding this widely aknowledged necessity, financial sector reform in Myanmar has been slow. Held back by inertia, the resistance of incumbent interests, and the sheer complexity of the task, only in the final year of the Thein Sein administration were the fundamentals of financial reform put on the agenda. As a result of this and given inevitable parliamentary and implementation delays, the real task of reinvigorating Myanmar's financial sector falls to the country's next government.

The purpose of this study is to assess the state of Myanmar's financial sector, identify the problem areas and chokepoints, and suggest ways forward. The paper draws on the latest thinking on financial sector reform as applicable to Myanmar's particular circumstances and history. The study offers practical recommendations Myanmar's monetary authorities can use now and in the future.

This study is divided into sections dealing with central banking, monetary, and exchange rate policy; the structure of Myanmar's banking sector; some individual bank profiles; the return of foreign banks to Myanmar; mobile banking and its possibilities; the new *Financial Institutions Law*; rural finance; informal financial services; microfinance; the return of cooperative credit; capital and financial market developments; and, finally, the return of private insurance companies to Myanmar. It concludes with recommendations.

2. CONTEXT

Myanmar's financial sector has historically involved much drama and not a little ruin. The subject of a crippling financial crisis in 2003, the universal nationalization of banks in the 1960s, and periodic episodes of currency demonetization, the sector began a fitful process of reform and recovery over the past decade. This accelerated during the Thein Sein administration, albeit fitfully and with many limitations, as this study demonstrates.

When viewed against widely used metrics for financial sector development, Myanmar continues to lag. Observing the overall context, the German development agency GIZ (*Deutsche Gesellschaft für Internationale Zusammenarbeit*) concludes that the "financial sector in Myanmar is the least developed of all countries in Southeast Asia and cannot adequately fulfill its role as a financial intermediary" (Foerch et al. 2015, 15). The World Economic Forum ranks Myanmar at 134 out of 144 countries in businesses' ability to access finance (Foerch et al. 2015, 11). Meanwhile, the 2016 edition of the World Bank's *Ease of Doing Business Index* celebrates Myanmar's improvement over its 2015 result (167 out of 189, compared with 177 out of 189 in 2015). And yet, the same survey reported a slippage in the ease of getting credit—from 171st to 174th place (World Bank 2015b).

The World Economic Forum ranks Myanmar at 134 out of 144 countries in businesses' ability to access finance.

Table 1 lists the total credit provided to the private sector (a key indicator of the contribution of a financial sector to economic development) in member countries of the Association of Southeast Asian Nations (ASEAN). Under the Thein Sein administration, growth in this metric has been strong. Growing by 50 percent a year in fiscal year (FY)2012/13 and FY2013/14, private sector credit expanded at a still relatively impressive 36 percent in FY2014/15 (World Bank 2015a, 20).[1] As these data indicate, even though Myanmar has experienced strong growth in this metric during the Thein Sein government, the country remains well behind its peers and neighbors—not just the six original ASEAN members, which are now largely middle-income, but even the poorer, new entrant, socialist-transition countries of Cambodia, Lao People's Democratic Republic, and Viet Nam.

[1] This growth probably decelerated during the second half of calendar year 2015, according to private briefings with various monetary authorities in Myanmar.

TABLE 1. PRIVATE SECTOR LENDING (% OF GDP) IN ASEAN COUNTRIES, 2015

ASEAN '6'	%	ASEAN (CLMV)	%
Brunei Darussalam	31	Myanmar	15
Indonesia	36	Laos	39
Philippines	36	Cambodia	45
Thailand	97	Viet Nam	97
Malaysia	134		
Singapore	173		

Source: Almekinders et al. (2015) and author's calculations

Meanwhile, and notwithstanding the shiny new bank shopfronts, automatic teller machines (ATMs), point-of-sale (POS) terminals, and all the other accoutrements of modern banking that have recently appeared, Myanmar's formal financial system is not *inclusive*. Data on financial inclusion are variable and unreliable, but it is highly plausible that no more than about 10 percent of Myanmar's population has a bank account, and only a few more have access to formal lending. Less than 3 percent of Myanmar's population has any type of formal insurance.[2]

In the absence of access to formal financial services, most people in Myanmar rely on the informal sector—for loans, to place savings, to make and receive remittances. According to Making Access Possible (MAP), a collaboration of a range of government and multilateral agencies, foreign donors, and founded by the United Nations Capital Development Fund (UNCDF), over 9 million people in Myanmar had loans from the informal credit sector in 2013, to a value of Myanmar kyat (K) 5.4 trillion (then equivalent to US$5.7 billion). This compared with K5 trillion in credit extended from the formal banking sector, spread among just 60,000 borrowers (MAP 2014, 8). The footprint of Myanmar's formal financial system is, in short, an extraordinarily narrow one.

The incapacity of Myanmar's financial system to sustain long-term finance—critical for capital formation and industrial transformation—is another indicator of the still-unresolved ills besetting the country's financial sector. Hemmed in by regulations that prohibit financial institutions from lending for anything but the short term and require abnormally high levels of collateral, almost no loans in Myanmar are for terms of more than one year and most are for less than six months. Long-term capital aggregation and allocation in Myanmar do not take place through the country's formal financial sector.

Unfortunately, matters at the other end of the scale—managing the short-term liquidity that sustains financial institutions day-to-day—are scarcely better realized. Liquidity management across the financial sector is poor and, as a consequence, liquidity crises and credit squeezes are routine. Of course, the periodic liquidity crises highlight a broader problem: the lack of real banking done by Myanmar's banks and their inability to undertake it. Restricted in the ways noted above, too many of Myanmar's banks are effectively little more than complex pawnshops and apply little but the most rudimentary credit analyses and other standard methodologies to their lending. As Myanmar's Minister of Finance put it, "Myanmar's existing banks are not yet fully matured in asset and liability management and liquidity forecasting" (Oxford Business Group 2014, 51).

It is highly plausible that no more than about 10 percent of Myanmar's population has a bank account, and only a few more have access to formal lending. Less than 3 percent of Myanmar's population has any type of formal insurance.

A related problem is that Myanmar's banks universally report very low levels of nonperforming (or compromised) loans. While this sounds like a virtue, the reported numbers are almost certainly the result of poor accounting and disclosure structures, rather than an unusually virtuous cohort of borrowers. In the place of hard information on this front, Myanmar's banking scene is constantly awash with rumors of failed and failing banks, to the great detriment of systemic stability.

Finance in rural Myanmar is in the worst state of all and constitutes perhaps the most critical problem of the country's financial sector.

Finance in rural Myanmar is in the worst state of all and constitutes perhaps the most critical problem of the country's financial sector. The international and historical narrative of financial capital providing the means for industrial transformation is familiar. Less understood is the way that financial access is transformative for agriculture. This is despite the fact that the phenomenal and much remarked-upon growth of the Asian "tigers" was first a story of great productivity gains in intensive, small-scale, household agriculture—and the finance that supported it. Accordingly, for this reason alone, it is critical to get rural finance in Myanmar right.

In recent years, great efforts have been made to reform Myanmar's financial sector. These efforts, led by a small core of reformers within the Thein Sein government—too often struggling against recalcitrant colleagues and vested interests—as well as by some especially innovative and energetic private enterprises, have been little short of heroic. Yet, it has not been enough and notwithstanding all the changes, Myanmar remains without the financial system it needs. The task of reforming and rehabilitating Myanmar's financial sector will thus fall to the new government led by the National League for Democracy (NLD) that will form in 2016.[3] This government will not start from scratch, but the road ahead will be as steep as it is promising.

A NOTE ON DATA

Data problems in Myanmar are the stuff of legend and, accordingly, much remarked upon. In recent years, political change in Myanmar, as well as international assistance from a host of agencies, has improved matters significantly. Nevertheless, problems and anomalies persist. This paper uses official data provided by the formal authorities in Myanmar, but augments these with data gathered from other sources (including the International Monetary Fund [IMF], World Bank, and other multilateral agencies) and interviews with key industry players. All data are subjected to what reason and experience suggest are plausible. Naturally, responsibility for the conclusions so reached by this process rests solely with the author.

[2] Such metrics are the consensus across the spectrum of studies of Myanmar's financial sector, including MAP 2014, MAP 2014b, World Bank 2014, Livelihoods and Food Security Trust Fund (LIFT) 2014.

[3] This paper was written before the NLD Government was formed.

3. CENTRAL BANKING IN MYANMAR

Although created in 1948 as a paragon of monetary orthodoxy, the Central Bank of Myanmar (CBM) has spent much of its existence as little more than a financing arm of the state.[4] Excessive government spending (much of it devoted to the military), deficient and dysfunctional taxation arrangements, and a general lack of understanding of the importance of monetary stability, created a context in which the CBM has enjoyed little control over its nominal responsibilities. Formally a unit of the Ministry of Finance and Revenue (hereafter, Ministry of Finance), it has traditionally not been close to being an independent institution. Table 2 below illustrates this role at the outset of the installation of the Thein Sein government. As can be seen from the data here, printing money for the state was the CBM's task at hand:

TABLE 2: CBM AS STATE FINANCIER (2005-2011)

Financial Year	Central Bank Lending to Government	Government Treasury Bonds Outstanding
2005/06	2,165	79
2006/07	2,763	118
2007/08	3,534	180
2008/09	3,881	298
2009/10	4,727	896
2010/11	6,021	1,311

Source: Myanmar Central Statistical Organization

[4] Starting its existence as a converted "currency board," the then Union Bank of Burma (as the central bank was once named) could hardly have had a more orthodox pedigree. Such orthodoxy did not take long to be dissipated. For more on Myanmar's monetary and banking history, see Turnell (2009).

INDEPENDENCE AND THE 2013 CENTRAL BANK LAW

Perhaps the biggest single legislative reform enacted by the Thein Sein administration in the context of the financial sector was the promulgation of a new *Central Bank of Myanmar Law.* This law, which came into effect in July 2013, is designed to establish the legal independence of the CBM and, of perhaps even greater importance, the perception of such independence within and outside the country. The 1990 *Central Bank Law* contained many of the technical aspirations and methodologies of international-standard central banking (few of which were ever implemented), but lacked the now standard notion of independence.[5]

The core of the 2013 *Central Bank Law* (CBL) consists of a number of measures that assert the CBM's autonomy from the Ministry of Finance and its spendthrift past. The governor of the CBM is elevated to the level of a minister of the cabinet (CBL, section [s] 108). An initial plan to make the CBM even more independent of the government by making the institution a Union-level body, similar in status to the Auditor General's Office (part of the executive branch of government, but apart from cabinet), was shelved, as it would have required constitutional amendment.

Under the new law a board of directors is the CBM's ultimate internal decision-making body. It has nine members and is chaired by the governor of the CBM. Four of these (the governor and three newly-created deputy governor positions) come from within the CBM itself, the other five being "external professional experts selected by the government" and approved by the parliament (CBL, s 9). Directors cannot be members of parliament or a political party, nor can they hold more than 5 percent equity in a corporation (CBL, s 10). The expertise of the five external directors must be in operational areas of central banking: economics, finance, banking law, accounting, and/or auditing. The deputy ministers of the ministries of Finance and National Planning and Economic Development are permitted to attend the monthly meetings of the Board but (in theory) are not allowed to take part in its deliberations (CBL, s 21e).

The governor and deputy governors of the CBM enjoy a degree of security of tenure. Their appointments, made by the president but requiring parliamentary approval, can be terminated only on the basis of voluntary resignation; breaches of the appointment requirements (being convicted of a crime occasioning imprisonment or acquiring equity ownership in excess of the 5 percent limit); missing more than three consecutive board meetings; or being the subject of a presidential finding that they are incapable of discharging their duties. The term of office for the governor of the CBM is five years, and that of directors is four years. Both the governor and directors can serve only two terms (CBL, s 9b).

Security of tenure is important in granting senior officers and directors of the CBM the confidence to act independently of the government. As noted, the *Central Bank Law* contains provisions for delivering such security, but these are uncertain and incomplete. It is, for instance, unclear whether the removal of senior staff or CBM directors requires parliamentary approval, just as it is uncertain whether the same pertains to a presidential finding that a director is incapable of discharging duties. In this area alone, the role of the president is unilateral and unchallengeable—and thus somewhat problematic for the notion of credibly establishing perceptions that the CBM is genuinely independent of the President's office.

The CBM is authorized under the *Central Bank Law* to conduct what is commonly known as open market operations: buying and selling financial securities to influence monetary conditions (CBL, s 45). Myanmar, however, does not yet possess the active secondary markets in securities that would allow these operations. Instead, the CBM conducts deposit and credit auctions.

In modern central banking practice, transparency and accountability are meant to be the natural accompaniment of independence. Under the 2013 *Central Bank Law*, the CBM is compelled to submit reports on monetary conditions to parliament at least twice a year, and to publish quarterly reports on monetary developments (CBL, s 38–39). Thus far it has fallen short in this.[6]

Monetary Policy Instruments

To perform its monetary policy duties, the CBM is authorized under the *Central Bank Law* to conduct what is commonly known as open market operations: buying and selling financial securities to influence monetary conditions (CBL, s 45). Myanmar, however, does not yet possess the active secondary markets in securities that would allow these operations. Instead, the CBM conducts deposit and credit auctions. So far these are really only useful for sterilizing the CBM's buying and selling in the foreign exchange market (to stabilize the kyat) rather than in influencing broader monetary conditions, which are affected more by the floors and caps the CBM imposes on the interest rates that banks pay and charge (more below). A key insight into the conduct of monetary policy around the world is that transparency and openness in open market operations can assist central banks in achieving their objectives by shaping market expectations. This is recognized in the *Central Bank Law* (CBL, s 46), which asserts that the CBM will "announce to the public" its dealings in financial markets for policy ends. The same section of the *Central Bank Law* seeks to clarify the uses of minimum bank reserves for policy purposes.

Other Implications of the New Central Bank Law

In conjunction with the CBM's greater responsibilities and powers, four new policy committees have been established within the CBM. These are concerned with monetary policy, financial stability, payments systems, and foreign exchange management.[7] How much power these committees wield, and how they mesh with the responsibilities of the three new deputy governors is, as yet, unclear. As will be seen later in the context of Myanmar's practice of exchange rate policy in recent times, in this area opacity reigns.

[5] The former *Central Bank of Myanmar Law* No. 15/1990 was automatically repealed upon the promulgation of the new law (CBL, s 118). The new law states that "rules, regulations, bylaws, orders and directives made or issued under the repealed Bank Law … or under any other power shall, in so far as they are not contradictory to the provision of this [new] law, continue to have effect" (CBL, s 119). The practical impact of this provision remains to be seen.

[6] The latest annual report available on the CBM's website, for instance, is for fiscal year 2011/12.

[7] Staff numbers at the CBM are also expected to double over the next few years, to over 2,000 across its three offices in Nay Pyi Taw, Yangon, and Mandalay.

Given Myanmar's unfortunate history of periodic demonetization episodes, the 2008 Constitution includes a guarantee "not to demonetize currency legally in circulation" (Constitution, s 36e).[8] This is reinforced in the 2013 *Central Bank Law*, which includes the assurance that any "necessary" withdrawals of currency notes in circulation take place only with the approval of the parliament (CBL, s 67a).

EVALUATING THE CBM'S AUTONOMY

Of course, achieving effective independence for the CBM depends on much more than its governing law and internal appointment and dismissal procedures. Above all, its ability to break away from its hitherto primary role of financing the state will be critical.

What is the outcome thus far on this aspect?

As with so much else on the reform front in Myanmar, the answer is some progress, with much still to be done. As Table 3 reveals, and as the IMF notes in its latest (2015) Article IV Report, the CBM remains the primary vehicle for funding Myanmar's budget deficits.

TABLE 3: CBM AS STATE FINANCIER: THEIN SEIN ADMINISTRATION

Financial Year	Central Bank Lending to Government	Government Treasury Bonds Outstanding
2011/12	7,673	1,817
2012/13	8,318	2,487
2013/14	8,726	2,804
2014/15	10,126	2,900

Source: Myanmar Central Statistical Organization

Such "money financing" of Myanmar's budget deficits amounted in FY2014/15 to around 2.2 percent of gross domestic product (GDP). This, in turn, has led to rapid growth in reserve money in Myanmar which, according to the IMF (2015, 31) grew by over 11 percent in FY2014/15 and was projected to expand a further 18 percent in FY2015/16.

This effectively "loose" monetary policy of the CBM has consequences, especially for inflation. In the aforementioned Article IV report, the IMF was especially pessimistic, suggesting that Myanmar's economy was simultaneously in danger of overheating and that the "downside risks to growth and stability in the near term" had increased (IMF 2015, 5). Putting some numbers to these troubling indicators, the IMF estimated that inflation will rise to 13 percent by the end of FY2015/16 (far above that of peer countries), the current account deficit will widen to 9 percent of GDP, and the CBM's foreign reserves will decline to just less than 2½ months of import coverage. The latter problem is already distorting decision-making within the CBM, as will be shown later in this report.

[8] Myanmar has experienced three "demonetization" episodes over the last 50 years, the most bizarre of which included the replacement of decimal currency notes with a series based upon the number nine. For more on these, see Turnell (2009).

Despite the rising yields, large and persistent disparities remain between the CBM's "liquidity-mopping" objectives, and the outcomes achieved.

Monetary Policy

The CBM's longstanding role as the default financier of state spending remains, absent significant fiscal reform, the most important barrier to conducting appropriate monetary policy in Myanmar. But it is not the only one. Notwithstanding the reforms of recent years, the country remains without the fundamental institutions, instruments, and infrastructure necessary for a truly market-based policy framework. Interest rates are fixed without consideration of market conditions, interbank and money markets scarcely exist, CBM lending to the banks is too readily available, and the country lacks the reliable government debt instruments that would provide the means for the conduct of open market operations. All these issues are explored in more detail later in this study. Of course, making monetary policy management all the harder is Myanmar's historical legacy of monetary instability, arbitrary policymaking, and a broad, profound mistrust in monetary institutions.

As noted earlier, in the absence of functioning government debt markets within which to conduct open market operations, Myanmar has attempted to use another, potentially useful mechanism. This takes the form of deposit auctions conducted by the CBM, and by which it can in theory drain liquidity from the banking system or inject funds into it. Thus far the deposit auctions have not really succeeded, however. The rates offered by the CBM have been too low to attract loose liquidity from the banks when the system is in surplus, while efforts to use the auctions to augment liquidity when conditions become tight are undermined by too easy (and cheap) recourse to the CBM's discount window (IMF 2015, 8-9). The CBM publishes the results of the auctions on its website, but the data reveal the very large gap between deposit auction offers and the amounts subsequently purchased at those auctions. Table 4 presents a month-end sample of deposit auctions over the past year. Despite the rising yields, large and persistent disparities remain between the CBM's "liquidity-mopping" objectives, and the outcomes achieved.

TABLE 4: CBM DEPOSIT AUCTION OUTCOMES[9]

Month	CBM Offer Kyat millions	Range of Bid Yields Accepted (%)	Deposit Volumes Kyat millions	Bids Accepted/ CBM Deposits on Offer (%)
Dec 2014	80,000	4.00-4.00	20,050	25.0
Jan 2015	80,000	4.48-5.00	25,000	31.3
Feb 2015	215,000	4.4-4.5	40,000	18.6
Mar 2015	197,000	3.35-3.5	100,000	40.8
Apr 2015	434,000	3.4-5.5	5,000	11.5
May 2015	240,000	3.5-4.5	100,000	41.7
June 2015	200,000	5.65-5.8	50,000	25.0
July 2015	300,000	6.3-6.5	135,000	45.0
Aug 2015	385,000	6.85-7.00	100,000	26.0
Sept 2015	250,000	6.85-7.00	100,000	40.0
Oct 2015	380,000	7.00-7.00	3,000	0.8

Note: Presented here is a sample of the auctions held in each period, selected as close as possible to the end of each month. "Bids accepted" percentages are the author's calculations.

Source: Central Bank of Myanmar

Progress has been made on the monetary policy front in Myanmar under the Thein Sein administration. Central is the already-discussed granting of a degree of independence to the CBM and its revitalization through some key personnel appointments. Likewise, there has been some movement toward creating the "missing" monetary institutions and market infrastructure. Nevertheless, much remains to be done if Myanmar is to enjoy the monetary and financial stability the country needs to support its economic transformation. Necessary reforms to such institutions and instruments are outlined in recommendations at the end of this study.

EXCHANGE RATE REFORMS

A year before the 2013 *Central Bank Law* was promulgated, Myanmar's exchange rate arrangements were revolutionized by the government's decision in April 2012 to allow the foreign exchange value of the kyat to be determined through a managed float. Myanmar's previous dual exchange rate system—with an official rate that set the kyat at around K6:US$1, compared with an unofficial market rate that mostly fluctuated around K1,000:US$1—had long been the most public symbol of the country's economic idiosyncrasies.

Under the new arrangements, an auction is held each morning among Myanmar's commercial banks to determine a reference rate for the kyat against the U.S. dollar, the euro, and the Singapore dollar. Once the reference rate is set, banks and money changers can then exchange the kyat within a band of +/-0.8 percent above or below the reference rate.

The new exchange rate arrangements met with near-universal acclaim, and were long regarded as the signature economic reform of the Thein Sein administration. Moreover, for the first year or so after the change, matters ran relatively smoothly. Indeed, to the extent that there were complaints over the new arrangements, they mainly centered upon the kyat's appreciation across FY2012/13, driven notably by the broad international enthusiasm for Myanmar's reform narrative and the country's economic potential. However, as it turned out, the new system had some underlying technical problems, not least of which was the delayed emergence of a functioning interbank market for foreign exchange—a delay that simultaneously kept the role of the CBM artificially central to the whole system of determining the exchange rate, while also continuing to provide space for an informal foreign exchange market and an accompanying shadow rate for the kyat.

In late 2014 affairs started to go further awry. Reversing the earlier trend, the kyat began what soon turned into a rapid and sustained decline against the U.S. dollar. By late 2015 this decline was on the order of 20 percent or so, leading to something of a misguided panic in some quarters in Myanmar. In fact, much of the "fall" of the kyat could have been better expressed as a rise in the value of the U.S. dollar, a global phenomenon most apparent in the relative decline in the exchange rates of most commodity-producing and transition countries.

Instead of accepting and explaining this decline, however, Myanmar's monetary authorities (including the CBM, within which, however, opinion was not at all unanimous) joined in the broader anxiety. Accordingly, instead of letting the kyat fall to an exchange rate that brought kyat demand and supply into balance, the authorities intervened and sought to prop up the reference rate of the kyat by allocating it at the auction according to the amount bid, rather than at an equilibrating price. From then on, the authorities implicitly defended a quasi-official exchange rate of around K1,105:US$1 (as against a market price then of around K1,267:US$1). This artificially created an excess demand for U.S. dollars over supply, leading to shortages of that currency and the imposition of restrictions on quantities of dollars that could be withdrawn from banks (not to exceed US$5,000 per transaction, with a maximum of two transactions per week).

These restrictions applied even to designated foreign currency accounts, and to both individuals as well as large corporations—the latter leading to significant difficulties for foreign firms in meeting payroll and other routine payments. Other administrative controls were placed on access to foreign exchange, while the parliament directed the CBM to investigate whether domestic private banks were hoarding U.S. dollars. Remarks by the speaker of the lower house of the parliament also led to suspicions about the two foreign telecommunications firms (Telenor and Ooredoo). The speaker implicitly accused the two firms of draining

[9] Central Bank of Myanmar, "Results of Deposit Auction," http://www.cbm.gov.mm/deposit-auction, (accessed November 5, 2015).

Myanmar of U.S. dollars through repatriation of profits and other funds. Such accusations played to what might be regarded as traditional suspicions of "foreign finance" in Myanmar. The companies vigorously denied the allegations.[10]

Meanwhile, a black market for foreign currency was reenergized and an informal exchange rate emerged at growing variance to the quasi-official rate, peaking in July 2015 when the informal U.S. dollar rate was 16 percent higher than the quasi-official rate. Speculators, notably including Myanmar's private banks, poured into this market. Unwilling and often unable to buy or sell foreign currencies at the new, official exchange rate, many banks bought and sold from and into this unofficial market. Commenting on the issue later, the chair of Kanbawza Bank took umbrage at the term "black market" that had been used in describing the practice:

> They call it the black market, but it's the real market. It's very difficult for banks to follow the rules.[11]

An official at the CBM said anonymously:

> We deliberately made our currency appreciate, while there was an actual depreciation happening. The whole informal market re-emerged, no transactions were happening through the banks any more. That's when we came to the brink of collapse.[12]

Finally, the CBM, supported in the background by a number of multilateral agencies, reversed its nascent efforts to set a particular kyat rate. Averting the mini-crisis for the time being, the CBM said in public statements that it would henceforth amend the reference rate

> …in line with the market price …in order not to have multiple exchange rates for foreign currency.…Now we have decided to let the FX auction discover the market price so that our reference rate will reflect the market prevailing rate.[13]

The post-July 2015 calm lasted a few months, until ever-growing concerns over the dollarization of Myanmar's economy brought about a new set of restrictive measures in mid-October 2015. The CBM suddenly revoked the foreign exchange licenses of hundreds of businesses in Myanmar including hotels, restaurants, telecommunications companies ("telcos"), supermarkets and other retail outlets—close to all nonbank license holders. As it turned out, the revocation applied just to businesses' acceptance of payments in physical foreign currency. The CBM said that the cancellation of the licenses, with all to be revoked within days of the announcement, was "intended to promote the use of the kyat in making payments for goods and services within the country and to cut down the use of cash by encouraging domestic debit cards and credit cards, internal payment cards, and on-line payment system."[14] The CBM's statement was a curious one—not least because it was almost impossible to imagine that domestic credit and debit cards were a substitute for U.S. dollar payments, especially among enterprises heavily engaged with international tourists.

Put simply, and as it presently stands, the CBM's internal culture is not conducive to modern central banking. Expertise in the CBM is overwhelmingly organized along the lines of the command-and-control frameworks of the past, while many of the staff are conservative and resist change.

The reasons behind these CBM actions have been difficult to fathom. Dollarization is a potentially real problem in Myanmar, especially for a central bank anxious to establish its monetary and regulatory authority across a sector with multiple circulating currencies. Nevertheless, the arbitrary nature of these decisions and their erratic timing did little but remind people, within Myanmar and outside, of the country's unstable monetary past.

The hand of powerful government figures in this episode cannot be discounted. Nevertheless, it also reveals some deep-seated problems within the CBM itself, notwithstanding that inside its walls are some dedicated and highly skilled reformers. Put simply, and as it presently stands, the CBM's internal culture is not conducive to modern central banking. Expertise in the CBM is overwhelmingly organized along the lines of the command-and-control frameworks of the past, while many of the staff are conservative and resist change. Even though teams of foreign experts work inside the CBM (from the IMF, certain Japanese development and monetary agencies, GIZ, and the Bank of Thailand), interactions between them and local staff are limited and primarily formal.[15] Significant cohorts within the CBM have a degree of hostility to foreign advice; accordingly, in many areas lip-service rather than implementation is a common response to suggested reform.

Similarly undermining reform within the CBM is the degree to which it is factionalized, functionally and in other ways, and decisions are made in what are in effect intellectual and policy-making silos. The new *Financial Institutions Law of Myanmar*, for example, remained unknown to the CBM's Supervision Department, the department most affected by the law, until after it was presented to a parliamentary committee.

Under the Thein Sein administration *de jure* reform of the CBM made substantial progress. For *de facto* change, Myanmar must await new hands at the wheel.

[10] For these controversies, see Clare Hammond, "Telecom Operators Set the Record Straight on USD Flows," *Myanmar Times*, July 30, 2015, http://www.mmtimes.com/index.php/business/technology/15758-telecom-operators-set-the-record-straight-on-usd-flows.html, (accessed November 2, 2015).

[11] Cited in Antoni Slodkowski and Simon Webb, "Return of the Dollar Black Market Shows Limits of Myanmar's Reforms," *Reuters*, October 19, 2015, http://www.reuters.com/article/2015/10/20/us-myanmar-dollars-insight-idUSKCN0SD2E020151020, (accessed October 21, 2015).

[12] Ibid.

[13] CBM official cited in Clare Hammond, Aye Thidar Kyaw, and Jeremy Mullins, "Central Bank's Kyat Rate Jumps," *Myanmar Times*, July 14, 2015, http://www.mmtimes.com/index.php/business/15487-central-bank-s-kyat-rate-jumps.html, (accessed October 23, 2015).

[14] Aung Hla Htun, "Myanmar Revokes Forex Licences to Control 'Dollarization,'" *Reuters*, October 18, 2015, http://www.reuters.com/article/2015/10/18/myanmar-forex-idUSL3N12I04K20151018, (accessed October 19, 2015).

[15] This does not, however, stop the advice of foreigners being used within the CBM in various turf battles.

4. STRUCTURE OF MYANMAR'S BANKING SECTOR

As befits a country in transition, the structure of Myanmar's banking system is a hybrid bearing all the marks of past upheavals and new trajectories. Consisting of a quartet of fully state-owned policy banks, a gaggle of banks in which state actors play a controlling role, a dozen private banks of varying quality and energy levels and, finally, nine new foreign banks (Table 5), the system is both familiar and tailored to Myanmar's unusually turbulent financial history.

TABLE 5: THE BANKS IN MYANMAR

State-Owned Banks	Semiprivate Banks*	Private Banks	Foreign Banks
Myanmar Agricultural Development Bank	Gems and Minerals Development Bank**	Asia Green Development Bank	Australia and New Zealand Banking Group
Myanmar Economic Bank	Global Treasure Bank	Asia Yangon International Bank	Bangkok Bank (Thailand)
Myanmar Foreign Trade Bank	Innwa Bank***	Ayeyarwady Bank	Bank of Tokyo-Mitsubishi UFJ (Japan)
Myanmar Investment and Commercial Bank	Myanmar Citizens Bank	Co-operative Bank	Industrial and Commercial Bank of China
	Myanmar Construction and Housing Development Bank	Farmers Development Bank**	Malayan Banking Berhard (Maybank, Malaysia)
	Myanmar Microfinance Bank	First Private Bank	Mizuho Bank (Japan)
	Myanmar Tourism Bank**	Kanbawza Bank	Overseas Chinese Banking Corp. (Singapore)
	Myawaddy Bank***	Myanmar Apex Bank	Sumitomo Mitsui Banking Corp. (Japan)
	Nay Pyi Taw Sibin Bank	Myanmar Oriental Bank	United Overseas Bank (UOB, Singapore)
	Rural Development Bank	Shwe Rural and Urban Development Bank	
	Small and Medium Industrial Development Bank	Tun Foundation Bank	
	Yadanabon Bank	United Amara Bank	
	Yangon City Bank	Yoma Bank	

** Includes ministerial, municipal, military, and other banks with significant government ownership, but trading as commercial banks.*

*** Not yet in operation*

**** Military-owned bank*

SUPERVISION AND REGULATION

Formally the CBM has long adhered to the international standard for bank supervision known as the Basel Accords. Historically, however, bank regulation and supervision in Myanmar have been ad hoc, reactive, and opaque. Under Myanmar's previous military regimes the Basel Accords were given lip service but then largely ignored. The 2013 *Central Bank of Myanmar Law* reinforces the CBM's role as sector supervisor, giving it broad-ranging powers (CBL, s 68–75) in "regulating financial institutions for the stability of the monetary system…." Given the past, however, clearly implementation will be key.

The problems of implementation thus duly noted, as matters presently stand, the CBM is meant to hold the country's banks to an expanded version of the broad Basel framework. An important part of this are the following prudential standards that all banks supervised by the CBM must formally meet. (The list is followed by a comparison in Table 6 with ratios elsewhere.)

- Minimum capital adequacy ratio of 10 percent of risk-weighted assets
- Liquidity ratio (liquid assets to current liabilities) of a minimum of 20 percent
- Single borrower exposure limit of 20 percent of capital and reserves
- General provision against bad and doubtful debts of 2 percent of loan portfolio
- Reserves to deposits ratio (in the form of cash balances with the CBM) of 5 percent
- Minimum K30 billion of paid-up capital if engaged in both domestic and foreign exchange banking
- Maximum 10 percent equity holding in any nonfinancial institution
- Capital-to-deposits ratio of 4 percent

TABLE 6: COMPARING MYANMAR'S PRUDENTIAL RATIOS [16]

Prudential Regulation	Myanmar	Viet Nam	India	Indonesia
Capital Adequacy Ratio	10%	9%	9%	8%
Liquidity Ratio	20%	15%	25%	n.a
Lending to Single Entity	20%	15%	15%	20%
Reserves Requirement	10% of deposits with the CBM	Yes, but discretionary upon individual banks	4%	n.a

Source: Organization for Economic Cooperation and Development (OECD) (2014)

[16] Table derived from a number of sources, including *Financial Institutions of Myanmar Law*, a similar table in OECD (2014, p.198), and the website of the State Bank of Viet Nam, http://www.sbv.gov.vn, (accessed November 5, 2015).

An additional array of enmeshing regulations have impaired the ability of Myanmar's banks to perform financial intermediation of the standard variety. The most obvious of these are the interest rate ceilings and floors set by the CBM.

Bank supervision is supposed to entail on-site inspections by the CBM and provision of data, including daily, weekly, monthly, and annual reporting of critical prudential metrics, from banks to the CBM. Some of this reporting is also meant to be public, but few of Myanmar's banks make even annual reports publicly available. Bank auditors must be appointed with the CBM's approval and are accountable both to the Central Bank and the commissioning bank.

The bank regulations examined thus far are more or less in line with international standards, even if imperfectly implemented, and roughly supportive of prudent, functional banking. Significantly, however, an additional array of enmeshing regulations have impaired the ability of Myanmar's banks to perform financial intermediation of the standard variety. The most obvious of these are the interest rate ceilings and floors set by the CBM. These determine that the private banks in Myanmar must pay 8 percent on deposits and charge no more than 13 percent on loans. Such rates are often below Myanmar's high and volatile inflation rates, rendering the returns to both savers and the banks themselves negative in real terms. Financial "repression"—resulting in the volumes of both savings and loans being lower than they would otherwise be—is just one consequence of the caps and floors on interest rates. Interestingly, the prescribed bank deposit rate as of early 2016 is lower than that of the minimum rate payable on Myanmar's treasury bonds, which is one reason for the relative increase in attractiveness of these instruments among local investors in recent times.

Other inhibiting, and prudentially unnecessary, restrictions include:[17]

- A prohibition on private banks lending to farmers and cultivators;[18]
- A ban on banks' lending for terms of more than one year;
- A cap on aggregate bank lending of 80 percent of the deposit base;
- A ban on granting uncollateralized loans[19] (currently all loans must be backed by urban land, a fixed deposit account or government bonds, machinery, gold, or a limited range of agricultural commodities);
- Excessive requirements on collateral *margins*: with the exception of a deposit account, which must exactly match the size of a loan, all collateral items must have a value in excess of 200 percent of loan value; and

[17] While many of these restrictions are not clear-cut prohibitions, the many CBM "instructions" and "directives" serve to inhibit nearly completely many practices. For instance, certain CBM instructions seem to suggest that long-term loans can be made, if funded by long-term deposits. Others imply loans beyond one year are prohibited generally. Likewise, the instructions dictating the interest rate cap and floor are contradicted by instructions on hire purchase products (near universally not offered in practice) that allow an annual 15 percent interest charge. There is a plethora of other similar examples.

"Hire purchase" refers to an arrangement whereby a purchaser pays for a good over a number of periods. In the United States and Canada, a hire purchase is referred to as an installment plan, although under a hire purchase ownership remains with the seller until the last payment is made, whereas under an installment plan the purchaser takes ownership immediately.

[18] Except Global Treasure Bank and Rural Development Bank.

[19] The 1990 *Financial Institutions of Myanmar Law* allowed uncollateralized loans, but following the 2003 banking crisis, collateral-backed loans only have been permitted. The CBM has apparently told banks that uncollateralized lending will be permitted once a credit bureau is established.

- A ban on private banks paying interest on foreign currency deposits (at present only state-owned banks are allowed to pay interest on such accounts).

As shall be examined later, these regulations on Myanmar's banks have a number of deleterious effects. The collateral requirements are especially damaging, not least in conforming to a banking culture already disposed to focus on collateral valuation rather than credit and business analysis. Regarding banks' capabilities in credit and business analysis, some industry players are blunt. According to a senior executive of one of the major private banks, most of Myanmar's banks are "clueless" when it comes to credit assessment—as opposed to valuing collateral, in which their skills "are up there with the pawnshops."[20] The basic credit product available to business in Myanmar is an overdraft secured by collateral, which overwhelmingly is urban land. Naturally, this precludes most small- and medium-sized enterprises (SMEs) from the financing considerations of banks. According to surveys collated by the Organization for Economic Cooperation and Development (OECD) (2014, 193), the vast majority (64 percent) of enterprises of all sizes and sectors in Myanmar had neither borrowed from a bank nor sought to do so because of an array of perceived insurmountable obstacles, listed here in order of seriousness of the obstacles concerned:[21]

- Collateral requirements too inflexible 34%;
- Loan procedures too complex 28%;
- Loan term too short 28%;
- Interest rate too high 27%.

Similarly, the regulatory constraints facing Myanmar's banks produce other unorthodox outcomes, especially when combined with other problematic aspects of Myanmar's political economy. For instance, the lack of a properly functioning legal process through which banks might seek to foreclose on the land of defaulting borrowers often leads banks to insist that property be placed in their name at the outset of a loan. Should there be default, no court process is thus needed for the bank to claim the asset. In the meantime, however, the ability of borrowing firms and individuals to pursue their interests based on their true asset/capital position is clearly impaired.

Meanwhile, the regulations noted above apply to the private and semiprivate banks, but only incompletely to those wholly owned by the state. Among the latter cohort, the Myanmar Agricultural Development Bank sits under the Ministry of Agriculture and is not required to meet the CBM's regulations. With respect to the other state-owned banks (which are now formally supervised by the Financial Regulatory Department (FRD) of the Ministry of Finance—also the regulator for microfinance and insurance), certain regulations are meant to apply (most concerned with loan size, term, interest charges, and borrower attributes), but these do not include capital or other prudential metrics.

The lack of a properly functioning legal process through which banks might seek to foreclose on the land of defaulting borrowers often leads banks to insist that property be placed in their name at the outset of a loan.

[20] Private conversation with the author, 2015.

[21] Other issues included perceptions that banks did not understand business financing; disclosure requirements were too stringent; banks delivered poor customer service; difficulties in providing necessary financial information; and an acknowledged failure of businesses themselves to know how to access banking services. Actual data supplied by the OECD at http://dx.doi.org/10.1787/888893134787, (accessed August 22, 2015).

These changes have been sufficient to drive the increases in private bank lending and deposit mobilization highlighted elsewhere in this study, and are indicative of the great potential that could be harnessed quickly given substantial reform.

REFORMS AND INITIATIVES

Necessary major legislative change to reform Myanmar's banking system has only just come to pass. As shall be examined in more detail below, a new bill to undertake this necessary reform—the *Financial Institutions Law* (FIL) was placed in the Bank and Financial Affairs Development Committee of Myanmar's parliament in late 2014, sparking a highly divisive debate. It did not emerge from the committee before the parliament concluded ahead of Myanmar's elections, but it appeared again—and was passed—in the post-election, lame duck parliament in late November 2015.

Because of the delays in passing the FIL, the transformation of Myanmar's banking system, and especially the bringing of its supervisory and regulatory framework up to the norms of a modern financial system, has not taken place. This is cause for much regret. Progress has been made around the edges of reforming Myanmar's financial sector, but these advances have not been sufficient to create financial intermediation of the sort that can create and allocate the capital the sector needs for genuinely transformational growth.

Nevertheless, changes have been made to some of the strictures on Myanmar's banks, and their modes of operations, such that in appearance, and partly in reality, they are different institutions than they once were. These changes have been sufficient to drive the increases in private bank lending and deposit mobilization highlighted elsewhere in this study, and are indicative of the great potential that could be harnessed quickly given substantial reform.

Changes made during the Thein Sein administration (usually through CBM regulatory notifications) include:

- Eliminating the requirement that banks raise stand-alone capital and seek approval for the opening of each new bank branch.
- Reducing the long-standing minimum capital-to-deposits ratio requirement on banks from 1:10 to 1:25. The 1:10 requirement, which was implemented in the wake of Myanmar's devastating 2003 banking crisis to limit the amount of leverage that banks took on, had become a substantial barrier to mobilization of deposits.
- Expanding the list of allowable loan collateral to include—in addition to urban land—gold and a small range of agricultural commodities. In practice, however, Myanmar's banks usually still insist upon land as loan collateral.
- Creating a national deposit insurance program. Centered on a state-owned insurance company (Myanmar Insurance), this voluntary program for all banks is meant to cover a maximum of K500,000 (about US$400) per borrower. Banks pay Myanmar Insurance a premium of 0.25 percent of deposits covered. Although 17 of Myanmar's private banks are said to have taken up the insurance initially, not all have continued with it. According to some of Myanmar's bankers, the level of residual distrust in the country's formal financial sector is such that an insurance scheme would do little to sustain confidence in a crisis and, as such, was an "unnecessary expense."[22]

[22] Private correspondence between a private bank executive, speaking anonymously, and the author, July 2015.

- Permitting banks to provide automatic teller machines (ATMs), issue debit cards, permit purchases through point-of-sale (POS) terminals, and (in May 2015) issue credit cards. These freedoms have created what is probably the most visual manifestation of Myanmar's banking reforms. In practice, however, the spread of ATM networks has yet to transform consumer banking in Myanmar because of the requirement that each card have a separate (non-interest bearing) account that cannot be used for any purpose but to access ATMs. With respect to using debit cards beyond ATMs, POS transaction terminals are now in place in several hundred retailers, restaurants, and hotels across Myanmar. However, poor Internet connections in many locations somewhat undermine their impact.

- In light of developments with respect to ATMs and electronic cards, global card-issuing firms such as Visa and MasterCard have arrived. An initiative essentially led by the private banks (especially Kanbawza Bank), the initial motivation was to provide card services to facilitate the growing numbers of foreign tourists.[23] MasterCard and Visa (which arrived in November and December 2012, respectively) have been followed into Myanmar by the cards of China's Union Pay (February 2013) and Japan Credit Bureau (September 2013). In November 2013, Co-operative Bank (CB Bank) introduced the Easi Travel Master Card, a prepaid travel debit card that Myanmar citizens can use abroad.[24]

- Establishing a credit bureau is in progress (to be operational in June 2016), with the assistance of the International Finance Corporation (IFC) of the World Bank and the United Kingdom's Department for International Development (DFID). Employed all over the world, but especially useful in countries where title over property is often difficult to establish, credit bureaus create what is effectively reputational collateral by allowing lenders "to access borrowers' credit history, evaluate loan risks, and make lending decisions more quickly."[25]

In addition to the above deregulatory measures concerning domestic operations, in April 2012, the banks received a series of new freedoms that accompanied the reform of Myanmar's exchange rate regime (the shift from the old fixed peg to the managed float, as discussed above). These included:

[23] Amid the many reports detailing the visits of envoys of the global debit and credit card issuers, see S. Vallikappen, "Sacks of Cash in Myanmar Hard to Rout For MasterCard, Visa," *Bloomberg*, October 21, 2013, http://www.bloomberg.com/news/articles/2013-10-20/sacks-of-cash-in-myanmar-hard-to-displace-for-mastercard-visa, (accessed February 8, 2016).

[24] MasterCard, "MasterCard and CB Bank Announce First Prepaid Travel Card in Myanmar," MasterCard news release, October 8, 2013, http://newsroom.mastercard.com/press-releases/mastercard-and-cb-bank-announce-first-prepaid-travel-card-in-myanmar-2/, (accessed November 5, 2015).

[25] International Finance Corporation, "IFC Supports Central Bank of Myanmar to Develop Credit Reporting System and Expand Access to Finance for Businesses," IFC news release, November 14, 2014, http://ifcext.ifc.org/IFCExt/pressroom/IFCPressRoom.nsf/0/473BF09BE6D000A485257D90003B2EB2?opendocument, (accessed November 4, 2014).

- Allowing private banks to open money change counters and deal in foreign exchange (October 2011).

- Allowing private banks to offer foreign currency deposits to both Myanmar residents and foreigners (May 2012).

- Allowing banks to sign agreements with international remittance firms. The first such deal, between Myanmar Oriental Bank and Western Union, was signed in September 2012.

- Creating an interbank market for foreign exchange (August 2013). This market remains, however, undeveloped and relatively illiquid.

SANCTIONS

One of the most significant changes afforded Myanmar's banking sector since the advent of Thein Sein's administration comes from outside the country through the lifting of financial sanctions. Such sanctions were dominated by those applied by the United States, under the 2003 *Burmese Freedom and Democracy Act* (BFDA) and the *Tom Lantos* (JADE) *Act* of 2008, which banned the export of U.S. financial services to Myanmar. Sanctions and, more significantly, the deliberate policies of the past State Peace and Development Council (SPDC) regime to wind down much of the banking system after Myanmar's 2003 financial crisis, effectively isolated Myanmar from the global financial system and impeded the flow of new ideas, methods, and norms.

The U.S. Treasury's Office of Foreign Assets Control has eased sanctions in several steps. Beginning April 17, 2012, U.S. firms were allowed to provide financial services to Myanmar for the purposes of religious, humanitarian, and other nonprofit activities. Effective July 11, 2012, the U.S. Treasury issued general licenses allowing U.S. firms to export financial services to Myanmar and make investments there.[26] In February 2013, U.S. sanctions on Myanmar's banking sector were further eased when it was announced that four banks included on the U.S. Treasury's Specially Designated Nationals (SDN) list could now conduct business with U.S. financial institutions.[27] The four banks were the state-owned Myanmar Economic Bank (MEB) and the Myanmar Investment and Commercial Bank (MICB), as well as two banks founded by two of Myanmar's most prominent "cronies," the Asia Green Development Bank (AGD) and the Ayeyarwady Bank (AYB). Being on the SDN list had excluded these banks from engaging in business with U.S. financial institutions, despite the generalized lifting of the broad financial services ban. With respect to the two private banks, this latest easing is limited to the conduct of transactions business (primarily funds transfer, correspondent relations, and the like). U.S. banks continue

[26] See General License 16, "Authorizing the Exportation and Re-exportation of Financial Services to Myanmar," Department of the Treasury, July 11, 2012, http://export.gov/thailand/doingbusiness/burma/sanctions/, (accessed May 6, 2016). The United States maintains a Specially Designated Nationals list of individuals and groups (such as terrorists and drug traffickers) with whom U.S. persons and firms are prohibited from doing business.

[27] For the SDN list, see https://www.treasury.gov/resource-center/sanctions/SDN-List/Pages/default.aspx. U.S. Department of the Treasury, "General License with Respect to Asia Green Development Bank, Ayeyarwaddy Bank, Myanmar Economic Bank, and Myanmar Investment and Commercial Bank," February 22, 2013, http://www.treasury.gov/resource-center/sanctions/Programs/Documents/Myanmarg119.pdf, (accessed March 4, 2015).

to be restricted from investing in AGD or AYB or from forming joint venture relations with them. Both owners remain on the SDN list individually, as do three other banks: the Myanmar Foreign Trade Bank (the state-owned institution that controls much of Myanmar's revenues from gas and other foreign exchange), as well as the military-owned Innwa and Myawaddy Banks (controlled respectively by the military's two giant holding companies, Myanmar Economic Corporation and Myanmar Economic Holdings).

Of course, over and above the specificities of who is sanctioned or not is a general lingering impact of sanctions on international perceptions—an important matter given the escalating fines levied on banks that fail to comply with past prohibitions. Many international banks accordingly remain wary of Myanmar broadly as a jurisdiction, unwilling to drill down into the specifics of the actual customers with whom they might be dealing.[28] Clearing such perceptions away will take time and perhaps require a wholesale change to the Myanmar political economy.

MONEY LAUNDERING PROBLEMS LINGER

At various points Myanmar's government has introduced legislation designed to combat money laundering. An important regulatory issue more or less everywhere, it has an elevated importance in Myanmar—a country known for being one of the world's leading sources of narcotics. The principal anti-money laundering body in the world is the Financial Action Task Force (FATF) of the OECD. At various points in the past it has excoriated Myanmar, including it on annual lists of non-cooperating jurisdictions and urging its exclusion from the international financial system. In 2015, recognizing efforts made, FATF took a somewhat softer line. Nevertheless, its findings confirm that Myanmar is not yet where it needs to be. Here is FATF's October 2015 judgment:

> Myanmar has taken important steps toward improving its AML/CFT [anti-money laundering and combating the financing of terrorism] regime…However, despite Myanmar's high-level political commitment to work with the FATF and APG [Asia-Pacific Group on Money-Laundering] to address its strategic AML/CFT deficiencies, Myanmar has not made sufficient progress in implementing its action plan, and certain strategic deficiencies remain. Myanmar should continue to implement its action plan to address these deficiencies, including by: (1) adequately criminalizing terrorist financing; (2) implementing adequate procedures to identify and freeze terrorist assets; and (3) ensuring an operationally independent and effectively functioning financial intelligence unit. The FATF encourages Myanmar to address the remaining deficiencies and continue the process of implementing its action plan.[29]

[28] As an example of this phenomenon, see Jeremy Mullins, "US Banks Stay Picky on Myanmar Transformers," *Myanmar Times*, June 19, 2015, http://www.mmtimes.com/index.php/business/15108-us-banks-stay-picky-on-myanmar-transfers.html, (accessed August 22, 2015).

[29] FATF's statement was made on October 23, 2015. See http://www.fatf-gafi.org/countries/j-m/myanmar/documents/public-statement-october-2015.html, (accessed November 3, 2015).

5. INDIVIDUAL BANK PROFILES

STATE-OWNED BANKS

Since its independence from Britain in 1948, state-owned banks have played an unusually prominent role in Myanmar. Established according to the fashion of the times and a widespread belief that private (but especially foreign) finance constituted both a threat to sovereignty and a hindrance to the state's development goals, state domination of Myanmar's financial sector reached its apogee in 1964 when all private banks were nationalized. Soon after, and together with already established sector-focused state-owned banks, these banks were merged into a single entity—the monolithic People's Bank of the Union of Myanmar (PBUB). This was subsequently divided along sectoral lines in the mid-1970s, creating three of the four currently operating state-owned banks, along with the CBM. Private banks were allowed to form in Myanmar from 1990 under the *Financial Institutions of Myanmar Law* of that year. Nevertheless, until very recently, the state-owned banks greatly dominated the sector.

The state-owned banks' domination of Myanmar's banking sector is surely coming to an end. This report has already noted growth in private sector banks; similar growth has eluded the state-owned banks. Their assets in FY2014/15 accounted for just 29.5 percent of GDP (compared to 58.5 percent for private banks), down 2.5 percent since 2013 (IMF 2015, 20). Private sector lending by state-owned banks now accounts for just 2.5 percent of GDP, compared with private sector lending by the private banks of 16.1 percent (IMF 2015, 31). Naturally, one set of customers that the state-owned banks does not have to fear losing through competition is state-owned organizations of any form. State actors are compelled to bank with their state-owned brethren.[30]

Myanmar has four fully state-owned banks: the Myanmar Economic Bank (MEB); the Myanmar Foreign Trade Bank (MFTB); the Myanmar Investment and Commercial Bank (MICB); and the Myanmar Agricultural Development Bank (MADB). The MEB is a broad banking institution with a large network of rundown branches, lax lending standards, indifferent management, and obsolete systems; it functions primarily as a funding vehicle for state economic enterprises, and to provide treasury and other functions for the government. MEB loans to the private sector account for less than 10 percent of the bank's total assets (OECD 2014, 195). It surely has significant bad loans on its books and, despite its branch network,

[30] A requirement confirmed in answer to a question in Myanmar's lower house of parliament (the *Pyithu Hluttaw*) in August 2015. "Pyithu Hluttaw Roundup," *The Global New Light of Myanmar*, August 26, 2015, 2.

would struggle to hold depositors in a competitive banking environment. According to one senior official within the MEB, it "will take time to become efficient with new products, as we are unfamiliar with modern banking systems."[31]

A recent audit report of the MEB revealed that it has not been profitable since 1990.[32] As shall be examined in more detail below, one of the most significant borrowers from the MEB is the MADB, which takes just over half of MEB's loan portfolio, but which pays an interest rate of just 4 percent on its loans, funds on which the MEB itself pays 8 percent. In the first six months of the 2015/16 fiscal year the MEB had interest revenues of K9.3 billion, against interest expenses of K240 billion. Naturally, it cannot absorb losses of this magnitude and in November 2015 it requested additional allocations of nearly K80 billion from the Union budget.[33]

Notwithstanding the losses it incurs, across 2015 deposits strongly flowed to the MEB—and momentarily away from private banks deemed by many as vulnerable to Myanmar's rising political and other risks. According to the IMF (2015, 20), MEB deposits are now the equivalent of over 5 percent of Myanmar's GDP.[34] As a consequence, the MEB is fairly awash with liquidity but has little idea what to do with the funds at its disposal. As noted, some of this liquidity has made its way (unprofitably) to the MADB, but increasingly the MEB has become a large buyer of Myanmar government treasury bills. This practice has had consequences for the treasury market. The MEB, at the insistence of the Ministry of Finance, has been unwilling to pay the minimum interest rate necessary to sell all the bills in an open market at the clearing rate. The forced allocation of bills to the MEB at below the clearing rate has imposed a below-market yield that discourages other buyers and leaves the CBM to take up the slack.

The organization Making Access Possible (2014, 2) is sanguine that the MEB could become the future vehicle for greater savings mobilization in Myanmar, but acknowledges this would require dramatic modernizing of the bank's systems. The World Bank is currently engaged in an advisory capacity on the possible reform of both the MEB and MADB. Its findings are eagerly awaited.

Following recent reforms to Myanmar's exchange rate system as discussed above, the MICB and MFTB have lost much of their previous dominance of formal foreign exchange business. Like the MEB, they would be hard pressed to survive in a truly competitive financial sector. With their activities hitherto centered on rationing funds (especially foreign exchange) and ensuring the implementation of regulation (such as determining evidence of foreign earnings), they are increasingly losing market share to their more customer-focused competitors. That said, both banks remain a haven for the foreign exchange deposits of government departments, state economic enterprises, and some individuals (domestic and foreign). In early 2015 rumors spread in Myanmar banking circles that the MICB would be restructured and privatized. As of early 2016, nothing concrete had emerged.

The MADB is in perhaps the worst shape of all the state-owned institutions. Its under-performance is an important contributor to the lack of progress in Myanmar's agricultural sector as a whole. Given its would-be central role in rural Myanmar, as well as the methodological peculiarities of rural lending, the MADB is examined in much more detail below in the section on rural finance.

In November 2015 an unnamed official of the CBM speculated on the future of all the state-owned banks. After acknowledging that all would continue to lose market share to their private sector counterparts, he suggested that only dramatic changes would make them competitive: First, they need to focus on developing human resources and infrastructure, as well as policy reforms. Second, they need to be corporatized or reformed through public-private partnerships, which will hopefully happen at some stage under the NLD government.[35]

PRIVATE BANKS

As noted at the outset of this study, Myanmar's private banks are not yet the institutions the country needs. Nevertheless, their growth (albeit from a very low base) has been impressive. Table 7 shows deposits from and lending to the private sector. With the caveat that some of the deposit growth has taken place through the MEB (as noted earlier), the narrative of growth overwhelmingly belongs to the private banks.

Increasingly the MEB has become a large buyer of Myanmar government treasury bills.

Notwithstanding the losses it incurs, across 2015 deposits strongly flowed to the MEB—and away from private banks deemed by many as vulnerable to Myanmar's rising political and other risks.

The narrative of growth overwhelmingly belongs to the private banks.

TABLE 7: BANK DEPOSITS AND LENDING

Fiscal Year	Deposits	% GDP	Lending to Private Sector	% GDP
2011/12	7,010	16.2	3,255	7.5
2012/13	11,733	24.6	4,899	10.3
2013/14	16,494	30.2	7,471	13.7
2014/15	20,399	32.5	10,125	16.1

Source: IMF (2015, 31)

[31] The senior official was a manager of the MEB branch in Nay Pyi Taw. Aye Thidar Kyaw, "Rethinking Myanmar's State-Owned Banks," *Myanmar Times*, August 31, 2015, http://www.mmtimes.com/index.php/business/16227-rethinking-myanmar-s-state-owned-banks.html, (accessed September 4, 2015).

[32] "Myanmar Economic Bank has been Losing Money for Two Decades: Audit Report," *Eleven News*, July 13, 2013, http://elevenmyanmar.com/index.php?option=com_content&view=article&id=2752:myanmar-economic-bank-has-been-losing-money-for-two-decades-audit-report&catid=33&Itemid=356, (accessed October 7, 2014).

[33] Htoo Thant, "Deposit Rate at Myanmar Economic Bank Set to Triple," *Myanmar Times*, November 27, 2015, http://www.mmtimes.com/index.php/business/17846-deposit-rate-at-myanma-economic-bank-set-to-triple.html, (accessed December 1, 2015).

[34] After the National League for Democracy's victory in the November 2015 elections, this process was reversed and deposits flowed again to private banks.

[35] Aye Thidar Kyaw, "More Challenges Ahead for State-Owned Banks," *Myanmar Times*, November 4, 2015, http://www.mmtimes.com/index.php/business/17350-more-challenges-ahead-for-state-owned-banks.html, (accessed November 5, 2015).

Such is the aggregate and numerical picture of Myanmar's private banks. Naturally, these disguise considerable variation in individual bank strategies and performance. Individual analyses of Myanmar's private banks are offered below.

The Big Three

Three banks—Kanbawza, Ayeyarwady, and Co-operative (CB) Bank—dominate private sector retail banking in Myanmar. That said, **Kanbawza** could almost be regarded as its own category. By far Myanmar's biggest bank (it is three times larger than the next biggest bank in terms of assets, and nearly twice as large in terms of number of branches and staff head count), Kanbawza Bank (KBZ) is the dominant private-sector financial institution in Myanmar. Founded in 1994 in Taunggyi (Shan State), Kanbawza Bank is part of the broader KBZ Group encompassing airlines, insurance (IKBZ—more on which below), tourism, agroindustry, infrastructure, light industry, and import-export.[36] The KBZ logo is one of Myanmar's most recognized symbols.

The KBZ Group's early history had it well associated with prominent members of the old SPDC regime, but more recently it has become known for winning numerous corporate social responsibility awards.[37] KBZ Group regularly tops the Ministry of Finance's list of top taxpaying companies.[38] Casting something of a shadow over the smooth image of the KBZ Group, however, have been the recent (unresolved) allegations of substantial involvement of KBZ founders with Myanmar's highly lucrative, and sometimes illicit, jade business (Global Witness 2015).

Kanbawza Bank itself has greatly expanded its capital base across the years, which now stands at a fully-paid K100 billion. KBZ has around K5,000 billion in assets, 12,000 employees, around 300 branches, and nearly 300 ATMs. It offers more or less the full range of allowable banking products in Myanmar, and in May 2015 became the first bank in the country to issue its own branded credit card after the CBM authorized the reintroduction of credit cards.[39] In September 2015 KBZ signed an agreement with Microsoft Corp. to modernize the bank's IT (information technology) infrastructure.[40] Depending upon the performance of the Yangon Stock Exchange, a stock market listing for the bank is in the foreseeable, though not immediate, future.

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[36] See KBZ Group's website, www.kbzgroup.com, (accessed August 18, 2015).

[37] Beyond its political connections, the extent to which jade mining was critical in the group's beginnings remains a question.

[38] Aye Thidar Kyaw, "Shifting Top Taxpayers as KBZ Leads Lists," *Myanmar Times*, January 2, 2015, http://www.mmtimes.com/index.php/business/12693-shifting-top-taxpayers-as-kbz-leads-lists.html, (accessed August 18, 2015).

[39] Aye Thidar Kyaw, "KBZ with First Domestic Credit Cards in a Decade," *Myanmar Times*, May 22, 2015, http://www.mmtimes.com/index.php/business/14620-kbz-with-first-domestic-credit-cards-in-a-decade.html, (accessed August 18, 2015).

[40] It is probable that these systems are currently in place only in about a quarter of KBZ's branches. Microsoft, "Myanmar Conglomerate Kanbawza Group Embarks on its Digital Transformation," Microsoft Corp., September 21, 2015, https://news.microsoft.com/apac/2015/09/21/myanmar-conglomerate-kanbawza-group-embarks-on-its-digital-transformation-journey-with-microsoft/, (accessed November 1, 2015).

Established in 2010, **Ayeyarwady Bank** has grown so rapidly that it is now, by most measures, the second largest private bank in Myanmar. Doing business under the shortened "Aya Bank" brand with over 115 branches and around 230 ATMs, Aya Bank is one of Myanmar's best-known financial institutions. A part of the Max Myanmar group of companies, Aya Bank is also one of the most technologically savvy of Myanmar's banks. It offers Internet, mobile, and electronic bill-payment services under its "i-banking" platform, built with the assistance of Ireland's CR2 Group.[41] In December 2015 Aya Bank had around K2,500 billion in assets, K2,100 billion in deposits, and loans outstanding of around K1,500 billion, and held K350 billion in government securities. The bank's loans-to-deposit ratio is a conservative 70 percent.[42] Aya Bank has fully paid-up capital of K30 billion, which means it will not have to raise new capital to reach the new CBM reserves minimum of K20 billion.

Aya Bank is the first Myanmar bank to be compliant with International Financial Reporting Standards and is also the first to be audited by one of the four major global accounting firms, Deloitte. Aya Bank has over 5,000 staff and employs a significant number of Myanmar expatriates. The bank has a close working relationship with Mizuho Bank, one of the three Japanese banks holding a banking license in Myanmar (more below).

Third-placed on most measures, **CB Bank** was created out of a series of mergers in 2004 of three cooperative banks, then state-owned: Co-operative Bank, Co-operative Farmers Bank, and Co-operative Promoters Bank. The three were managed by the Ministry of Cooperatives.[43] The Ministry no longer holds any equity in CB Bank, though staff and historical linkages suggest informal ties cannot be discounted. CB Bank was converted into a public company soon after the mergers and is now part of the Kaytumadi group of companies that has interests in insurance (Citizen Business Insurance), construction, real estate, tourism and hotels, mining, and agriculture.

CB Bank has fully paid-up capital of K20 billion, which places it precisely at the CBM's minimum. Accordingly, it is likely that a capital-raising by CB Bank will take place in the short to medium term. As shall be examined in more detail later, CB Bank is one of the institutions (the other two being Yoma and United Amara Bank) engaged in innovative agricultural financing through its collaboration with India's Sohan Lal Commodity Management Group (SLCM), which provides credit against stored commodities. Since 2013, CB Bank has been in an alliance with Japan's MUFJ Bank (subsequently one of nine foreign banks given banking licenses in Myanmar) for the provision of technical assistance.

CB Bank is one of the institutions ... engaged in innovative agricultural financing.

[41] Ayabank has a sophisticated website that is both a financial services platform and a source of information about the bank, http://ayabank.com/, (accessed August 8, 2015).

[42] http://ayabank.com/investor-relations/financial-highlights/, (accessed August 8, 2015).

[43] CB Bank has a sophisticated and interactive website: www.cbbank.com.mm, (accessed November 3, 2015).

Also assisting CB Bank, but specifically in the context of supporting the bank in providing financing for micro, small, and medium enterprises, is the German government-owned development bank, KfW.[44] Through the Ministry of Finance, KfW is providing CB Bank with EUR3.3 million to lend to SMEs.

CB Bank has over 140 branches throughout Myanmar, along with a large ATM network. It is a prominent player in the Myanmar banking scene, though its hitherto close competition with KBZ seems to have lost momentum somewhat over the last year or two. CB Bank's seasonal liquidity management is less than it could be and it stopped making new loans during the tight monetary conditions of January to March of 2015, as did KBZ.

Resurgent and Growing Banks

This category includes some of the new players established in 2010 (Asia Green Development Bank, United Amara, Myanmar Apex Bank) as well as some transforming institutions such as the Global Treasure Bank. Above all, however, it includes Yoma Bank.

Yoma was the second biggest private bank in Myanmar before the 2003 banking crisis laid waste to the sector. For a decade after these events, Yoma was relegated to simply being a provider of remittance services and operated under a restricted license to this end. Nevertheless, even during this period it stood out for the integrity and vision of its owners and managers.

Since the return of its full banking license in 2012, Yoma has surged back as one of Myanmar's leading banks. It is now probably the fifth-largest private bank and by some measures is the country's most internationally connected financial institution. Setting out to be a bank servicing small to medium enterprises, Yoma has partnered in this endeavor with the World Bank's private financing arm, the International Finance Corporation (IFC). To this end, in September 2014 the IFC provided Yoma Bank with a US$5 million convertible loan (convertible to equity) aimed at allowing Yoma to extend an additional 1,000 new loans (up to an aggregate of US$370 million) to small and medium enterprises, with the IFC covering the foreign exchange risks of the funding arrangement.[45] Another partnership of possible great import for Yoma, and perhaps for the sector as a whole, is its joint venture with Telenor, the Norwegian telecommunications company, to establish the mobile-money product "Wave Money," the details of which are outlined below. Finally, the German development agency GIZ is also working with Yoma, especially on staff training.

A large portion of Yoma Bank's loans are self-amortizing (around half), with the remainder in the form of business overdrafts (40 percent) and hire purchase (10 percent, mostly on vehicles). Such a portfolio, plus the bank's predilection for maintaining high levels of liquidity across the cycle, means that Yoma is often a lender of liquidity to other banks during tight conditions (especially the regular seasonal peak in January-March).

Yoma has surged back as one of Myanmar's leading banks. It is now probably the fifth-largest private bank and by some measures is the country's most internationally connected financial institution.

Myanmar Oriental Bank (MOB), like Yoma, was a member of the first wave of private banks allowed in the early 1990s. It has strong ties to Myanmar's ethnic Chinese business community. With over K230 billion in assets, 26 branches, and 1,000 staff, the MOB specializes in servicing small traders in their domestic and international operations. In February 2014 the IFC entered into an agreement with MOB to supply a US$5 million trade-finance facility to allow it to "help local companies increase their imports and exports, generate more foreign exchange, and create jobs."[46] In August 2015 this interest in Myanmar Oriental by the IFC was expanded in the form of a US$7 million convertible loan.[47] The arrangement was almost identical to that reached earlier with Yoma to support lending to SMEs. According to the joint statement from the IFC and MOB, "IFC's long-term financing will help MOB move closer towards its goal of providing more than US$200 million in loans to small and medium enterprises, its core client group, by 2019."[48] MOB enjoys a strong reputation within Myanmar's banking scene as a player with a keen commercial focus.

Asia Green Development Bank (AGD), **United Amara Bank** (UAB), and **Myanmar Apex Bank** (MAB) were established, alongside Aya Bank, in the final wave of new banks created under the old military regime. All three have grown strongly, if not to the extent of Aya Bank, though both AGD and UAB have been somewhat constrained by problems related to their owners.

AGD, which currently has just over 50 branches, K500 billion in assets, K30 billion in paid-up capital, and over 2,000 staff, was founded as a part of the Htoo Group. Its owner, as an individual, as well as both the Htoo Group and the AGD, are on the U.S. Treasury's SDN list. In 2015, however, the owner and groups relinquished their 60 percent stake in the bank, selling part of their equity to an existing director of AGD and the remainder to a son of Myanmar's former long-time dictator, General Ne Win. The latter aspect caused considerable controversy and was regarded as harmful to AGD's standing.[49] In October 2015 AGD released its annual results, reporting a drop in profits occasioned by increasing competition among the banks for deposits (with banks routinely paying above the 8 percent minimum interest rate) and in selling remittance products, as well as increasing costs from the expanding branch network and from upgrading IT systems. Meanwhile, AGD's plans

[44] For more on KfW's activities in Myanmar, see https://www.kfw-entwicklungsbank.de/International-financing/KfW-Development-Bank/Local-presence/Asia/Myanmar/index.html, (accessed November 26, 2015).

[45] IFC, "IFC and Yoma Bank Ink Deal to Expand Financing for Small and Medium Enterprises in Myanmar," IFC Press Release, September 16, 2014, http://ifcextapps.ifc.org/ifcext/pressroom/ifcpressroom.nsf/0/DA68A4369A7ED58185257D55002561CE?opendocument, (accessed November 3, 2015).

[46] The deal was signed on February 18, 2014. Details on this and other aspects of MOB's operations can be found at the Bank's website, www.mobmyanmar.com, (accessed August 14, 2015).

[47] IFC, "IFC Helps Myanmar Oriental Bank Expand Financing for Small Businesses to Spur Economic Growth," August 19, 2015, IFC News, (accessed August 20, 2015).

[48] Clare Hammond, "IFC Signs Second Convertible Loan with Local Bank," *Myanmar Times*, August 20, 2015, http://www.mmtimes.com/index.php/business/16074-ifc-signs-second-convertible-loan-with-local-bank.html, (accessed August 21, 2015).

[49] See Kyaw Hsu Mon, "Ne Win's Scions Plan Takeover of Tay Za's Bank," *The Irrawaddy*, July 22, 2014, http://www.irrawaddy.org/business/ne-win-scions-plan-takeover-tay-zas-bank.html, (accessed August 17, 2015).

to list on the planned Yangon Stock Exchange (YSX, more on which below) are, according the bank, "at the final stage."[50]

United Amara Bank (UAB) is also an institution with an ownership structure that would prove problematic to potential foreign investors. Part of the IGE Group, which is still subject to U.S. sanctions and is associated with a former Minister of Industry under the old SPDC regime and a leading figure broadly within the United Solidarity and Development Party (USDP), UAB has around K600 billion in assets, around 5,000 employees, 40 branches, and K30 billion in authorized and paid-up capital.[51] As noted earlier, UAB is one of three private banks collaborating with India's SLCM group in the development of a commodity warehouse receipt plan to provide finance for agricultural producers.

Some Smaller Institutions

Some relevant, smaller institutions also exist. These institutions are mostly lowly capitalized. Because of that, the aforementioned new minimum capital requirements under the new *Financial Institutions Law of Myanmar* will, if promulgated, likely create pressure for consolidation. Banks in this category include:

- **Asia Yangon International Bank** (10 branches, just over 100 employees and around 7,000 account holders). Very little is publicly known about this bank, which has no website and seems to advertise little. The bank's financial services seem to be exclusively wholesale, with a slant toward real estate and property development.
- **First Private Bank** (FPB). Founded by an influential figure in Myanmar banking, Dr. Sein Maung, FPB has long been innovative along a number of product lines, including mobile banking.[52] Likewise, as a public company of around 6,700 shareholders, FPB's ownership structure is progressive in the Myanmar context. No single owner controls more than 2 percent of shares. Dr. Sein Maung (who remains chairman) is not in favor of a public listing on the forthcoming YSX, noting concerns about speculators and the fear that "you lose control once you join the stock exchange."[53] FPB has been cautious about expanding its branch network beyond the nearly 30 it now has and has been equally conservative in its online banking and ATM services. FPB has K100 billion in authorized capital, and so will not need to raise more for regulatory purposes.

[50] Aye Thidar Kyaw, "AGD Banks Prepares IPO as Profits Drop," *Myanmar Times*, October 26, 2015, http://www.mmtimes.com/index.php/business/17175-agd-bank-prepares-ipo-as-profits-drop.html, (accessed October 28, 2015).

[51] See website of UAB, http://www.unitedamarabank.com/, (accessed November 4, 2015).

[52] In addition to being founder and chair of First Private Bank, Dr. Sein Maung currently serves as vice-chair of the Myanmar Banking Association and is perhaps the most outspoken (across many years) of all of Myanmar's bankers.

[53] Jeremy Mullins and Myo Lwin, "Profiles: A Look at Two Private Banks," *Myanmar Times*, July 15, 2014, http://www.mmtimes.com/index.php/special-features/194-your-money-2014/11030-profiles-a-look-at-two-private-banks.html, (accessed November 4, 2015).

- **Global Treasure Bank** (GTB). Formerly the Myanmar Livestock and Fisheries Development Bank and owned by the eponymous government ministry, the bank was privatized and renamed in 2013. As a result of its former role and ownership, GTB has an unusually widespread branch network, with 107 branches in most of Myanmar's states and regions.[54] As with most of Myanmar's private banks, GTB derives much of its business from remittances. In volume terms these rose 27 percent across FY2014/15, but fierce competition in this product line saw equivalent profits down by 50 percent across the same period.[55] The legacy of past loans made while the bank was in government hands weighs heavily on GTB, which reported nonperforming loans to the fisheries sector rising to 7.26 percent in late 2015.[56] Industry rumors put the figure at three times that.
- **Myanmar Apex Bank**. One of the four banks created in 2010, Myanmar Apex Bank is a subsidiary of the Eden Group of companies. This group is mainly involved in construction, but also has interests in retail petroleum, agriculture, and tourism. The tourism interests include a joint venture with the Hilton Group. The bank currently has 65 branches, nearly 3,000 employees and around K1 trillion (US$1 billion) in assets.[57] Myanmar Apex Bank is on the cusp of becoming one of the major players in Myanmar banking.
- **Tun Foundation Bank** (TFB). TFB is a well-respected bank founded in 1994 soon after private banks were first reauthorized in Myanmar. It is a commercial bank, but unusual in that most of its profits are allocated to a charitable trust that supports health and education projects.[58] TFB has long been prominent in promoting economic reform dialogue in Myanmar, and in the relatively closed-off 2000s sponsored research and held a number of seminars on Myanmar's economy. In FY2014/15 TFB began bringing all its branches online through an agreement with the international IT firm Oracle to install modern banking hardware and software systems.[59]
- **Shwe Urban and Rural Development Bank**. This is a new institution, created in June 2014, with initial paid-up capital of K10 billion; this suggests that capital

[54] For more details on the products and services offered by the Global Treasure Bank, see the bank's website, www.gbmm.com.

[55] Aye Thidar Kyaw, "Bank Profits Squeezed by Growing Competition," *Myanmar Times*, October 27, 2015, http://www.mmtimes.com/index.php/business/17196-bank-profits-squeezed-by-growing-competition.html, (accessed October 28, 2015).

[56] Ibid.

[57] See the website of Myanmar Apex Bank, http://www.mabbank.com/, (accessed November 2, 2015).

[58] For details of the charities supported and other information on TFB, see the bank's website at http://www.tunfoundationbankmyanmar.com/eng/, (accessed November 2, 2015).

[59] "Tun Foundation Bank Upgrades Online Systems," *Myanmar Times*, May 12, 2014, http://www.mmtimes.com/index.php/business/10290-tun-foundation-bank-upgrades-online-systems.html, (accessed November 2, 2015).

will need to be raised at some point.[60] This bank is the creation of the tycoon owner of Myanmar's Sky Net television network, who has numerous other interests in tobacco, gems, alcohol, and agribusiness; he is well connected, with businesses in sectors where market competition is limited by protective policies.

SEMIPRIVATE BANKS

Beyond the four major state-owned banks are other institutions connected in various ways to organs of the state (the military, ministries, local government) in Myanmar. Accordingly, the banks in this category perform an amalgam of policy functions as well as those more familiar to commercial banking.

By far the most prominent of these are the Myawaddy and Innwa banks. **Myawaddy** is owned by the giant military conglomerate, Myanmar Economic Holdings Limited (MEHL).[61] MEHL share capital is owned in turn by the Directory of Procurement of Myanmar's Ministry of Defense (which holds A, or voting, shares) and various armed forces' cooperatives, regimental associations, and veterans organizations (which hold B shares). MEHL has interests in many parts of Myanmar's economy, but especially in gem production and marketing, hotels, tourism businesses, construction, real estate, beverages, and trading. The chairman of the Myawaddy Bank is usually a senior military officer, as are members of the bank's board. Myawaddy Bank does not provide much public information on its activities, but it has around 40 branches, around K1,100 billion in assets, and some 2,500 staff. The Aung Thitsa Oo Insurance Company is an affiliate of Myawaddy. Both Myawaddy Bank and MEHL remain sanctioned by the United States and appear on the U.S. Treasury's SDN list.

Innwa Bank is a subsidiary of the second of Myanmar's dominant military enterprises, the Myanmar Economic Corporation (MEC). Whereas MEHL mostly concentrates on trading and light industry, MEC focuses on heavy industry. Like MEHL, its share capital is owned by serving and retired military officers, who similarly fill senior positions in both MEC and Innwa Bank. Formally registered as an investment and development bank (a distinct category under the 1990 *Financial Institutions of Myanmar Law*), Innwa Bank currently has just over 30 branches and about K300 billion in assets. It has authorized capital of K30 billion, so it will not need to raise capital to meet the CBM's new minimums. Innwa is a little less shy than its Myawaddy sibling, but information on the bank's activities is still rather opaque.[62] Innwa is affiliated with the Aung Myint Moh Min Insurance Co. Both MEC and Innwa are sanctioned and appear on the U.S. Treasury's SDN list.

Myanmar Citizens Bank (MCB) was established in 1991 and is part-owned by the Ministry of Commerce. MCB

Whereas MEHL mostly concentrates on trading and light industry, MEC focuses on heavy industry.

[60] Thiha, "Banking—Another Business Step of Shwe Than Lwin," *Consult Myanmar*, June 16, 2014, http://consult-myanmar.com/2014/06/16/banking-another-business-step-of-shwe-than-lwin-2/, (accessed August 21, 2015).

[61] The company was formerly known as Union of Myanmar Economic Holdings Limited (UMEHL), and is often referred to by this name, even today.

[62] Unlike Myawaddy Bank, however, Innwa Bank has a website, http://www.ablmm.com/, (accessed November 2, 2015).

In most countries state-owned "policy" or development banks have led to severe disappointment.

was long notable for the fact that its shares were listed for over-the-counter trading at the Myanmar Securities Exchange (more on which later). A mid-size bank with a dozen branches, MCB focuses on trade finance. It has around K200 billion in assets, and paid-up capital just short of the CBM's new K20 billion minimum. The bank's authorized capital is K75 billion. MCB strongly opposed the authorization of mobile money arrangements by nonbank institutions such as telecommunications firms.[63]

Three of Myanmar's formal banks are owned by the municipal authorities of Yangon, Mandalay, and Nay Pyi Taw respectively (**Yangon City Bank**, **Yadanabon Bank**, and **Nay Pyi Taw Sibin Bank**). Each of these banks is capitalized at very low levels (K500 million, K300 million, and K3 billion), has no more than a few thousand customers, and has just a few branches. Very little is known of their activities and it is difficult to conceive of them as banks at all in the conventional sense.[64]

THE NEW POLICY BANKS

Under the Thein Sein administration, the changes made to banking and finance in Myanmar have mainly been in a liberal, market-oriented direction, however fitfully and incompletely implemented. Standing in stark contradiction to this general trend, however, has been the rise of state-owned "policy" or development banks, all aimed at a target sector of the economy.

Of course such banks are not new to Myanmar, nor are they uncommon elsewhere in the world. However, in most countries their creation has led to severe disappointment. Notwithstanding its advisory role at the CBM and more broadly with the government, the IMF has had little success in stemming the momentum in the policy bank direction. Drawing attention to the issue in its 2014 Article IV Staff Report on Myanmar, the IMF cautioned:

> While policy banks can be useful, international experience shows they often make poor lending decisions and are not commercially managed, meaning that they incur large losses that ultimately have to be covered by the government budget. They therefore need to protect the quality of their loan portfolios, be closely supervised and operate on a level playing field with other commercial banks, which requires strong management and credit assessment skills. The number of new policy banks should be minimized and their external borrowing tightly circumscribed. (IMF 2014, 15)

As a matter of routine, IMF Article IV reports allow all member governments to respond to the findings of IMF staff; in this instance the Myanmar authorities took up the opportunity to respond to the concerns over the policy banks. Pointing to

> … *political imperatives* … [they] explained that they considered that such banks could play an important role in developing the economy in areas where market-based incentives alone would

[63] MCB's website can be found at http://mcb.com.mm/, (accessed November 26, 2015).

[64] Information on these banks here is gleaned through author's private correspondence with industry players.

> under-serve segments of the population, or specific sectors such as agriculture (IMF 2014, 16, emphasis added).

The same respondents gave some ground to the IMF, however, with the latter reporting that their Myanmar interlocutors "… indicated that they were exploring options to mitigate risks, including consolidation of policy banks into one national development bank …" (IMF 2014, 16).

Nothing since has been heard on this consolidation proposal. In the meantime, the following are some of the known details about each of the new policy banks.

Construction and Housing Development Bank (CHDB). CHDB was established by the Ministry of Construction in July 2013 to offer longer-term loans to property developers and construction companies, as well as homebuyers for lower-cost housing and apartments. Its loan terms are up to 8 years, significantly longer than the mandated, annual terms of other banks, but still well short of the mortgage terms (30 years and more) that are routine in much of the world. Thus far the CHDB seems to have made little impact on the market, with potential borrowers complaining about uncertain procedures as well as the still too-short loan maturities.[65]

Myanmar Microfinance Bank (MMB). Created in July 2013, MMB is licensed as a development and investment bank rather than a commercial bank.[66] It can, however, undertake commercial banking activities with the permission of the CBM. It makes loans, backed by collateral, directly to micro and small enterprises, but it makes uncollateralized loans to low-income borrowers indirectly, using the Central Cooperative Society as its intermediary. MMB's deposit interest rates are relatively high and above the regulatory minimums—8.25 percent per year on call deposits, while term deposits of a year or more earn 10 percent. Loans are mostly charged at the 13 percent per annum ceiling. The extent to which this bank is implicated in the great expansion of cooperative credit in Myanmar (referred to in Section 12 of this study), as funded by loans from the China Export-Import Bank is, at this point, somewhat obscure. The widespread belief within banking circles in Myanmar is that the MMB controls up to about 30 percent of the China loan dispersal.

Rural Development Bank (RDB). Very little information is publicly available with respect to the RDB.[67] Created by the Ministry of Livestock, Fisheries, and Rural Development, the RDB seems to be the replacement for the partially spun off Global Treasure Bank, which was previously the Ministry's financial arm when it was the Myanmar Livestock and Fisheries Development Bank. However, the RDB's ownership seems to be more widely spread, including interests held by various local governments whose agricultural sectors overlap the Ministry's responsibility areas.

The widespread belief within banking circles in Myanmar is that the MMB controls up to about 30 percent of the China loan dispersal.

Meanwhile, two new policy banks are pending: a **Myanmar Tourism Bank** that is the creation of the Myanmar Tourist Federation, and a **Gems and Minerals Development Bank** proposed by the Myanmar Gems and Jewelers' Entrepreneurs Association.[68] Progress toward establishing both of these banks is well advanced. The CBM has already approved an application for a banking license for the Tourism Bank. For the Gems and Minerals Bank the process of raising sufficient capital—K20 billion is the target in light of the requirements of the new FIL—is underway. Potential investors willing to contribute K400 million are being offered directorships of the bank; this amount might be beyond most of Myanmar's mining companies but for "jade entrepreneurs on the other hand, this amount is nothing."[69]

Reaction to the New Policy Banks

Myanmar's new policy banks seem to have been a step too far for a number of industry players in Myanmar, who are overwhelmingly skeptical of the banks' viability and anxious about the damage they might cause the rest of the sector. This is true of the local bankers, many local regulators, and also international agencies (the IMF concerns have already been noted) and advisers to the sector. The IFC's representative in Myanmar was especially (and, unusually, publicly) critical, declaring in the pages of the *Myanmar Times* in August 2015 his concerns over the narrow focus of the banks and the contagion that their failure could bring:[70]

> Banks need a diversified asset base, otherwise it's a recipe for disaster. For example, one bad year for Myanmar tourism could significantly impact a bank focused on tourism … The policy banks are still small but it's a matter of confidence. There is no guarantee that a small bank failure won't cause a confidence crisis across the whole industry. This could lead to uncertainty and people may decide to withdraw their money as a precaution, which in itself can trigger a bank run.

Finally, acknowledging the enduring shortage of qualified bankers in Myanmar, the IFC representative said he feared that "the new banks are likely to drain the already-thin resources."[71]

[65] Myat Nyein Aye and Tin Yadandar Htun, "Yangon Urgently Needs Low-Cost Housing," *Myanmar Times*, June 9, 2015, http://www.mmtimes.com/index.php/business/property-news/14938-yangon-urgently-needs-low-cost-housing.htm, (accessed August 2, 2015).

[66] Details from the website of MMB, http://www.mmbbank.com.mm/, (accessed August 21, 2015).

[67] At the time of writing, Rural Development Bank's website was "under construction," http://www.rdbankmm.com/, (accessed August 21, 2015).

[68] Clare Hammond, "Industry Banks Add to Sector's Risk," *Myanmar Times*, August 21, 2015, http://www.mmtimes.com/index.php/business/16111-industry-banks-add-to-sector-s-risk.html, (accessed August 22, 2015).

[69] The assertion by U Myo Myint, President of the Myanmar Mineral Entrepreneurs Federation as reported in Chan Mya Htwe, "Gems and Minerals Bank to Register in September," *Myanmar Times*, September 2, 2015, http://www.mmtimes.com/index.php/business/16268-gems-and-minerals-bank-to-register-in-september.html, (accessed September 4, 2015).

[70] Clare Hammond, "Industry Banks Add to Sector's Risk" *op.cit.*

[71] Ibid.

6. MOBILE BANKING AND ITS POSSIBILITIES

In recent years great excitement has accompanied the rise, in practice but even more for the *potential*, of mobile money schemes. Based upon the mobile phone and its attendant networks, such arrangements have been presented (with no little evangelical fervor at times) as the last, best solution for chronic financial exclusion among poor and geographically dispersed populations.

The transformative possibilities of mobile banking and money arrangements have been a perennial concern of just about every study of Myanmar's financial sector. Mobile banking has also been the subject of great media interest, locally and internationally, even catching the attention of *The Economist* which described it as a "leapfrogging" opportunity as early as 2013.[72]

In an attempt to make manifest the promise of mobile banking for Myanmar, and to get on top of its prudential regulation, in December 2013 the CBM issued its *Mobile Banking Directive*. Based upon similar laws in Bangladesh and other countries further down the track on this front, the directive listed a very liberal number of services that banks in Myanmar are authorized to offer by mobile phone:

- Payment and receipt of remittances, onshore and offshore;
- Deposit and receipt of cash through bank branches, agents, and ATMs;
- Payments to and from government, businesses, and individuals (bills, salaries, taxes, pensions, dividends, premiums);
- Bank transfers between accounts, individuals; and
- Microfinance payments and repayments.

However, the directive limits the size of individual mobile transactions to a maximum of K500,000. A maximum of three transactions are allowed per day and they cannot total more than K1 million.

In December 2013 the CMB issued its *Mobile Banking Directive* [which] listed a very liberal number of services that banks in Myanmar are authorized to offer by mobile phone.

[72] "Mobile Banking in Myanmar: Leapfrog Spotting," *The Economist*, September 28, 2013, http://www.economist.com/news/finance-and-economics/21586841-mobile-phones-may-regenerate-countrys-withered-banking-system-leapfrog-spotting, (accessed August 16, 2015).

The CBM's directive made it clear that, thus far, Myanmar is pursuing only a bank-led model of mobile banking. Under this model, differentiated from nonbank models in which a mobile phone company is usually the dominant counterparty, a customer must use a bank account to make and receive payments. Banks use mobile phone operators to make actual transfers of funds, but these operators function only as the agents of banks. Of course, under this model banks are also responsible for their customers' money in the operation of mobile banking:

> … banks and financial institutions shall take responsibility for the losses of customers that occur as the result of any inappropriate actions of their branches, cashpoints, agents and partners.[73]

Currently six local banks in Myanmar offer mobile banking (Ayeyarwady, CB Bank, FPB, Myawaddy, Innwa, and Yoma) built upon platforms that access the networks of the two new foreign mobile phone operators, Telenor of Norway and Ooredoo of Qatar. The mobile platforms of Ayeyarwady and CB Banks are probably the most advanced and widespread.

Nevertheless, and as noted already, genuine mobile financial service providers (MFSP) *based on mobile operators* rather than banks, are not yet authorized in Myanmar (despite being allowed under the new FIL, and despite the fact that the CBM has already drafted—but not issued—permitting regulations). MFSP mobile operator-dominated platforms exist in a number of countries, most prominently throughout Africa, where the Kenya-based M-Pesa system (of Safaricom, a telecommunication firm and subsidiary of Vodaphone) is in many ways the exemplar of the mobile money business. M-Pesa began almost accidentally when increasing numbers of Kenyans started transferring monetary value to each other in the form of "air time" on their mobile phones. This phenomenon quickly expanded into the provision of financial services, especially through the addition of optional financial products. Today M-Pesa and associated extensions dominate the banking sector in Kenya as well as some neighboring countries.[74]

The aforementioned and still-to-be-authorized "Wave Money" joint venture between Yoma and Telenor (49 percent owned by Yoma, 51 percent by Telenor) is indeed a true MFSP, rather than simply a mechanism linking existing bank products to existing customers by mobile phone. Wave is an interoperable service that functions through SMS as well as mobile applications using the Internet and, most importantly, via Telenor's vast and growing network of agents, as well as functioning at bank branches and ATMs at which customers can receive and deposit cash. Such agents have been critical to the success of mobile money arrangements, which elevates further the importance of the telecommunications companies (telcos) and their vast networks of agents selling SIM cards and other phone services. Telenor already has great experience in building and operating MFSPs.[75]

Thus far, Myanmar is pursuing only a bank-led model of mobile banking.

Genuine mobile financial service providers (MFSP) *based on mobile operators* rather than banks, are not yet authorized in Myanmar, despite being allowed under the new FIL.

Outside of the large telcos, banks, and other institutions, other players are also hovering around the edges of mobile banking and payments. Such actors are, of course, central to this emerging sector all around the world, but in Myanmar, too, there are start-up firms with energy and fresh ideas. One such firm is MyChat, a local Myanmar social media company known for offering chat services. In October 2015 it signed up with the online, London-listed payment provider MySquar to offer a MyPAY mobile payment service in Myanmar. MyPAY has said that it is "looking at partnering with a financial institution rather than a telco," thus keeping within the CBM directive.[76]

[73] Cited from Vanderbruggen and Dharmasi (2014), p.5.

[74] M-Pesa is also in India, Afghanistan, and Eastern Europe and is seemingly on the expansion path in many countries. In its aborted efforts to secure one of the telecommunicationslicenses offered in Myanmar to foreigners in 2013, Vodaphone included a Myanmar version of M-Pesa in its bid.

[75] Notably in Pakistan where, indeed, Telenor owns a controlling stake in one of that country's leading banks. For more, see Richard Handford, "Telenor Aims for H2 Money Launch in Myanmar, as Rival Ooredoo Gets Its Man," *Mobile World Live*, May 12, 2015, http://www.mobileworldlive.com/asia/asia-news/telenor-aims-h2-money-launch-rival-ooredoo-gets-man/, (accessed November 4, 2015).

[76] Catherine Trautwein, "MyCHAT to Get Mobile Payments," *Myanmar Times*, October 20, 2015, http://www.mmtimes.com/index.php/business/technology/17082-mychat-to-get-mobile-payments.html, (accessed October 28, 2015).

7. THE RETURN OF FOREIGN BANKS

In 1962, the incoming military regime nationalized the foreign banks operating in Myanmar. Active in the country for over a century and a part of the transformative story of Myanmar's agricultural sector in the 19th century, local subsidiaries of many of the storied names of international banking—the Hong Kong and Shanghai Banking Corp., the National City Bank of New York, Chartered Bank, and Lloyd's—were absorbed into the Peoples' Bank monolith. For the next 50 years, foreign financial institutions continued to be unwelcome in Myanmar. Nominally allowed under the 1990 *Financial Institutions of Myanmar Law*, in practice foreign banks remained a non-starter. To the extent that foreign banks entered into the discourse at all in Myanmar, it was usually just to fill the role of pantomime villains in nationalist (often government-sponsored) narratives of the country's history. For those who wanted to look beyond these caricatures, there was little but the faded magnificence of the old bank buildings of downtown Yangon, crumbling reminders of paths otherwise once traveled.

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In 2014 all of that changed. On September 30, the CBM announced the names of nine foreign banks that were to be awarded licenses to operate in the country. A keenly awaited decision which followed a generally well-regarded selection process the year before (which was assisted by a German consultancy firm), the "winners list" caused few shocks:

- Australia and New Zealand (ANZ) Banking Group (Australia);
- Bangkok Bank (Thailand);
- Bank of Tokyo-Mitsubishi UFJ (Japan);
- Industrial and Commercial Bank of China (China);
- Malayan Banking Berhad (Malaysia);
- Mizuho Bank (Japan);
- Overseas Chinese Banking Corp. (Singapore);
- Sumitomo Mitsui Banking Corp. (Japan); and
- United Overseas Bank (Singapore).

The lineup was nonetheless revealing. All three of Japan's giant banks received licenses, reflecting the size and increasing regional ambitions of these institutions as well as Japan's own substantial investment in its Myanmar diplomacy. The two Singapore banks were likewise expected, especially given Singapore banks' traditional roles of facilitating high-end financial services for Myanmar's elite and providing the means by which the less privileged working in the region send money home to Myanmar. No one could have doubted that at least one bank

from Thailand, Malaysia, and China would be included (the first and last of these being the largest of Myanmar's trading and investment partners), while Australia's ANZ took the single Western bank slot. A last-minute decision by Standard Chartered not to submit an application made ANZ a near certainty, especially given that its only competitor was a somewhat unlikely bid from a small French bank.[77]

LOCAL OPPOSITION AND A RESTRICTIVE MANDATE

The arrival of foreign banks in Myanmar took place amidst the stiff opposition of most of the local players, who spent considerable time and resources first in resisting their entry and then, once foreign banks had been approved, in limiting foreign banks' allowable activities. The local banks were worried about their ability to compete with the new foreign banks, with most seeing these foreign banks as an existential threat and, perhaps for some, also seeing them as a welcome source of salvation. The chair of Yoma Bank suggested at a conference in August 2015 that the arrival of the foreign banks pointed to the strategic direction in which local institutions needed to move:

> At the top end of the market, local and foreign banks are fighting over a few thousand clients. Tactically, if you continue with that strategy as a local bank you will be challenged. The competencies of the foreign banks are much higher, the technology is better, the balance sheet is bigger. Local banks will need to adapt and go down-market, to the SMEs [small and medium-sized enterprises] where it is almost impossible for the foreign banks to follow.[78]

Lest this sound like a retreat, the Yoma chair also made clear that this foreign banking segment of the market was also the most important for Myanmar's future. Noting that the local banks needed to learn structural modernization and technology from the foreign competitors, he also suggested that what they needed was confidence: "The local banks should be very confident in what they can do …. They have a better understanding of the local market, something foreign banks cannot buy."[79]

Coming to a similar conclusion was Dr. Sein Maung. Summarizing hopes, fears, and tensions, he declared that Myanmar would not be ready for any *more* foreign banks until they came up with concrete ways to transfer skills to local players:

> Without a strategy it's just lip-service. Technology and software we can buy, but when it comes to improving skills and knowledge, we have to rely on the foreign banks. I expect a lot from them, as without their cooperation we can't learn much.[80]

[77] The French bank was BRED (*Banque Populaire S.A.*), a cooperative bank with over 250 branches in France and, of relevance here, 75 branches in French overseas territories. Via a subsidiary, COFIBRED S.A., the bank also partnered with the IFC and the German development bank KfW to bring the Cambodian microfinance bank, ACLEDA, to Myanmar (examined elsewhere in this paper).

[78] Quoted in Clare Hammond, "Foreign Banks Call for Market Access," *Myanmar Times*, July 28, 2015, http://www.mmtimes.com/index.php/business/15702-foreign-banks-call-for-market-access.html, (accessed November 2, 2015).

[79] Quoted in Khine Kyaw, "Myanmar, Foreign Bankers See Need for Closer Cooperation," *The Nation*, August 3, 2015, http://www.nationmultimedia.com/business/Myanmar-foreign-bankers-see-need-for-closer-cooper-30265739.html, (accessed November 2, 2015).

[80] Quoted in Clare Hammond, "Foreign Banks Call for Market Access," *op. cit.*

Foreign banks are restricted in significant ways and quarantined from many parts of Myanmar's financial sector.

Japan's Bank of Tokyo-Mitsubishi UFJ (MUFJ) and Singapore's United Overseas Bank (UOB) are especially active, both in the size and scope of their activity and the extent to which they are already pushing up against the regulatory limits of activity.

Notwithstanding these opinions, foreign banks are restricted in significant ways and quarantined from many parts of Myanmar's financial sector. Among the requirements and restrictions imposed on them are:

- Minimum paid-up capital of US$75 million;
- One branch only;
- An income tax rate of 35 percent (versus 25 percent for local banks);
- A prohibition on lending to Myanmar nationals or enterprises, except in partnership with a local bank; and
- A ban on taking deposits from Myanmar nationals.

The *Transfer of Immoveable Property Act* also imposes restrictions. It prohibits foreigners from taking land as collateral, so even if foreign banks were permitted to lend to local firms these loans would be limited. On the other hand, the interest rate floors and caps imposed on the local banks do not apply to the foreign entities. The end result of all of this? The foreign banks in Myanmar are relegated in essence to the providing financial services to other foreign investors. In many, even most cases, these will be investors who hail from the same countries from which the individual banks themselves come.

LICENSED FOREIGN BANKS

By the end of October 2015, all nine foreign banks granted provisional entry the previous year had moved forward. Licenses were received, offices had been established, and various outreach activities extended (most of the foreign banks have training and technology-sharing agreements with local banks). Modest beginnings in banking business itself were also made, thus far mostly consisting of (as expected) facilitating the trade and funding needs of home country investors in Myanmar.[81]

However, a couple of the banks have been more adventurous. Japan's Bank of Tokyo-Mitsubishi UFJ (MUFJ) and Singapore's United Overseas Bank (UOB) are especially active, both in the size and scope of their activity and the extent to which they are already pushing up against the regulatory limits of activity.

MUFJ, the first of all the foreign banks to arrive, brought US$100 million in capital (an additional US$ 25 million over the US$75 million minimum) and in August 2015 made the first unambiguous local currency loan by a foreign bank: K900 million (around US$740,000) to a Japanese/Myanmar joint venture trading house.[82,83] MUFJ's Myanmar operation lends in Singapore dollars and euros, as well as U.S. dollars, and currently has around 120 customer

[81] ANZ Bank, the most globally-focused of Australia's large banks, is representative in this context. Apart from a commitment to service multinationals and companies broadly wanting to access Myanmar, ANZ has made a point of stressing its (and, by extension, Australia's) strength in "natural resources, infrastructure and agriculture." See ANZ Bank, "ANZ Receives Final Myanmar Banking License Approval," ANZ Bank news release, September 30, 2015, http://www.media.anz.com/phoenix.zhtml?c=248677&p=irol-news&nyo=0, (accessed November 1, 2015).

[82] Of historical interest: one ancestor of the much-merged MUFJ is the Yokohama Specie Bank (YSB). An extraordinary institution that financed much of Japan's involvement with the rest of the world in the first half of the twentieth century, the YSB was active in colonial Myanmar from 1914. During the Japanese occupation of Myanmar (1942–1945), it even effectively served for a while as the central bank. After the war, YSB was reorganized into the Bank of Tokyo (Turnell 2009).

[83] Taiga Uranaka, "MUFG is First Foreign Bank to Make Myanmar Currency Loan," *Reuters*, August 6, 2015, http://www.reuters.com/article/2015/08/06/mufg-myanmar-idUSL3N10H1R820150806, (accessed August 11, 2015).

firms. Over 80 percent of these customers are subsidiaries of Japanese corporations, though the bank also includes among its clients Coca-Cola and Unilever. So far, MUFJ has collected around US$70 million in deposits in Myanmar. It has also borrowed in kyat from local banks to augment its local currency capacity.

UOB made the first onshore foreign currency loan by a foreign bank in May 2015 and had loan commitments across its first year of business of over US$300 million.[84] The other banks that have brought in significantly more capital than the regulatory minimum are Bangkok Bank (US$200 million) and Sumitomo Mitsui (US$200 million).[85] Meanwhile, Mizuho Bank was the first to take advantage of the relaxed conditions allowed by Myanmar's special economic zones (SEZs), by opening a second office in November 2015 at the Thilawa SEZ, a special economic zone that has attracted the support of the Japanese government and the investment of a number of Japanese corporations.[86]

JOINT VENTURE BANKS?

The idea that local and foreign banks could form joint venture operations has survived the arrival of the foreign banks. Pushing the model rather more than most, however, is Taiwan's Cathay United Bank, which also has a funding arrangement with KBZ. Cathay United has such a joint venture subsidiary (Indovina Bank) in partnership with Viet Nam's largest (partly-)private bank, Vietinbank. Others are less convinced. Singapore's largest bank, DBS (a surprise omission from the foreign bank license winners) regarded looser partnerships that bring in new technologies and ideas as plausible, but saw joint venture arrangements as posing a risk of reputational damage: "If foreign banks take an interest in a local bank and there is a scandal, it will taint the reputation of the entire group."[87] First Private Bank's Dr. Sein Maung also had misgivings, albeit from a very different angle. Noting that foreign banks were vital to the local banks "when it comes to improving skills and knowledge," he added that it has proven challenging to find possible foreign bank partners because the foreign banks require, unacceptably, 80 percent ownership of prospective joint ventures.[88]

SECOND ROUND OF FOREIGN BANK ENTRY

In February 2016 the CBM announced a second round of foreign bank applicants. Thirteen pre-qualified applicants were named:[89]

- Bank for Investment and Development of Viet Nam,
- Cathay United Bank (Taiwan),
- CTBC Bank (Taiwan),
- E.SUN Commercial Bank (Taiwan),
- First Commercial Bank (Taiwan),
- Kookmin Bank (South Korea),
- Mega International Commercial Bank (Taiwan),
- Shinhan Bank (South Korea),
- State Bank of India,
- State Bank of Mauritius,
- Taiwan Business Bank,
- Taiwan Cooperative Bank, and
- Taiwan Shin Kong Commercial Bank.

The most interesting aspect of the list of new applicants is the preponderance of banks from Taiwan (8 of the 13). The list is not, however, random: banks from countries that already have a licensed banking entity in Myanmar were automatically excluded. As with the first round of foreign bank entry, each applicant was given a period in which to set up operations and to ensure functional banking operations before the license itself would be awarded at the end of first quarter 2016.

[84] Siow Li Sen, "UOB Helping Clients Invest in Myanmar," *The Business Times*, June 30, 2015, http://www.businesstimes.com.sg/banking-finance/uob-helping-clients-invest-in-myanmar, (accessed November 2, 2015).

[85] Sara Perria, "Foreign Banks Go Native with a Flourish in Myanmar," *Nikkei Asian Review*, June 11, 2015, http://asia.nikkei.com/Business/Trends/Foreign-banks-go-native-with-a-flourish-in-Myanmar, (accessed November 2, 2015).

[86] "Mizuho Bank to Open Office at Thilawa," *Bangkok Post*, November 3, 2015, http://www.bangkokpost.com/news/asean/753148/mizuho-bank-to-open-office-at-thilawa, (accessed November 4, 2015).

[87] Chief Executive of DBS Group Sin S. Lim quoted in Clare Hammond, "Foreign Banks Call for Market Access," *op. cit.*

[88] Ibid.

[89] Central Bank of Myanmar, "Information Regarding the Award of Banking License in the Republic of the Union of Myanmar," *Central Bank of Myanmar Press Release*, February 6, 2016, http://www.cbm.gov.mm/sites/default/files/regulate_launder/20160208_press_release_final_0.pdf, (accessed February 8, 2016).

8. THE NEW FINANCIAL INSTITUTIONS LAW OF MYANMAR

In essence, the FIL is a very good law; if it is implemented properly it *could* reinvigorate the reform process in Myanmar.

However, the FIL will present significant challenges to the incumbent local banks in Myanmar, as well as to their owners and senior executives.

The need for new legislation governing the activities of financial institutions grew more obvious and urgent during the Thein Sein administration: to drive forward reform, place domestic regulation in conformity with international norms, and to better support (the many) technological and methodological changes in banking over the last two decades. The old overarching law, the *Financial Institutions of Myanmar Law* (FIML), promulgated in 1990, more often disregarded than observed, had become obsolete. Implementing and observing laws matters more in Myanmar than simply writing and passing them. Nevertheless, the time to replace the FIML had come.

In December 2014 a draft new *Financial Institutions Law* (FIL) made its long-awaited appearance. Written under the auspices of the CBM, the draft FIL was largely the creation of the World Bank and other international advisers, and accordingly incorporates much of international best practice in bank regulation, as well as measures and devices that are successfully employed elsewhere in the region. In essence, the FIL is a very good law; if it is implemented properly it *could* reinvigorate the reform process in Myanmar. At the time of writing (January 2016), the FIL has been passed by both of Myanmar's houses of parliament and, accordingly, has become law. It will be implemented through enabling rules and regulations that had yet to appear.

However, the FIL will present significant challenges to the incumbent local banks in Myanmar, as well as to their owners and senior executives. Given how successful these banks and executives were in pushing back against foreign bank entry (noted above), a keen struggle can be expected. Such a struggle, and its outcome, will reveal the extent to which Myanmar might emerge with a competitive open economy, or one that is crony-dominated and state-centred. Some of the key features of the FIL include:[90]

[90] The draft is available on the CBM website, http://www.cbm.gov.mm/content/1075, (accessed October 29, 2015).

- All existing banks must be authorized under the new law, and thus all bank owners, senior executives, and board members must meet the FIL's various "fit and proper person" tests. Such tests are standard everywhere, of course. However, despite being greatly needed in Myanmar in order to build a strong and trusted banking sector, and being paid lip-service in Myanmar's existing banking laws, these tests have hitherto largely been ignored.
- In being reauthorized under the FIL, all existing banks must surrender their banking licences within six months of the new law coming into effect. This requirement has caused concern among Myanmar's private banks, anxious that potential doubts arising from this process could cause nervousness among depositors and other creditors.
- It establishes requirements for capital adequacy, liquidity, large exposure limits, and other measures that carry with them the lessons from the 2008-09 global financial crisis, and could be regarded as state of the art in bank supervision. Yet, and not withstanding how "best practice" they are in a global sense, they are also adapted to the particular circumstances and difficulties in a country such as Myanmar.
- All banks must have a minimum capital of K20 billion.
- It establishes some very necessary restrictions on lending to related parties. Such loans must be approved by a minimum of a two-thirds majority decision of a bank's board, and the loans must fully meet existing collateral requirements.

The new features offer some promising possibilities and a few areas to watch with caution:

- The restriction on lending to related parties, as well as disclosure requirements regarding the interests of bank directors, transparency rules on holding companies and the like, should add to the measures above in overhauling Myanmar's banking sector.
- The FIL has some good sections dealing with money laundering. As noted earlier, Myanmar has often been criticized for falling short in this area. The provisions in the FIL would, if implemented, effectively address this otherwise significant barrier to international dealings with Myanmar's banks and their customers.
- The FIL has some very forward-looking provisions for authorizing e-money, e-banking, mobile banking, and other emerging technologies. It also encourages the creation of credit bureaus. All of these have much potential, and their effectiveness is amply demonstrated elsewhere in emerging markets, not least in Africa.
- The FIL has some very well developed proposals for unwinding and (potentially) rehabilitating failing and failed banks. All are very state of the art, and with the lessons of 2008-09 at the forefront.
- One negative aspect of the new FIL is its maintenance of a broad hostility toward foreign finance. In this case, it is in the form of an injunction against foreign "nonbank financial institutions" (NBFIs). Foreign NBFIs can open representative offices under the FIL, but they are not permitted to offer financial services.
- Meanwhile, a significant omission in the FIL are references to the state-owned banks. These are seemingly not captured within its remit, thus continuing (even exacerbating) regulatory distortions and misdirection on the state/private divide in banking in Myanmar.

If *properly applied*, the FIL will rule out of banking many of the existing and dominant personalities.

Some areas will clearly raise the hackles of some of the incumbent local banks. Stated simply, if the law is properly applied, many current bank owners and executives will fail "fit and proper person" tests, while the activities of their banks will breach connected lending injunctions. In short, if *properly applied*, the FIL will rule out of banking many of the existing and dominant personalities.

The new FIL is well-crafted banking legislation. It incorporates a great many regulatory innovations arising out of experience during the global financial crisis and is cognizant of many of the other developments that affect modern banking (not least in the areas of e-banking and cyber security and standards). It is also an extraordinarily complex piece of legislation. Such complexity may be something of a problem. Myanmar's banks are not yet compliant with the basic Basel I prudential and capital adequacy framework, let alone the Basel II, III, and IV follow-ups.

9. RURAL FINANCE

Myanmar's agricultural sector, the source of livelihood of over 70 percent of the country's population, is chronically undercapitalized.

Myanmar's agricultural sector, the source of livelihood of over 70 percent of the country's population, is chronically undercapitalized.[91] Few farmers enjoy any access at all to formal finance, and those that do receive far less than they need. Informal finance—family, friends, local moneylenders—are the recourse of most people in rural Myanmar, but such finance is expensive, unreliable, all too-often socially destructive, and no more sufficient than its formal counterpart.

MYANMAR AGRICULTURAL DEVELOPMENT BANK

The Myanmar Agricultural Development Bank (MADB) was created in 1953 to provide Myanmar's farmers with the affordable credit they needed and is the only financial institution to serve this population for much of its history. Myanmar's second largest bank in terms of branch outreach (around 220 branches throughout the country), the MADB currently claims around 2 million customers (Nilar Win 2013, 6; World Bank 2014).

The MADB's problems are myriad, fundamental, and chronic.

The MADB's problems are myriad, fundamental, and chronic. They are embedded in the bank's authorizing legislation, in its practices, in its deficient and obsolete infrastructure, and in its organizational culture.[92] They include:

The MADB's Lending Is Insufficient and Too Narrow

- The MADB offers seasonal crop production loans (terms of less than 1 year) and term loans (a) 1-3 years or (b) more than 3 years. The former represented 98 percent of its outstanding loans in 2014 and was concentrated on production of just four commodities—paddy, sesame, peanuts, and beans. It provides no funding for other fruits and vegetables, the rearing of livestock, food processing, or just about any other activity up or down the value chain (World Bank 2014, 19).
- Despite this narrow concentration, even the financing of the four crops falls well short of need. The MADB provides production loans only for the first 10 acres of cultivation per farm, and in the case of paddy—by far the dominant crop, comprising nearly 90 percent of cultivator loans by value—only up to K100,000 per acre. This amount is significantly up from previous years; however, it is still notably less than average per acre paddy production costs,

[91] Less than 3 percent of all formal lending in Myanmar goes to the rural sector (OECD 2014, 208).

[92] The worst limitations with respect to the performance of the MADB are not due, however, to restrictions in the *Myanmar Agricultural Development Bank Law* (as amended in 1996). That said, plans to modify the law—a necessary but not sufficient condition if the bank is to be turned around; were reportedly afoot. See "Plan to Improve Myanmar Agricultural Development Bank Law," *The Global New Light of Myanmar*, January 26, 2015, http://globalnewlightofmyanmar.com/plan-to-improve-myanmar-agricultural-development-bank-law/, (accessed August 4, 2015).

which range from K200,000 for poor quality rice to K400,000 for high quality rice. In short, even farmers who receive MADB loans are significantly underfunded. The average size of an MADB loan is around K200,000 (approximately US$170).

- There are significant differences in access according to farm size. According to Making Access Possible (2014, 9) 54 percent of farmers with plots of 10 acres or larger have access to MADB loans, a ratio that falls to just 24 percent for farmers who have plots of 2 acres or less.
- Term loans (of up to three years) are meant to be available for longer-maturing crops such as sugarcane, tea, and coffee. However, in 2012, such loans amounted to little more than 2 percent of the MADB's total portfolio, with sugarcane taking the dominant share.
- The MADB devotes a tiny amount of funding (0.02 percent of its portfolio in 2014) for farm machinery. Such loans cover only up to 50 percent of the value of the machine in question, which serves as collateral for the loan (World Bank 2014, 21).
- Apart from these limited loans for machinery, MADB loans are purely for funding working capital. No loans are currently provided for longer-term investment. Other financial instruments routinely employed by farmers elsewhere in the world (such as warehouse receipt financing, letters of credit, trade finance, and leasing) are not offered.
- In addition to narrowly defined loan purpose, borrowing from the MADB is also restricted in other ways. As noted below, the MADB conducts no credit assessment of borrowers, but entire townships are excluded from its lending if any of their inhabitants are in default against past loans. Likewise, many cultivators in Myanmar are without formal use-title over the lands they farm. According to the World Bank (2014, 17), the number of potential borrowers excluded in this way is estimated at around 3.5 million—one and a half times the number of farmers currently given loans.
- One of the most damaging aspects of MADB's loans is that they must be repaid, in full, at harvest. Given the great poverty of the majority of Myanmar's farmers and their lack of financial reserves, this means that near-universally they must sell their crops immediately at harvest—precisely at the moment at which, furiously competing against each other, the prices they can yield for their product are at their lowest.

The MADB Is Financially Unsustainable

- The MADB has no control over the interest rates it charges and pays on its loans and deposits. These are set instead by the Ministry of Agriculture and Irrigation. After a reduction in June 2014, the MADB charges a highly subsidized rate of 5 percent a year on its loans (down from a range of 13–18 percent, while 8 percent was paid on deposits) (World Bank 2014).[93]

[93] Kyaw Ko Ko, "State Bank Lowers Interest Rates on Loans to Farmers to Stimulate Growth," *Myanmar Times*, May 29, 2014, http://www.mmtimes.com/index.php/business/10518-state-bank-lowers-interest-rates-on-loans-to-farmers-to-stimulate-growth.html, (accessed August 4, 2015).

- The MADB is currently operating on an interest rate margin of just 0.5 percent (MAP 2014, 10). According to MAP, the MADB currently subsidizes its average borrower (with respect to the average loan size) at around US$15 (MAP 2014, 19).
- For most of its history, the MADB has been unable to fund its lending through deposits accumulation. The country's long history of monetary instability, and the wariness with which Myanmar's rural populace regarded the MADB in particular, meant that savings mobilization through the bank was never more than marginal. In recent years however the MADB has been discouraged from seeking deposits, not least by Myanmar's parliament amidst (justifiable) concerns that withdrawals were made too difficult. According to the World Bank (2014, 23) more than 90 percent of the MADB's deposits have been withdrawn since 2011.
- In the absence of necessary deposits, the MADB depends upon subsidized borrowings from its state-owned sibling, the Myanmar Economic Bank (MEB), to fund lending. The MEB currently provides funds to the MADB at a 4 percent per year interest rate; the extent of the subsidy is readily apparent given that the MEB must pay 8 percent per year on its own deposits. As the World Bank (2014, 9) notes, it is the Myanmar government that must bear the cost of MADB loans and the fiscal burden they impose.
- Exacerbating the MADB's lack of financial sustainability is a long-standing requirement (written in the 1990 *Myanmar Agricultural Development Bank Law* itself) that 75 percent of the bank's profits be transferred annually to the state. This significantly reduces the MADB's ability to likewise use retained earnings to boost the bank's currently (inadequate) K1 billion authorized capital base.

Risk Management at the MADB Is Largely Non-Existent

- The MADB undertakes no credit analysis or other assessments of its borrowers. Instead, credit committees from villages in townships that are not in arrears on previous loans automatically approve loans once relevant documentation has been completed. MADB staff are not represented on these committees, nor do they play an advisory or other role.
- In place of individual credit assessment, the MADB lends to farmers in groups of between 5 and 10 people, who collectively guarantee each other's loans. Such joint-responsibility "contracts," though widely employed beyond Myanmar, are the source of much resentment among the country's agricultural producers.
- The concentration of the MADB's lending in a very narrow range of commodities and activities, uncollateralized and largely undiversified, only aggravates the risks the bank faces.[94]

[94] Myanmar's fitful introduction of new farmland laws will give an increasing number of farmers use title over their land. Such title *may* at some point provide the MADB and other banks with collateral against rural lending, but much remains to be done. For a discussion of Myanmar's new land laws, and their problems and complexities, see Fink (2015).

The MADB Does Little to Promote Financial Inclusion

- While the MADB has the second-largest branch network of any bank in Myanmar, these branches are too few to provide for genuinely inclusive outreach. Its branches are within a reasonable distance for less than half of Myanmar's farmers. As a result, for the majority of potential borrowers, access to the bank entails considerable travel costs.
- Contrary to best practices in rural finance, MADB staff are not permitted to travel to villages and no mobile banking platforms have as yet been developed.
- The inaccessibility of the MADB's branches is mirrored in difficulties of internal communications within the bank. The MADB's information-technology infrastructure is inadequate and obsolete, communications and the movement of money between the head office and branches takes place mostly through post, fax, and physical transfer, with all the attendant inefficiencies and risks these entail.

The MADB's Internal Systems Are Obsolete and Inadequate

- The MADB uses paper-based documents for all records and has very limited IT systems for data retention and analysis.
- Communication with customers is similarly rudimentary. In its 2014 analysis of the MADB, the World Bank concluded that under its current operational arrangements:

  > …it is difficult for MADB to manage customers' accounts and notify customers of their debt burden. With the existing system, it is hard for the bank's management to perform its business functions and manage risks. (World Bank 2014, 30)

MADB Governance Is Poor

- The MADB is not supervised by the CBM. Indeed, it is not formally a bank under the *Financial Institutions of Myanmar Law*, but a stand-alone entity of the Ministry of Agriculture and Irrigation. Accordingly, the MADB is not required to meet, and is unlikely to meet, any of the prudential requirements imposed on banks under any of Myanmar's laws pertaining to financial institutions.
- The World Bank concludes that corporate governance within the MADB broadly is "weak" (2014, 9). The bank's board has no independent members and is comprised of individuals solely drawn from the agriculture ministry. The board meets infrequently and none of its deliberations, nor those of the MADB's senior management, are made public. The chairman of the board is the agricultural minister. The MADB has no audit committee, and its accounts are neither independently audited nor prepared in compliance with international accounting standards.
- Most senior staff are political appointees (many are retired military personnel) with little or no knowledge of rural finance methodologies. The MADB's professional staff, who are often skilled in such techniques (most of its 2,000-plus staff have bachelor degrees), enjoy little operational autonomy (World Bank 2014, 31).

- Notwithstanding its very public role, the MADB is the only state-owned bank not to have a website.

MADB and the Floods

Adding to the MADB's longer-term woes, though in large part yet another manifestation of its inability to deal with Myanmar's challenging environment, has been the damage wrought by the country's July-August 2015 floods. The destruction affected about 20 percent of Myanmar's cultivated area, temporarily displaced 1.6 million people, and caused economic losses equivalent to about 3 percent of Myanmar's FY2014/15 GDP (Government of the Union of Myanmar 2015). Clearly, a sizeable number of the MADB's borrowers were badly affected, and their loans compromised accordingly. The end of the current season in April 2016 will reveal the extent of the loan losses. More broadly, this latest natural disaster highlights the MADB's exposure to natural disasters in a country often afflicted by them.

SOME INITIATIVES BEYOND THE MADB

The overbearing but dead weight of the MADB, along with the notable lack of substantial reform more broadly in Myanmar's agricultural sector (a standout failure of the Thein Sein administration), has precluded much in the way of private sector initiatives in rural finance. However, this is not the whole story. In 2014, plans emerged, for instance, for a Farmers Development Bank (FDB).[95] Created by the Myanmar Farmers Development Party, the FDB principals proposed to raise capital of K30 billion. Majority ownership of the FDB is meant to reside with party members and other farmers (51 percent), with foreign investors participating as well, although this last aspect would require a special dispensation from the CBM.[96] The FDB reportedly signed a memorandum of understanding with Thailand's Krung Thai Bank to provide technical assistance and to "invest in the business."[97] As of this report, nothing appeared certain, even if a functioning private agricultural bank is certainly called for.

In late 2015 a similar institution, no less dimly lit in what is publicly known about it, was announced in the form of the "Ayeyarwaddy Farmers Development Bank" that may trade under the name of "Abank." This bank, founded by a consortium that includes the Ayeyarwady regional government and 15 partners of the Ayeyar Hinthar Companies Group, is ostensibly about supporting agriculture in its broadest sense, including support to millers, livestock producers, and rubber producers, as well as factories that may emerge.[98] Abank is also looking at linking with the foreign

[95] "Myanmar Opposition Party to Set Up Agricultural Bank," *Nikkei Asian Review*, October 25, 2014, http://asia.nikkei.com/Business/Deals/Myanmar-opposition-party-to-set-up-agricultural-bank, (accessed October 23, 2015). Thurein Hla Htway, "Banking on the Farm Vote," *Nikkei Asian Review*, March 6, 2015, http://asia.nikkei.com/Politics-Economy/Policy-Politics/Banking-on-the-farm-vote, (accessed October 23, 2015). Specific CBM regulations upon the MFDP can be found at the central bank's website http://www.cbm.gov.mm/content/873, (accessed October 23, 2015).

[96] A dispensation seemingly given, among other concessions, courtesy of the specific regulations for the FDB. See the CBM's dedicated regulations, http://www.cbm.gov.mm/sites/default/files/regulate_launder/regulation_for_farmer_development_bank.pdf, (accessed November 5, 2015).

[97] "Myanmar Opposition Party to Set Up Agricultural Bank," *Nikkei Asian Review, op. cit.*

[98] Chan Mya Htwe, "Ayeyar Hinthar Opens Ayeyarwaddy Farmers Development Bank," *Myanmar Times*, December 1, 2015, http://www.mmtimes.com/index.php/business/17892-ayeyar-hinthar-opens-ayeyarwady-farmers-development-bank.html, (accessed December 3, 2015).

banks, retailing the wholesale funds the latter can provide. At the time of writing, no details with respect to capital, proposed branch network, and the like were available.

SLCM

Perhaps the most promising of all of the initiatives in rural finance during the Thein Sein administration has been the warehouse/collateral management arrangement introduced by the Indian agri-logistics firm Sohan Lal Commodity Management (SLCM). This arrangement, under which farmers are given advances against the collateral of their stored crop, is a time-honored one that allows farmers to receive funds they need while allowing them to time the arrival of their crop to the market. At present, and for many decades, Myanmar's farmers have had to sell their product more or less immediately upon harvest, at which time the prices they can command are at their minimum. Allowing farmers to store their product to better time its arrival in the market (as they did in the colonial era in Myanmar, when some of the European banks had in place similar arrangements) can potentially greatly increase their incomes.[99]

SLCM's arrival in Myanmar has been in partnership (briefly noted above) with some of the country's leading private banks (Yoma, CB Bank, United Amara). The banks lend against the warehouse receipts supplied by SLCM against the commodities stored by the farmers. This collateralized lending against product safely in the hands of a trusted third party minimizes risks and transaction costs to the lending banks. Naturally, the three banks charge the standard maximum lending rate against the loans of 13 percent per year. The maximum size of a loan against a farmer's crop is 60 percent of the value of the stored commodity.[100] At present the arrangement is modest. By late 2015, around US$1 million worth of loans had been disbursed against 15 commodities stored in warehouses of a capacity of around 100,000 square feet.[101]

Perhaps the most promising of all of the initiatives in rural finance during the Thein Sein administration has been the warehouse/collateral management arrangement introduced by the Indian agri-logistics firm Sohan Lal Commodity Management (SLCM).

Allowing farmers to store their product to better time its arrival in the market can potentially greatly increase their incomes.

[99] Lloyd's Bank and Chartered Bank were the pioneers for the method in Myanmar in the early years of the 20th century. For more, see Turnell (2009).

[100] Zaw Htike, "Yoma Bank, Indian Firm Plan Warehouse Receipt Financing," *Myanmar Times*, January 26, 2015, http://www.mmtimes.com/index.php/business/12884-yoma-bank-indian-firm-plan-warehouse-receipt-financing.html, (accessed October 19, 2015).

[101] "Agri-logistics Firm SLCM Group to Foray into ASEAN, African Regions," *Economic Times*, July 5, 2015, http://articles.economictimes.indiatimes.com/2015-07-05/news/64112229_1_agri-logistics-rs-50-crore-disbursement, (accessed October 19, 2015).

10. INFORMAL FINANCE: UBIQUITOUS AND TIME-HONORED

Simply talking to people in Myanmar from all walks of life, and from the poorest to the wealthiest and most-connected, makes manifest the utter ubiquity of this informal realm.

All of these informal sources of credit have been around in Myanmar for centuries.

CREDIT AND SAVINGS

The myriad of problems with the MADB compels many farmers in Myanmar to find alternative credit in the informal credit sector. Needing to plug the funding gap of inadequate MADB loans and meet the repay-at-harvest requirements, farmers borrow from commodity brokers, input suppliers, informal moneylenders, family, and friends.

Of course, the MADB's failures are just one element in the persistence of informal finance in Myanmar. The broader lack of trust in formal financial institutions, along with the great weight of history, practice, and familiarity, is key to the survival of arrangements that continue to dominate the financial landscape of most of Myanmar's citizens. According to MAP focus group surveys, respondents had:

> ... positive perceptions about using financial services offered by unregulated financial service providers … because they felt that these were more convenient and that the requirements set by regulated financial institutions excluded low-income earners. Respondents indicated that although unregulated providers charged high interest rates for credit, they were the preferred choice because of their proximity, flexible operating hours, immediate relief and negotiable borrowing terms. (MAP 2014, 15)

The overall scale of the informal sector in the Myanmar economy, which employs an estimated 65 percent of the country's working population, also influences the scale of informal financing. The MAP data (in Section 2 of this paper), which suggest that the informal financial sector was at least as large as its formal counterpart, provide one snapshot of this, but simply talking to people in Myanmar from all walks of life, and from the poorest to the wealthiest and most-connected, makes manifest the utter ubiquity of this informal realm.

Informal finance in Myanmar takes many forms. Table 8 gives the broad categories of informal finance providers, the interest rates they charge, the collateral they demand (if any), and the loan size and repayment terms they offer.[102]

All of these informal sources of credit have been around in Myanmar for centuries. Informal moneylenders have more or less always been ubiquitous, but they loom largest in Myanmar's broader history in the episode of the *Chettiars*, a money-lending caste from Tamil Nadu in India who became instrumental in financing the country's transformation into the world's largest rice exporter by the early twentieth century. In the colonial era, the *Chettiars* were the critical conduit through which the funds of the exchange banks, largely European, were distributed to the cultivators

[102] The information collected in this table is derived from scores of interviews and other field research by the author down the years. It has been cross-checked against data reported by Proximity Designs in its 2014 report on financial inclusion in rural Myanmar.

TABLE 8: INFORMAL CREDIT PROVIDERS IN MYANMAR

Informal Finance Provider	Interest Rate Charged	Collateral Type	Loan Size	Loan Term
Informal Moneylenders	10-20%/month	Usually none	Negotiable	Day minimum/month maximum
Rotating Credit & Savings Associations (ROSCAs)	3-5%/ month	Peer pressure/social capital	Up to around K1 million	Maximum of around one year
Agricultural Merchants/ Brokers	4-5%/ month	Repeat Business Relationship	Usual value of harvest	Harvest period (~6 months)
Pawnshops	2-20%/ month	Gold and other items	Based on collateral	Maximum of 4-5 months[103]

in the countryside. *Chettiar* lending methodologies (detailed in Turnell 2009) foreshadowed many of those at the cutting edge of rural and microfinance providers today, and they provided financing for Myanmar's rice sector for many decades. But the *Chettiar* story did not end well. With the arrival of the Great Depression came mass land alienation as defaulting borrowers surrendered their land as collateral to the *Chettiars*. Then came the Second World War, the expulsion of the *Chettiars* by the invading Japanese, and a post-war settlement in newly independent Myanmar that made clear the *Chettiars* would not be welcome back.

Today Myanmar's informal moneylenders are overwhelmingly from the same ethnic background as the communities in which they operate. As can be seen from Table 8, the interest rates they charge are high, but their procedures, paperwork, and other requirements are not especially burdensome. Who are these moneylenders? They come in myriad forms. Some are relatively rich local landholders, the most prosperous of the farmers of a village or tract. Some are professionals, in that moneylending is more or less the heart of their business. Many are local shopkeepers. Many are simply Burmese women, "aunties" with some cash to spare and a need to supplement their own families' incomes. According to MAP (2014b, 15), there are an estimated 400,000 informal moneylenders in Myanmar—or roughly one for every 1,000 adults in the country.

Rotating Savings and Credit Associations (ROSCAs), as labeled in Table 8 and so called in the academic vernacular, are likewise endemic throughout Myanmar. They go under different labels according to local custom, with many bearing the name of *Su Kye*. All share the same basic methodology as community groups, with up to 20 members who pool savings, usually on a weekly basis, and take turns drawing or borrowing from the collective "pot." ROSCAs depend greatly on trust and, as such, their membership often comprises people who work together or enjoy some other binding social ties. Breaches of trust by members are not unknown, but are readily punished through social censure. Apart from being commonplace throughout Myanmar, ROSCAs are also a familiar feature of Burmese refugee communities in neighboring countries.

Credit advanced by commodity brokers and middlemen, which in other countries has been the subject of much research and celebration (often relabeled as value chain finance), has existed in Myanmar from the earliest days. It is perhaps an obvious relationship for the extension of credit, but in Myanmar it is costly (especially as compared to the MADB-subsidized loans that levy just 5 percent a year and banks that levy 13 percent) and is not, at least yet, potentially transforming in the way that truly innovative value chain finance has come to be. Commodity broker finance was ubiquitous and formalized during the colonial era, when it was provided, at base, by European trading enterprises. After Myanmar became independent, it continued to play a formal role in rice production in the form of advanced purchase by the State Agricultural Marketing Board (SAMB). For much of its existence (under this and later names), the SAMB enjoyed a monopoly over the buying and selling of paddy in Myanmar (Turnell 2009).

The interest rates they charge are high, but their procedures, paperwork, and other requirements are not especially burdensome.

[103] In Yangon, the local government (the Yangon City Development Committee, YCDC) has set the maximum pawnshop term at 4 months, 10 days.

Because many people in Myanmar are remote from, excluded from, or untrusting of banks and other formal institutions, savings primarily take the form of items of intrinsic value.

As with all of these informal financial instruments and arrangements, pawnshops are likewise ancient and ubiquitous in Myanmar. Pawnshops in Myanmar take many forms—from the 184 outlets of the state-owned Myanmar Small Loans Enterprise (MSLE), to private pawnbrokers registered with the MSLE and with local authorities (just over 1,800), to informal and unregistered operators offering tiny sums at very high interest rates (MAP 2014, 6). Many pawnbrokers only accept gold and other items of value, while others will lend against household items of next to no intrinsic value but of high *use value* to their owners. The maximum loans extended are typically no more than about 65 percent of the value of the pawned item if it had to be sold. Recourse to pawn brokers has traditionally transcended wealth and class, but in recent times (with the rise of private banks, credit cards, and other facilities) it has become more a practice of the poorer sections of Myanmar society.[104]

On the savings side of the equation, informality is again the dominant feature in the financial landscape of most of Myanmar's citizens. Because many people in Myanmar are remote from, excluded from, or untrusting of banks and other formal institutions, savings primarily take the form of items of intrinsic value, with the exact type depending upon wealth and occupation. Thus savings take the form of gold, jewelry (often worn, especially for women as bangles), stored paddy, other durable foodstuffs, and cash (with fresh U.S. dollar bills greatly preferred). All of these items are overwhelmingly stored in the home and its surrounds, in boxes, trunks, tins, pots, and sometimes even safes. Of course, the ROSCAs noted above are a social mechanism by which kyats are saved in another informal way. As with every facet of the informal sector, informal savings are a feature of most households in Myanmar. Few of the richest residents of Myanmar will be without gold or the ubiquitous wad of pristine US$100 notes.[105]

INTERNATIONAL REMITTANCES

For many developing countries, the money sent by their citizens from abroad constitutes a larger source of foreign exchange than international trade, aid, or foreign investment.[106] According to the

[104] For an interesting window into the life of a small-scale, unregistered pawnbroker and his clients, see Joshua Carroll, "Inside Myanmar's Pawn Shop Culture: 'We Wouldn't Accept Filthy Kitchen Utensils, or Used Underwear,' " *The Guardian*, April 27, 2015, http://www.theguardian.com/global-development-professionals-network/2015/apr/27/inside-Myanmars-pawn-shop-culture-we-wouldnt-accept-filthy-kitchen-utensils-or-used-underwear, (accessed October 27, 2015).

[105] Very much favored today is the latest design of the US$100 note, complete with the encircling "blue ribbon" colors and dynamic watermarks.

[106] As shall be seen, international remittances are overwhelmingly made through informal mechanisms, but in-country payments are increasingly undertaken by way of private banks.

World Bank, in 2015 such remittances, made by an estimated 250 million migrants across the globe, will have amounted to around US$440 billion to developing countries alone.[107] The sheer volume of remittances, coupled with the fact that they are both relatively stable and often countercyclical, makes them a potentially powerful source of development finance.

Many of the issues relating to remittance payments, however, are clouded by a lack of data and information on the method used to remit funds. The IMF records annual data on official worker remittance payments, but these are limited to payments made through official banking channels. Remittances that flow through private and unofficial channels, and via nonbanking instruments, are not recorded. This is problematic for many countries and circumstances, but it is especially significant for migrants from countries in which trust in banks is mostly absent. As is apparent throughout these pages, this describes the situation in Myanmar precisely.[108]

According to the IMF (2015, 30) official worker remittances to Myanmar totaled around US$1.3 billion in FY2014/15 (just over 2 percent of GDP). Of course, and as noted above, these official flows greatly understate the remittances sent by Myanmar's estimated 2 million or so migrant workers and refugees who live outside its borders, and which are made overwhelmingly (85 percent plus) through informal payment mechanisms.[109] Informal payment mechanisms persist, despite the arrival of Western Union and Moneygram and the links these and similar international monetary transfer firms have established with Myanmar banks. These firms have captured some of the remittance business to and from Myanmar but, as noted in more detail below, mostly they have made life easier for the informal *providers* of remittances services, rather than their customers. Myanmar's banks themselves do little in the way of direct transfers with overseas institutions, despite increasing linkages, especially into the region. In short, the informal finance sector continues to dominate the remittance business in Myanmar.

Informal Remittance Channels and Instruments

Informal movements of money to and from Myanmar take many forms, including the most obvious method of simply carrying cash in and out in person. Above all, however, remittances in Myanmar are done through what is universally known throughout the country as the *hundi* system.

Known variously around the globe as *hawala* (in the Arabic-speaking world), *chiao hui* (China), and *poey kwan* (Thailand), *hundi* is a device in which monetary value is transferred through a network of dealers or brokers from one location to another. The mechanics of their operations are relatively straightforward, as can be seen in the example in the box below.

A number of matters remain unresolved in the above example. First, the *hundi* dealer in Thailand now owes the *hundi* dealer in Myanmar for the remittance payment. How will this be settled? There are a number of ways, depending upon the circumstances. One of the most common, highly applicable in the context of Myanmar, is that the debt between the two *hundi* dealers will be settled in goods. Many *hundi* dealers are, in fact, shop keepers and traders of various kinds, with *hundi* dealing being a side activity. So, in the case above, goods to the value of the remittance debt will ultimately make their way from the *hundi* dealer in Thailand to the Myanmar counterpart. In cases such as Myanmar, with little in the way of domestic production of complex consumer items, the importation of goods presents a ready avenue for *hundi* settlements. But beyond such in-kind settlements are a number of other reconciliation devices. When *hundi* dealers have access to financial institutions, funds can be directly sent through banks or money transfer firms. This is increasingly the case according to pioneering new research (Kubo 2015). The banks' now more efficient distribution channels (established in their own right and through Western Union and the like) have led to a situation in which "informal remittance methods have been evolving along with the development of Myanmar's banking sector" (Kubo 2015, 1). As Kubo further notes, specifically in describing the situation as it involves the remittance channels between Myanmar and Thailand:

> Informal money transfer operators make use of bank branches as the interface with remitters and recipients. Many migrant workers transfer funds from branches and automated teller machines (ATMs) of Thai banks to the accounts of informal operators in Thailand, and some of these operators make payments to the recipients of Myanmar banks. Thus, banks are effectively incorporated into informal remittance channels (Kubo 2015, 1-2).

When banks are not accessible, *hundi* settlement can occur through the exchange of near-monetary commodities such as gold, precious stones, and, sometimes, contraband such as narcotics.

In practice, various complications come into the simple picture painted above, most of which, however, only add to the appeal of the *hundi* system. For instance, to ensure security, the Burmese migrant worker is usually given an authentication code by the *hundi* dealer in the host country. This code is communicated by the *hundi* dealer to an equivalent in Myanmar (usually by phone) and by the Burmese migrant worker to their beneficiary in Myanmar (also usually by phone). This beneficiary must reveal the authentication code to the *hundi* dealer in Myanmar in order to receive the remittance payment. Another complication to the simplified example above is that often the *hundi* commission is not an explicit independent charge, but an implicit fee levied by discounting the exchange rate through which the remittances are calculated. Finally, and as is readily apparent from the above, at the core of the *hundi* system is trust. For the senders and receivers of remittances such trust is won by observation of the system in successful operation and by repeated dealings. Among *hundi* dealers themselves trust is often based on kith and kin relationships.

The remittances sent by Myanmar's estimated 2 million or so migrant workers and refugees who live outside its borders ... are made overwhelmingly (85 percent plus) through informal payment mechanisms.

***Hundi* is a device in which monetary value is transferred through a network of dealers or brokers from one location to another.**

HOW HUNDI WORKS

Person A, a Burmese migrant worker in Thailand, desires to send money home to her family in Myanmar. To do this, she approaches a *hundi* dealer whom she knows and pays them, in baht. The *hundi* dealer now contacts their counterpart (another *hundi* dealer) in Myanmar, who pays Person A's family in *kyat*. The amount received by the family will be the *kyat* equivalent of that paid by Person A in *baht*, less an amount representing the commission charged by the two *hundi* dealers. As far as Person A is concerned, the transaction is now complete. She has sent her money home.

[107] World Bank, "Remittances Growth to Slow Sharply in 2015, as Europe and Russia Stay Weak; Pick Up Expected Next Year," World Bank press release, April 13, 2015, http://www.worldbank.org/en/news/press-release/2015/04/13/remittances-growth-to-slow-sharply-in-2015-as-europe-and-russia-stay-weak-pick-up-expected-next-year.print, (accessed October 27, 2015).

[108] One of the major barriers to the use of formal transfer mechanisms is, not surprisingly, the legal status of the sender. If a migrant worker is without legal status in the host country, using a bank or a formal money transfer firm (where formal identification is usually a requirement) is both difficult and risky. This also precisely describes the typical situation of the migrant from Myanmar.

[109] For more on the background of these, see Turnell, Bradford, and Vicary (2009).

11. MICROFINANCE

Microfinance has a somewhat long and tortured history in Myanmar. For much of the time the sector has existed, in various forms since 1997, at the fringes of legality. Dependent on specific memoranda of understanding and often simply on regulators looking the other way, for the longest time microfinance in Myanmar teetered between achieving genuine success and coming to a sudden halt.

In 2015, microfinance in Myanmar gained new legal foundations, and has achieved growth and outreach. Altogether, around 250 microfinance institutions (MFIs) are now present in the country, serving over 1.2 million clients and with a total loan portfolio of just over US$200 million. The MFIs include a handful of prominent international nongovernmental organizations (NGOs), around 20 local NGOs, nearly 80 financial cooperatives, a dozen or so foreign microfinance companies, and nearly 100 local microfinance companies. Many of the local microfinance companies are former and current money-lender firms.

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Many of Myanmar's MFIs were established during the Thein Sein administration, during which time Myanmar became, and to some extent remains, something of a hotspot for footloose international investors, NGOs and global charities, the multilateral lending institutions, and the development agencies of a number of governments. A great proportion of all of these, in turn, promote microfinance as a sector into which they will allocate funds. For such actors, microfinance ticks all sorts of boxes for their donors and constituencies back home. As such, and in contexts in which Myanmar finds itself now, microfinance is often the "first cab off the assistance rank," that is, the initial, almost-obligatory, donor priority.

The trouble, of course, is that the influx of funds and new players into microfinance, especially into countries that lack supporting infrastructure, can undermine prudence and good practice. The disasters created by excessive flows of donors' funds into microfinance lending is a long list that includes recent crises in Bangladesh, Bosnia, India, Mexico, Nigeria, and Pakistan (Roodman 2012, 275–279).

So far in Myanmar the problem of excessive funding is not yet in evidence. However, a proliferation of MFIs is already a cause of concern. Some of Myanmar's MFIs are effective, efficient, and of a scale and ambition from which much might be expected. Others are moribund institutions established merely to occupy a license in the misguided belief this would give them access to mobile payments business and thus speculative gain. Others, including some 50 financial cooperatives that have been rebranded and are masquerading as MFIs, raise prudential and consumer protection concerns.

In the light of these concerns, the regulator of microfinance in Myanmar, the Financial Regulatory Department (FRD), began in 2015 to issue new MFI licenses of just one-year duration. Table 9 provides data on the largest and most promising of Myanmar's MFIs:

TABLE 9: MICROFINANCE IN MYANMAR: BY THE NUMBERS *

Institution	Number of Depositors	Deposits $US 000s	Number of Borrowers	Loans Outstanding $US 000s
PACT Global Microfinance Fund**	673,828	35,689	623,864	112,152
ACLEDA Myanmar	46,202	308	32,863	8,572
Vision Fund Myanmar	n.a.	n.a.	58,943	8,029
Proximity Finance*	n.a.	n.a.	35,808	5,982
DAWN Microfinance	54,630	497	53,800	4,706

** As of June 30, 2015, except where indicated. ** As of December 31, 2015.*

Source: Microfinance Information Exchange (MIX Market)[110]

As seen in Table 9, microfinance in Myanmar is greatly dominated by the **PACT Global Microfinance Fund**, which is very large even by global standards.[111] It accounts for more than 50 percent of microfinance lending in Myanmar. An institution with a long history in Myanmar, PACT began as a project of the United Nations Development Program (UNDP) in 1997 with a ministerial memorandum of understanding against what was, otherwise, a singular lack of legal authorization for microfinance. After 15 years of living such a precarious existence (during which time, nevertheless, the PACT MFI grew and expanded), in February 2012 it was transformed (and legally established under the new microfinance law—below) into the Pact Global Microfinance Fund (PGMF). Mixing Grameen Bank lending methodologies (at the core of which is the celebrated peer group lending model and the stipulation on lending only to women) with business training of various forms, PGMF is both an MFI and a development NGO. Apart from making loans through the peer groups, PGMF encourages voluntary savings among its clients to the elastic limits of what is allowable. Borrowers also pay into a Beneficiary Welfare Fund (1 percent of the value of their loans, while PGMF contributes a matching amount) to meet contingencies and help borrowers in distress.[112] PGMF reports a repayment rate on its current portfolio of 99.3 percent.

The latest data on PGMF lending are included in Table 9, but since the creation of PACT, its various arrangements claim around 1 million borrowers. PGMF has expansion plans; its ambitions include adding 500,000 new borrowers and increasing its lending portfolio by over US$100 million over the next three years (2016 to 2019).

ACLEDA Myanmar is a subsidiary of the Cambodian Bank of the same name, but its operations come with the backing of the IFC, which holds a 15 percent stake.[113] COFIBRED, a cooperative bank from France that had been a bidder for one of Myanmar's foreign bank licenses, and the German government-owned development bank, KfW, hold another 15 percent each, while ACLEDA Bank (Cambodia) itself owns the remaining 55 percent. The existence of the IFC as a shareholder in ACLEDA has proved valuable for the MFI in raising offshore funds, including the ability to pay a higher interest rate (13 percent) on such funds than those permitted to other foreign MFIs. This ability was granted as a one-off authorization. As can be seen from Table 9, ACLEDA runs a reasonably substantial microfinance business in Myanmar. It currently has around a dozen branches, but is licensed to eventually operate in nearly 80 townships in the Yangon and Bago regions. Just over 34 percent of its loans are made in rural areas, as encouraged by the FRD. ACLEDA has paid-up capital of K8 billion. In FY2014/15 it recorded a profit of nearly US$1 million. In its FY2014/15 annual report, ACLEDA noted that it was examining "the possibility of becoming a full commercial bank."[114]

Vision Fund Myanmar was founded in 1997 by the global charity World Vision.[115] It does not seek to be a financial institution in the narrow sense, but uses its MFI to further the organization's broader humanitarian and development goals.

Proximity Finance is the MFI unit of the Proximity Designs social enterprise in Myanmar.[116] Established in 2004, it offers today a vast array of products and services designed to match the needs of rural dwellers in Myanmar. Proximity made its initial outreach with finance to fund its customers' purchases. Most of its current customers are farmers who cannot access funds from the MADB.

MICROFINANCE LAW

The most important development affecting microfinance in Myanmar under the Thein Sein administration has been its formalization and legalization through the Myanmar *Microfinance Business Law* (MFL) of November 2011.

The MFL authorizes the establishment of microfinance institutions to carry out a liberal array of activities, including to:

- Extend microcredit;
- Accept deposits;
- Receive and accept remittances;
- Carry out insurance business;
- Borrow locally and from abroad; and
- Carry out other financial activities.

[110] Mix Market Microfinance data for Myanmar can be found at http://www.mixmarket.org/mfi/country/Myanmar%20%28Myanmar%29?gclid=CKimzc-coMcCFcGTvQodAZUNJg, (accessed August 11, 2015).

[111] Much of the information is from PGMF's website, http://www.pactworld.org/country/pact-global-microfinance-fund, (accessed November 6, 2015). Background on the MFI's early years in Myanmar can be found in Turnell (2009).

[112] The August 2015 floods in Myanmar imposed severe losses on many of PGMF's borrowers and, accordingly, this fund is currently being heavily drawn upon.

[113] See ACLEDA Myanmar's website, http://www.acledamfi.com.mm/mm/eng/, (accessed November 6, 2015).

[114] ACLEDA MFI Myanmar Co., Ltd., "Annual Report 2014-2015," Bahar Township, Yangon Region, p. 11.

[115] For more on the background on Vision Fund's early history in Myanmar, see Turnell (2009). See Vision Fund's website, http://www.visionfund.org/1966/about/, (accessed November 6, 2015).

[116] See the Proximity Finance website, http://www.proximitydesigns.org/products-services/financial-services, (accessed November 6, 2015).

Minimum capital standards are specified under the MFL, appropriately at differential levels depending on whether an MFI takes in voluntary deposits or not. For deposit-taking MFIs the minimum amount of paid-up capital is set at K30 million (less than US$30,000), and for non-deposit taking MFIs capital must be a minimum of K15 million. Such an initial capital requirement is common throughout the microfinance industry (but the capital minimums in Myanmar are *very* low), as are the different amounts for deposit and non-deposit taking institutions.

Overseeing the evolving regulation and supervision of microfinance in Myanmar is the Financial Regulatory Department (FRD).[117] The FRD was formed out of the Myanmar Microfinance Supervisory Enterprise, itself spun out of the long-standing, state-owned pawnshop in Myanmar, the MSLE.

Over time, the details of the rules and regulations governing microfinance in Myanmar have evolved to include a great many standards that attempt to meet international best practice. Likewise, the FRD has been created to mimic the institutions that in other countries regulate microfinance entities. Yet the FRD struggles to properly implement the laws and regulations it is supposed to implement; it also has very little capacity to understand and incorporate the many new methodologies and technologies being applied elsewhere in the world. This has many implications for the sector, not least the lack of confidence inspired in its supervision of what is now around 200 MFIs of varying qualities and capacities. Another implication, apparent even in the absence of crises, is that many of the activities theoretically allowed under the MFL are not permitted in practice. Notably, these include an interpretation of the FIL that voluntary deposits *cannot* be collected by MFIs, even those with deposit-taking licenses (discussed in more detail below).

In 2014 a series of reforms were made to the regulations governing MFIs. Some of these came at the behest of two international studies into ways of improving financial inclusion in Myanmar—the UN Capital Development Fund's Making Access Possible (MAP) project, mentioned and used throughout this study, and the FIND (Financial Inclusion for National Development) project of the World Bank. Among the measures introduced, which were a mix of greater freedoms *and* new prudential requirements, were:

- Increasing the maximum single loan cap on MFIs from K500,000 to K5 million;
- Allowing MFIs (foreign and domestic) to seek equity financing;
- Allowing local MFIs to borrow from the Myanmar Economic Bank;
- Allowing foreign MFIs to borrow from foreign financial institutions, up to a maximum of $US3 million;
- Allowing MFIs to offer mobile phone-based payment services;

Many of the activities theoretically allowed under the MFL are not permitted in practice. Notably, these include an interpretation of the FIL that voluntary deposits *cannot* be collected by MFIs.

[117] The FRD website is located in the Myanmar Small Loans Enterprise section of the Ministry of Finance website—underlining the point that MFI regulation in Myanmar is yet to be placed within an appropriate framework. See http://www.mof.gov.mm/en/content/myanma-small-loans-enterprise.

- Requiring MFIs to make at least half of their lending in rural areas; and
- Requiring MFIs to meet a liquidity ratio of at least 30 percent, a debt to equity ratio of no more than 5:1, and a solvency ratio of greater than 15 percent (LIFT 2014, 85).

Despite the advocacy of MAP, FIND, funding bodies such as the Livelihoods and Food Security Trust Fund (LIFT), and just about every MFI in Myanmar, the cap on the maximum interest rate MFIs could charge remained at 30 percent per year (2.5 percent a month), while the minimum deposit interest rate to be paid was maintained at 15 percent per year.

Other impediments likewise remained, not least the interpretation of the MFL that MFIs were not to take voluntary deposits (beyond 5 percent of the value of a borrower's loan), or any deposits from nonborrowers. This restriction on deposits, presumably made out of a concern for the safety of depositors' savings against the backdrop of Myanmar's history of financial crises—and the great number of small, poorly managed, and relatively obscure MFIs that had been allowed to spring into existence—is a significant impediment. It restrains not just the ability of MFIs to properly and appropriately fund themselves and achieve financial sustainability, but also the possible contribution of the sector broadly to Myanmar's financial and economic development. As study after study has shown in recent years, MFIs' provision of a safe savings vehicle and a means by which clients' *own* funds can be employed for capital expenditure and consumption-smoothing without recourse to borrowing is likely to be the real contribution they make to broader economic development objectives.[118]

This restriction on deposits ... restrains not just the ability of MFIs to properly and appropriately fund themselves and achieve financial sustainability, but also the possible contribution of the sector broadly to Myanmar's financial and economic development.

Meanwhile, some of the 2014 freedoms listed above have proved in practice to be much less than they seem. For instance, the theoretical ability of local MFIs to borrow from the MEB is rendered irrelevant by the inability of that institution to lend against anything other than the aforementioned, very narrowly defined physical collateral. Foreign MFIs are similarly prevented from borrowing from international banks. Although in theory such borrowings can be undertaken at any interest rate, in practice the CBM does not allow loans upon which a rate of more than 10 percent a year is levied. Given that foreign banks normally require a foreign exchange hedging premium on loans to entities in Myanmar—on top of a margin that takes into account counterparty risk generally—few international commercial lenders would provide funds at anything less than between 13 to 17 percent a year (LIFT 2014, 85).[119]

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In a similar vein, the FRD has, in practice, banned the provision of term deposits and other bank-like products through which MFIs might legitimately fund themselves, even if those products were offered just to borrowers. Such deposit types can also greatly assist MFIs in their ability to properly deal with the liquidity mismatch that naturally arises from financial intermediation.

[118] For more on this understanding, see Roodman (2012).

[119] Among the very few financial firms offering exchange rate hedging in Myanmar, none offer a price below 10 percent of a transaction.

The injunction was almost certainly enacted under pressure from the formal banks—leaning on the regulator at a time when they feared losing market share to rivals who could not only offer a higher interest rate but also, because of the international backing of many of the MFIs, offer an extra dose of perceived safety and security along the way.

Progress in integrating the transformative possibilities of mobile telephony and microfinance has similarly been slow, despite the fact that microfinance is one of the services explicitly allowed under the CBM's *Mobile Banking Directive*.[120]

As noted above, this delay has caused a degree of consternation among a small cohort of MFIs, whose formation seems to have been predicated precisely on using their MFI status as the basis for getting into the mobile payments business. Some legitimate operators seem to have been similarly minded. In August 2015, Thailand's leading mobile phone retailer, Jay Mart, was authorized to establish a joint venture, microfinance operation in Myanmar (JP Finance) that will ostensibly be built around a phone network.[121] Scant details are available at this stage.[122]

[120] Vanderbruggen and Dharamsi (2014, 5).

[121] "JMT to Enter into Micro-Finance in Myanmar," *Mizzima*, August 14, 2014, http://mizzima.com/business-domestic/jmt-enter-micro-finance-myanmar, (accessed August 16, 2015).

[122] Myanmar's MFIs have complained about most of these restrictions. See Joshua Carroll, "Myanmar's Microfinance Leader Says Rules are Too Tight," *Catalyst Asia*, June 1, 2015, https://catalystasia.wordpress.com/2015/05/18/myanmars-microfinance-leader-says-rules-are-too-tight/, (accessed August 11, 2015).

12. THE UNFORTUNATE RETURN OF COOPERATIVE CREDIT

In Myanmar, cooperatives have mostly been a failure, not least because they require levels of trust and social capital that have never existed.

Over half a million borrowers are collectively claimed for the cooperatives, over K20 billion in loans, and around K30 billion in deposits.

Often listed as microfinance providers in Myanmar are the various financial cooperatives that exist in the country. Organized under the Ministry of Cooperatives (itself posing something of a problem in terms of regulatory clarity), there is, and always has been, a very large gap between the rhetoric of what cooperatives do in Myanmar and the practical realities on the ground. The cooperative movement has made enormous strides in many countries around the world, especially in contributing to financial inclusion. In Myanmar, cooperatives have mostly been a failure, not least because they require levels of trust and social capital that have never existed—in the colonial era, the early independence years, or the present. Yet, and notwithstanding this unpromising record, it is claimed that there are around 1,700 such institutions in Myanmar.[123] Nearly 50 of these (belonging to the Central Cooperative Society, more on which below) hold MFI licenses. Over half a million borrowers are collectively claimed for the cooperatives, over K20 billion in loans, and around K30 billion in deposits (OECD 2014, 210). These numbers are unreliable, and many cooperatives are moribund in reality. Nevertheless, the claims themselves illustrate the esteem the cooperative system continues to have for many in authority in Myanmar.

THE CHINA LOAN

Policymaking with respect to banking and financial affairs under the Thein Sein administration has been, for the most part (and with the policy banks and latest foreign exchange license issues aside), mercifully absent of the sometimes eccentric initiatives that were hitherto a feature in Myanmar. In August 2013, however, echoes of the past could be heard when news broke of a large—up to US$900 million—loan negotiated between Myanmar's Ministry of Cooperatives and the Export-Import (Exim) Bank of China. This loan, to be drawn down in tranches, was to be lent on to Myanmar's cooperatives which, in turn, would provide loans to individual borrowers. The Exim Bank loan was to be repaid in 10 years and came with an interest charge of 4.5 percent per year and a management fee of a further 1 percent. Meanwhile for the individual borrowers of the cooperatives the loan terms were very attractive; they were initially

[123] Private communication with an official in the Ministry of Cooperatives.

publicized at 1.5 percent a month (note that MFI loans are charged at 2.5 percent) and were subsequently reduced to 1.1 percent.[124]

The distribution of funds under these arrangements is a vast process, as is, accordingly, the purported expansion of the cooperatives network itself. These are some of the elements:

- According to the Minister of Cooperatives, the number of cooperative societies will increase by 5,000 and, subsidiary to these, borrowing groups consisting of five-person teams, functioning under a cooperative society, within which members would guarantee each other's loans, will be extended to each of Myanmar's 60,000 villages.[125]
- The ministry promises to supply each village borrowing group K100,000 in start-up capital. From this point, savings mobilization and loan repayments, together with further government grants, are meant to aggregate funds sufficient to offer borrowers loans of K100,000, rising in time to K500,000 per household. Against these loans, borrowers will be required to save, to a minimum of K50,000 in the case of the K500,000 loans.[126]
- Under the new system, loans can be used for a number of business purposes, but the expectation is that farmers will use capital to buy equipment such as tractors, tractor trailers, trucks, engines, generators, water pumps, and motorbikes. Urban borrowers are expected to purchase taxis, sewing machines, trishaws, and motorbikes, although the last item is presumably excluded in Yangon, given the ban on motorbike circulation there.[127]
- Meanwhile, as a pilot project for the broader system, cooperative credit is expanded among eight townships of Myanmar's capital, Nay Pyi Taw. This involves the provision of an extra K7 billion in funds, spread among 205 cooperative societies and their roughly 12,500 members. Loans are up to K500,000 (in line with the broader program) and are meant to be used for the purchase of agricultural vehicles and machinery.[128]

[124] Jay Supetran, "The China Loan: Managing and Sustaining Development," *Myanmar Insider*, August 2015, http://www.myanmarinsider.com/the-china-loan-managing-and-sustaining-devel/, (accessed November 4, 2015).

[125] The comments of the deputy minister were made before an international conference on microfinance in Myanmar, held in Nay Pyi Taw on May 9–10, 2013. The proceedings of the conference, "Emerging Microfinance Sector in Myanmar: Regional Lessons on Selected Issues," can be found at: http://www.mm.undp.org/UNDP_Publication_PDF/MFWSreport.pdf, (accessed October 23, 2015). The expansion of Myanmar's cooperative credit system *may* involve the absorption of the large PACT/UNDP microfinance institution noted above. Such an idea has never been far from the thoughts of the Cooperative Ministry (to the consternation of the PACT/UNDP people), but the issue came to the surface in more blunt ways during some of the speeches and announcements related here. Likewise, sometimes mentioned as the wholesale distribution vehicle for funds through the cooperative system is the Myanmar Microfinance Bank (MMFB), discussed above. Details have been elusive. Apex funding vehicles (such as the potential role of the MMFB as a supplier of wholesale funds to retail MFIs) sat atop the cooperative credit system in both the colonial and post-independence eras without much utility.

[126] These proposed loan terms are cited from "President U Thein Sein Calls for Hard Work," *The New Light of Myanmar*, August 20, 2013, pages 1 and 9.

[127] Statement made at the aforementioned international conference on microfinance in Myanmar, held in Nay Pyi Taw on May 9–10, 2013, in conference proceedings.

[128] For more on this pilot plan, see Hsu Hlaing Htun, "First Phase of Ambitious Ministry Lending Program Launched in Nay Pyi Taw," *The Myanmar Times*, August 25, 2013, http://www.mmtimes.com/index.php/national-news/7946-first-phase-of-ambitious-ministry-lending-program-launched-in-nay-pyi-taw.html.

Upper house MP Phone Myint Aung (of the New National Democracy Party) opined that the loan program "won't really change the lives of the farmers."

The actual borrower of the U.S. dollar loan from China is the Myanmar Foreign Trade Bank (MFTB), which then advances the Ministry of Cooperatives an equivalent sum of kyat for lending on to cooperatives.[129] The loan appears to have been taken in U.S. dollars to finance the import of Chinese goods. As such, the whole arrangement is like a vast hire purchase (or rent-to-purchase) plan.[130] The benefits to the Chinese suppliers from this are clear and apparent. Whether the arrangement locks local borrowers into the purchase of items they might not otherwise choose is an open (and worrying) question.[131]

Longer term, and noting the gap between the size of the Chinese loan and the ultimate cost estimates of the expanded program, Deputy Cooperatives Minister Than Tun made clear that the intention of the ministry was to seek "aid, grants, and concessional loans from international organizations."[132] The quest for international funding has also been a theme in a number of the speeches made by Minister of Cooperatives Kyaw Hsan.

In reaction to the Cooperative Ministry's announcements, Phyo Win, a member of parliament (MP) with the National League for Democracy (NLD), said that cooperative enterprises had "always been a failure."[133] Other MPs at the time took a similar line, with Representative Tin Nwe Oo rhetorically asking, "how many times has the cooperative system succeeded in our country?" while also remarking on the high interest rate China was charging for its initiating credit.[135] Upper house MP Phone Myint Aung (of the New National Democracy Party) opined that the loan program "won't really change the lives of the farmers."[135] Minister of Cooperatives Kyaw Hsan acknowledged that "the cooperative system has not succeeded in the past" but added that "we will try to learn from our mistakes."[136]

Upon this issue of the system's ability to cope with expansion, and of the Ministry of Cooperatives and regulators in directing it all, outside observers have also been skeptical, as captured by MAP:

[129] See Khin Oo Tha, "Chinese Bank to Loan $100 Million," *Mizzima News*, August 20, 2013, http://www.mizzima.com/business/economy/9883-chinese-bank-to-loan-100-million.

[130] The August 20 report in the *New Light of Myanmar* supports the idea that this is the arrangement.

[131] It cannot be assumed away that some of the foreign exchange proceeds of the loan may end up in places and pockets not properly intended.

[132] Statement made at the aforementioned international conference on microfinance in Myanmar, held in Nay Pyi Taw on May 9–10, 2013.

[133] U Phyo Win is cited in Win Ko Ko Latt, "MPs Approve Loan Despite Concerns Over Interest," *The Myanmar Times*, August 20, 2013, http://www.mmtimes.com/index.php/national-news/7947-mps-approve-loan-despite-concerns-over-interest.html.

[134] Tin New Oo is cited in Khin Oo Tha, *op. cit.*

[135] Phone Myint Aung is cited in Khin Oo Tha, *op. cit.*

[136] Kyaw Hsan cited in Win Ko Ko Latt, *op. cit.*

> A key issue facing the rapid growth of the cooperatives is the limited use of prudential standards and professional management systems, and, for example, clients are not required to undergo needs and risk assessments prior to disbursals. The supervisor (Ministry of Cooperatives) has limited tools to manage the funds, and the mandatory annual audits may be insufficient as the loan book grows. This is particularly important since, although Myanmar has had experience with cooperatives for a long time, sustainability at this scale is not yet proven and will require a few years of operation. (MAP 2014, 17)

The MPs and others cited here were surely right to be concerned. Put simply, cooperatives *have* always been a failure in Myanmar.[137] Established initially by the British colonial authorities to dilute the dominance of the *Chettiar* moneylenders, as well as to curry favor with the local populace, the first iteration of cooperatives collapsed in the 1920s amid both economic depression and a widespread lack of faith in the system. The revival of the cooperatives after independence, when they were seen as an acceptable device existing somewhere between capitalism and socialism, more or less went the same way, especially with respect to an all-pervasive belief that cooperative loans did not have to be paid back. After the military coup in 1962, cooperatives were once again a chosen vehicle for credit provision. In reality, however, they were little more than elements of the security apparatus and distribution devices for corruption, before disintegrating into irrelevancy. Up until the recent pronouncements, it is perhaps fair to say that the consensus among financial sector stakeholders in Myanmar was that the cooperative credit system as it existed was essentially moribund, an artefact of history unsuited to modern financial practices.

DIFFERENT THIS TIME?

Not least of the serious difficulties presented by the announced expansion of Myanmar's cooperative credit system is that highlighted by the MPs above; such initiatives have been applied many times before, with dismal effect. Are matters different now? It is hard to see how they would be. The program outlined thus far seems designed to repeat past errors, especially in the way it is so completely state-driven and operated. In fact, this latest version actually broadens the state's role. State direction is not only apparent in the construction and funding of the system itself, but also in the provision of the goods for which borrowings are made. As noted above, it would seem that the items against which the loans are made are procured from the Ministry of Cooperatives, direct from Chinese suppliers, and with no local review.

More than a few of the criticisms from MPs and others of the cooperative credit expansion plans center on its funding through the Chinese loan. Such critics point to the relatively high interest rate charges of this debt; its 4.5 percent-per-year levy plus management fee compares especially unfavorably with concessional lending from the World Bank, Japan, and others.[138] Myanmar is hardly in a position to be complacent about external debt and its recurrent costs. And the interest paid to China's Export-Import Bank has to be met by the ultimate borrowers—that is, Myanmar's farmers, small enterprise proprietors, and workers.

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While the overall volume of credit promised under the revitalized cooperative system is large, the loans available to individual borrowers are not. At the projected maximum of K500,000, they are insufficient to be transformative, even for microenterprises.

While the overall volume of credit promised under the revitalized cooperative system is large, the loans available to individual borrowers are not. At the projected maximum of K500,000, they are insufficient to be transformative, even for microenterprises, and are well short of the funds required for the very items held out to attract potential borrowers—the tractors, motorbikes, taxis, and sewing machines evoked by the Minister of Cooperatives.

One interesting future development on the China cooperative loan is the possibility it could be classified as an "odious debt"—a debt taken on "and spent against the interests of the population of a state, without its consent, and with full awareness of the creditor" (Howse 2007, 2). The highly pertinent consequence of debts so designated is that they may not—indeed, should not—be repaid. Yet another issue for Myanmar's future government to ponder.

[137] For details on the long history of financial cooperatives in Myanmar, see Turnell (2009).

[138] The World Bank's 40-year, US$260 million development loan to Myanmar is charged at 0.75% per year.

13. CAPITAL AND FINANCIAL MARKET DEVELOPMENTS

Myanmar's formal financial sector is a bank-based one in the pattern familiar to many transition and developing countries. Myanmar's government has issued treasury bonds and bills since the 1990s, but these instruments are overwhelmingly bought by the central bank (in the manner of "money financing" discussed earlier) and by banks (also as noted previously, and increasingly now the MEB). A formal, private-sector bond market does not exist in Myanmar. Similarly, markets to hedge risk through financial derivatives and similar instruments are as yet unknown. Progress has been made in recent years in developing financial markets in Myanmar, though the pace has been slow. This section explores some of the issues, focusing first upon the government bond and bill markets, and then the proposal for a Yangon Stock Exchange.

Basing the bond market upon administratively fixed yields is not a sustainable option over time ... in what would amount to a relatively simple reform that could advance sound public finances, the current bond system could be replaced by one in which bonds are sold at auction.

TREASURY BOND MARKET

International practice, as well as economic and public finance orthodoxy, tells us that by far the best mechanism, beyond current revenues, for financing government expenditure is selling treasury bonds. Myanmar currently sells such bonds at fixed yields determined by the government (in the growing magnitudes revealed in Table 2 and Table 3). At the moment, these yields exceed the minimum interest rates banks must pay on deposits. As a result, the bonds find customers among the banks themselves, and to a very limited extent among domestic private investors. However, basing the bond market upon administratively fixed yields is not a sustainable option over time. Myanmar's volatile inflation, uncertainties with respect to the banking sector, and other broader doubts mean that administratively set yields will not always, or even mostly, deliver bond buyers. Instead, in what would amount to a relatively simple reform that could advance sound public finances, the current bond system could be replaced by one in which bonds are sold at auction, the standard method of selling bonds more or less everywhere. The market-determined rates for Myanmar's debt thus generated would aid not just in its sale. The rates would also form reference rates upon which a newly-freed financial sector broadly could price the provision of finance.

The decision in April 2013 to allow secondary market trading in Myanmar government bonds was a positive, though insufficient, move in aid of the above. Likewise welcome was the establishment in September 2014 of a Treasury Department under the Ministry of Finance

which could, if and when the *Public Debt Management Law* is finally passed, create part of the necessary infrastructure for prudent public spending and financing.

TREASURY BILLS

In addition to its bond issues, Myanmar's Ministry of Finance sells short-term (mostly three-month maturity) treasury bills to fund the mismatch between government expenditures and receipts. Traditionally these bills, which were sold at an unattractive and low fixed yield in order to reduce the cost of such financing, were simply sold to the CBM. In that way they constituted a significant component of the financing of Myanmar's budget deficits noted throughout this study. In March 2015, however, an important, if as yet incomplete, reform was set in motion when the government announced its first auction for K50 billion of treasury bills. Conducted by the CBM through a tender system, the first auction attracted five bidders, all licensed financial institutions, and just over half of the bills on offer were taken up. Somewhat unfairly, the CBM came under criticism for the shortfall at the time, but the result of this *first* auction was not, in context, a bad outcome. More warranted has been criticism since (see IMF 2015, 5) that the Ministry of Finance continues to put an upper limit on the yields the bill auctions deliver, and, as a consequence, bill sales still do not meet their targets.

Why the resistance to market-determined yields? One answer is the old hostility within senior leadership to anything smacking of a loss of control. Another is that higher yields will impose greater fiscal financing costs. As noted above, the role of the MEB engaging in the bill auctions, bidding below market-clearing yields and yet receiving substantial allocations, only exacerbates matters.

The bill auctions take place every two weeks. The volumes put to tender vary significantly, however, with very large amounts issued for sale toward the end of the financial year to plug urgent funding shortfalls. The IMF recommends spreading out the sales to avoid the selling pressures and subsequent default take-up by the CBM (2015, 8).

Foreign banks are, at present, precluded from participating in the auctions. As with the other impediments above, the effect of this is to constrain a potentially important source of deficit financing.

A SOVEREIGN RATING FOR MYANMAR?

One of the final initiatives of the Thein Sein administration with respect to Myanmar's capital markets was its commissioning of the Standard Chartered Bank of the United Kingdom (universally known for its role in emerging markets) and Citigroup of the United States as sovereign credit ratings advisors.[139] The appointment, made with some fanfare in August 2015, was accompanied by warnings that Myanmar was not yet seeking a sovereign rating and international bond sales were not immediately in the cards. Rather, the two banks were to act as a bridge between the Myanmar government and the ratings agencies as preparation for a possible future rating, as well as to improve data collection and investor outreach.[140]

In March 2015, however, an important, if as yet incomplete, reform was set in motion when the government announced its first auction for K50 billion of treasury bills.

Establishing a sovereign risk rating is one of the necessary foundations for the development of capital markets in Myanmar.

The draft law ... assigns the financing of government debt to the Ministry of Finance, but directs that body to be transparent on the magnitude and types of debt taken on, as well as the scale and method of funding.

The move toward seeking a sovereign rating was applauded by more or less all sides of the political and other debates in Myanmar. Such ratings, as imperfect as they certainly can be, are nevertheless important in allowing the pricing of government bonds and, with these then established as a benchmark, a whole superstructure of private debt instruments priced according to varying degrees of risk. In short, establishing a sovereign risk rating is one of the necessary foundations for the development of capital markets in Myanmar—a modest, but positive step.

Some other reforms discussed during the Thein Sein administration but left incomplete at its conclusion included the aforementioned *Public Debt Management Law* that seeks to establish a new set of rules with respect to government debt instruments.[141] In particular, the draft law (which was to replace the colonial-era *Government Securities Act* of 1920) assigns the financing of government debt to the Ministry of Finance, but directs that body to be transparent on the magnitude and types of debt taken on, as well as the scale and method of funding these through the sale of government securities. The draft law also spells out the debt-raising capabilities of state and regional governments, as well as state economic enterprises. The former can borrow, but must have such borrowing approved by the Union government which, in turn, must record and integrate this debt in the Union budget as a whole. State economic enterprises remain restricted to borrowing only from the state-owned banks.

Throughout the Thein Sein administration, assistance in the development of Myanmar's capital markets was on tap from a number of sources. Support for the creation of the stock market is outlined below, but for the creation of a bond market, assistance has come from the Japan-ASEAN Fund for Technical Assistance and the ASEAN Bond Market Initiative.[142]

DEVELOPING A STOCK EXCHANGE

For over a decade, Japan's Daiwa Securities has been involved in a 50-50 joint venture with the MEB

[139] Kyaw Hsu Mon, "Standard Chartered, Citi to Advise on Credit Rating," *The Irrawaddy*, August 12, 2015, http://www.irrawaddy.org/business/91213.html, (accessed August 14, 2015).

[140] Standard Chartered Bank, "Myanmar Appoints Citi and Standard Chartered as Sovereign Credit Ratings Advisors," Standard Chartered Bank press release, August 12, 2015, https://www.sc.com/en/news-and-media/news/asia/2015-08-12-Myanmar-appoints-Citi-and-Standard-Chartered-as-Sovereign-Credit-Ratings-Advisors.html, (accessed September 14, 2015).

[141] Aye Thidar Kyaw, "Public Debt to be Handled Differently," August 12, 2015, http://www.mmtimes.com/index.php/business/15933-public-debt-to-be-handled-differently-if-draft-management-law-goes-ahead.html, (accessed October 30, 2015).

[142] "Activities on the Development of Capital Markets in Myanmar," website of the Central Bank of Myanmar, http://www.cbm.gov.mm/content/activities-development-capital-market-myanmar, (accessed September 16, 2015). An outline of JAFTA's program on Myanmar's bond market can be found in a brief memorandum, "Technical Assistance on Developing Bond Markets," on the ASEAN website, http://www.asean.org/archive/jobs/TORDBM1-My.pdf, (accessed September 16, 2015).

establishing the Myanmar Securities Exchange Center (MSEC) in Yangon.[143] The basis of what was *supposed* to be a fully functioning stock exchange, the MSEC was never more than a very small-scale affair that listed and traded just two stocks (Myanmar Citizens Bank and the Forest Products Joint Venture Corporation). Trading was paper-based and extraordinarily thin (it was often said that there were buyers, but no sellers of the listed stocks) and illiquid. Had events gone to plan, the initial over-the-counter trading on the MSEC would have graduated to a full bourse with the MEB running settlement functions and all backed by new securities laws and regulations. A number of half-hearted initiatives to these ends were launched in the early 2000s, not least prompted by the CBM, but Myanmar's political environment precluded anything material.

In 2012, however, momentum for finally realizing the establishment of a fully functioning stock exchange in Myanmar accelerated materially. In April 2012 it was announced that the operators of the Tokyo Stock Exchange had now joined the MEB-Daiwa partnership collectively in the Yangon Stock Exchange (YSX) Joint-Venture Company Limited, with the objective of having a fully computerized trading platform (a scaled-down version of Tokyo's own) up and running by 2015. The joint venture has paid-up capital of K32 billion (authorized capital of K100 billion) and is owned by MEB (51 percent), Daiwa Institute of Research (30.25 percent), and the Japan Exchange Group (18.75 percent).[144] Interestingly, given the ownership structure of the YSX as well as the presumed role to be played by the MEB in the MSEC, the bank chosen to create the settlement systems for the YSX was Kanbawza Bank (out of five bidders for the role).[145]

Projecting that between 180 to 300 firms would be listed and trading by 2020, Daiwa also began approaching prospective Burmese companies likely to list. The construction of the computerized trading backbone of the stock exchange has been funded by Japan's International Cooperation Agency.[146] In September 2014 it was announced that the first three stocks to be traded on the YSX would be the Asia Green Development Bank, the prominent investment holding company First Myanmar Investment (FMI, of which Yoma Bank is a subsidiary), and

[143] Myanmar had a stock exchange that survived from the late 1920s to the early 1960s (at which time it was abolished, along with much other private enterprise as noted in these pages). The Rangoon Stock Exchange traded, at its peak in the early 1930s, in the stocks of 51 companies, mostly mining and oil and rubber enterprises. Seven members (brokers) belonged to and ran the exchange, upon which they also speculated on their own account. It was a rather clubby affair, and to become a member, a broker had to be proposed by at least two existing members and be elected by all the others. The exchange met to trade once in the day, in early afternoon. U Tun Wai (1962) writes that, in addition to the formal brokers, "were about twenty or thirty street or pavement brokers located mainly on Mogul Street."

[144] Thomas Rhoden, "Yangon's Stock Exchange in Comparative Analysis," paper presented to the 2015 *Conference of Myanmar/Myanmar Studies*, Chiang Mai University, Thailand, July 25, 2015.

[145] Kyaw Phone Kyaw, "KBZ Chosen as Settlement Bank for Upcoming Stock Exchange," *Myanmar Times*, May 5, 2015, http://www.mmtimes.com/index.php/business/14290-kbz-chosen-as-settlement-bank-for-upcoming-stock-exchange.html, (accessed September 14, 2015).

[146] Antoni Slodkowski, "Daiwa Looks to Lead $380 Million Investments in Myanmar," July 23, 2012, *Reuters*, http://www.reuters.com/article/2012/07/23/us-Myanmar-japan-investment-idUSBRE86M07B20120723.

In July 2013, a new *Securities Exchange Law* (SEL) was enacted by Myanmar's parliament to establish the necessary legal infrastructure for a stock exchange.

the Myanmar Agribusiness Public Corporation (MAPCO, a creation of the Myanmar Rice Federation).[147] As it turned out, at the official opening of the YSX on December 9, 2015, six companies were approved to list. Asia Green Development Bank was not one of them, but joining FMI and MAPCO were First Private Bank Limited, Great Hor Kham Public (a construction-engineering-infrastructure firm), Myanmar Citizens Bank, and Myanmar-Thilawa SEZ Holdings (the company managing the Thilawa SEZ).

The official opening of the YSX, something of a marquee moment for Myanmar's financial world and its inhabitants, was, nevertheless, an odd affair. Not the least reason for this was an announcement made at the opening that no actual trading of stock would take place yet for some months. This caught the attention of the international press especially, but it did allow a particularly apt quote from Chairman of the Securities and Exchange Commission Myanmar Dr. Maung Maung Thein (who was also deputy finance minister) that "we waited a long time for the stock exchange market to appear, it doesn't matter that we need to wait one or two more months to sell shares."[148]

In July 2013, a new *Securities Exchange Law* (SEL) was enacted by Myanmar's parliament to establish the necessary legal infrastructure for a stock exchange. Drafted with the assistance of Japan's Policy Research Institute, the SEL established the Myanmar Securities and Exchange Commission to regulate securities markets, set out the procedures for obtaining a securities trading license, and outlined the legal framework for the YSX.[149] Updating Myanmar's company law remains a significant pending item (along with what reporting requirements will emerge). A hangover from the old *Company Law* in Myanmar, which dates back to 1914, and a major disincentive for international investors in equities in Myanmar, is the current policy establishing that the presence of even a single foreign investor in a Burmese company renders it to be classified as a foreign entity—and accordingly subject to a number of restrictions, not least in the use and ownership of land.[150]

Listing Rules

On August 14, 2015, the YSX announced the criteria companies would have to meet to list on the exchange.[151] These included a range

[147] "Yangon Stock Market Launch in 2015," *Bangkok Post*, September 30, 2014, http://www.bangkokpost.com/business/finance/435138/new-myanmar-stock-exchange-to-list-three-firms.

[148] Zin Thu Tun, "YSX Rings Opening Bell, but Trading Will Not Start for Months," *Myanmar Business Today*, December 14, 2015, http://www.mmbiztoday.com/articles/ysx-rings-opening-bell-trading-will-not-start-months, (accessed December 30, 2015).

[149] Than Htike Oo, "Japan to Help Myanmar Create a Securities and Exchange Law," *Mizzima*, August 14, 2012, http://www.mizzima.com/business/7751-japan-to-help-Myanmar-create-a-securities-and-exchange-law.html, (accessed September 17, 2014).

[150] This highly restrictive effect was supposed to be remedied by the promulgation of a new company law for Myanmar in 2015. As it turned out, however, the parliament did not pass this legislation before it completed its final sitting in August 2015. Accordingly, this obstacle remains in place. For more on the new *Company Law*, see Alexander Bohusch, "Update of the Myanmar Companies Law," *Myanmar News*, Luther Law Firm Limited, June 2015, http://www.luther-lawfirm.com/fileadmin/user_upload/PDF/Newsletter/Myanmar/NL_Myanmar_07-2015-Updated_Draft_of_the_Myanmar_Companies_Law.pdf, (accessed September 14, 2015).

[151] The criteria were published the same day in the government's newspaper, "Announcement of YSX's Listing Criteria," *The Global New Light of Myanmar*, August 14, 2015, p.12, http://www.moi.gov.mm/npe/nlm/?q=download/file/fid/2036, (accessed August 16, 2015).

of measures that seek to ensure market integrity, as well as consumer protection:

- Listing companies must have at least 100 shareholders;
- The paid-up capital of listing companies must be a minimum of K500 million at the date of application;
- Listing companies must have been trading profitably for at least two years before the date of application to the YSX; and
- Listing companies must establish systems to prevent insider trading.

Naturally, on top of these provisions, came other widely used listing requirements—"fit and proper persons" tests for listed company directors, disclosure and reporting requirements to the exchange, various proper accounting practices, compliance and taxation arrangements, and so on. The listing requirements have not escaped criticism, and, in the immediate aftermath of their proclamation, a skeptical dialog took place in the pages of the privately owned *Myanmar Times*.[152] In this forum, a number of concerns were raised, most centering upon possible market manipulation by listing firms making available only minority stakes to the public and keeping control in the hands of their otherwise private owners. Other issues included a lack of detail with respect to disclosure requirements (nothing specifically on the timing of reports and statements within a year, for instance), and with respect to the voting rights of public shareholders at annual general meetings.

Broking and Underwriting Licenses

Meanwhile, a notification from the Securities Business Supervisory Commission of the Ministry of Finance set out a series of different licenses for securities companies to provide services to the YSX. In particular, minimum paid-up capital requirements are set to gain a license in:

- Securities underwriting K15 billion,
- Securities dealing K10 billion,
- Securities broking K7 billion, and
- Securities investment advice K 0.03 billion.

Other, nonfinancial requirements on securities companies are more demanding, especially in the context of Myanmar where engagement in formal financial markets is not something most citizens could have experienced within its borders in recent years. These include requirements that directors of securities businesses have at least one year of experience in the industry; and that every securities business must have an expert with at least three years of experience in the sector, the latter surely opening the door almost exclusively to foreigners or expatriates.

In early October 2015 it was announced that conditional underwriting licenses had been offered to 10 bidders. This highest form of license to operate on the exchange allows the winning firms to engage in dealing, brokering, and consulting services. More broadly, such firms are expected to be market makers in seeking potential firms for listing. In selecting the underwriters, the role of the Japanese (both the Tokyo Stock Exchange staff as well as those from Daiwa) was critical in conducting compliance and capacity checks.[153] The inclusion of Daiwa in this is noteworthy, especially given that a subsidiary of the firm (Daiwa Securities Group) was one of the entities offered a license. Other license winners included Aya Bank and United Amara Bank.[154]

International Comparisons

Nascent stock exchanges have emerged in a number of transition economies in recent times. For Myanmar, the most relevant of these—for what to do and what not to do—are the stock exchanges in Viet Nam (two, one each in Hanoi and Ho Chi Minh City), Cambodia, and Laos. After a troubled early history, the exchanges in Viet Nam could be regarded as something of a model for what the YSX could become, while the exchanges in Cambodia and Laos provide a cautionary tale of what should be avoided. The two Vietnamese exchanges collectively listed, as of September 2015, around 600 companies with a market capitalization of over US$60 billion. The Lao exchange lists four companies (market capitalization of around US$1.3 billion), while the Cambodian exchange lists two companies (US$0.2 billion).[155] One of the successful innovations of the Vietnamese markets (surely replicable in Myanmar) was allowing foreign investors to buy stocks—gaining both a more stable investor cohort and tapping another source of capital in the process.

The specific fears regarding the performance and even worth of the YSX are echoes of a very broad and still unsettled debate among economists as to the efficacy of financial markets in countries without traditions of trading in secure property rights. Far better, argues the nay side of this debate, for countries such as Myanmar to trust in banks—institutions better able to deal with contingent information and close borrower monitoring. This is a long argument without proximate hope of resolution. In the meantime, the readers of the *Myanmar Times* can console themselves that their concerns mirror (consciously or unconsciously) the concerns over stock markets of probably the greatest modern thinker on economics:

> As the organization of investment markets improves, the risk of the predominance of speculation does … increase … Speculators may do no harm as a bubble on a steady stream of enterprise … a serious situation can develop … when enterprise becomes the bubble on a whirlpool of speculation. When the capital development of a country becomes a byproduct of the activities of a casino, the job is likely to be ill-done (Keynes 1936, 158–159).

[152] Clare Hammond, "Yangon Stock Exchange Listing Criteria Lacking Protection for Investors," *Myanmar Times*, August 17, 2015, http://www.mmtimes.com/index.php/business/16018-yangon-stock-exchange-listing-criteria-lacking-protection-for-investors.html#.VdGzy-UBbGY.mailto, (accessed August 18, 2015).

[153] Clare Hammond, "YSX Provisional Licenses Awarded," *Myanmar Times*, October 9, 2015, http://www.mmtimes.com/index.php/business/16911-ysx-provisional-licences-awarded.html, (accessed October 20, 2015).

[154] Ibid.

[155] Data from Investment Frontier, http://www.investmentfrontier.com/, (accessed September 14, 2015).

14. INSURANCE

Any understanding of Myanmar's financial sector must recognize its repression for most of the past 50 years. Certainly this theme has emerged many times in this study—whether looking at banking, monetary policy and prudential regulation, or rural finance. And yet, perhaps no component of Myanmar's financial sector has been so restricted as insurance.

Perhaps no component of Myanmar's financial sector has been so restricted as insurance.

Insurance was a vibrant if somewhat small corner of Myanmar's financial world in the colonial era. Independence brought about the entry of the state into the insurance sector through the nationalization of the Myanmar National Insurance Company, a local entity, in 1952. In 1959, this was followed by the establishment of the Union Insurance Board, which created a state monopoly in life insurance. In 1964, all private insurance companies were nationalized and ultimately rolled into the Insurance Division of the monolithic state bank monopoly—the aforementioned Peoples' Bank of the Union of Myanmar (PBUB).[156] This state of affairs lasted until the breakup of the PBUB in 1975, when insurance services were shifted to Myanmar Insurance, a new state monopoly authorized under the *Union Bank Law* of the same year. The 1993 *Myanmar Insurance Law* updated legislation on insurance products and services, while maintaining the state monopoly, and the 1996 *Insurance Business Law* created both an insurance sector regulator (the Insurance Business Supervisory Board [IBSB] to sit under the Ministry of Finance), and the legal *possibility* for private insurance companies.

The creation of private insurance companies proved to be a long and drawn-out process, with more than a few false dawns. Finally, in 2012 and as part of the broader financial sector liberalization measures elsewhere examined here, the IBSB called for bids for licenses to conduct insurance business in Myanmar. In order to receive a license, bidders had to commit to various criteria, including minimum capital requirements—K6 billion for life insurance-only firms, K40 billion for general insurers, and K46 billion to be able to do both. Of this capital, 10 percent had to be placed on deposit with the MEB to meet immediate payouts, 30 percent had to be deployed in the purchase of government bonds, and the remaining 60 percent (initially deposits in the MEB) could be withdrawn one year after licensing.

The requirement that Myanmar's insurance companies all charge the same premiums is counterproductive in a sector that currently reaches little more than 2 percent of the population.

Minimum capital requirements are, of course, appropriate and standard across the global insurance industry. As with Myanmar's banking sector, however, other decidedly unhelpful regulations greatly inhibit the sector, not least the requirement that Myanmar's insurance companies all charge the *same premiums* in

[156] For more on the PBUB, see Turnell (2009, 231–232).

order to avoid what the regulators consider to be "harmful competition." Together with the prohibition on foreign insurers (more below), this policy is surely counterproductive in stimulating outreach in a sector that currently reaches little more than 2 percent of Myanmar's population. Equally problematic is a requirement that all insurance companies in Myanmar (the state-owned Myanmar Insurance as well as the new private entities) are required to use government bonds to match any liabilities that exceed capital. This may be handy in financing government deficits, but it deprives the private credit market in Myanmar of a substantial capital resource.

In the end, the IBSB received 20 applications for insurance licenses, from which a dozen firms were chosen. These firms, and their owners, were:

- Aung Myint Moh Min Insurance (Myanmar Economic Corp.);
- Aung Thitsa Oo Insurance (Myanmar Economic Holdings Limited);
- Ayeyar Myanmar Insurance (Max Myanmar Group);
- Capital Life Insurance (Capital Diamond Star Group);
- Citizen Business (CB) Insurance (Citizen Business);
- Excellent Fortune Insurance (Excellent Fortune Development Group);
- First National Insurance (Htoo Group);
- Global World Insurance Group (Asia World Co.);
- Grand Guardian Insurance (Shwetaung Development Co.);
- IKBZ Insurance (KBZ Group);
- Pillar of Truth Insurance (Parami Energy Group);
- Young Insurance Global (Young Investment Group).

Among the firms above, half—IKBZ (Kanbawza), Citizens Business (CB), First National (Asia Green Development Bank), Ayeyar Myanmar (Aya Bank), Aung Thitsa Oo (Myawaddy), and Aung Myint Moh Min (Innwa)—are associated with conglomerates that also hold banking licenses. Some of the firms' owners are on U.S. sanctions lists (First National, Global World Insurance, Aung Thitsa Oo, Aung Myint Moh Min, and Ayeyar).

FOREIGN INSURANCE AND AN OPPORTUNITY LOST

Myanmar's current policy of excluding foreign insurance companies, more or less nakedly designed to protect the nascent (but overwhelmingly crony-connected) local firms, represents an opportunity lost, arguably even more so than the restrictions imposed on foreign banks.

Myanmar's current policy of excluding foreign insurance companies ... represents an opportunity lost.

The magnitude of such lost opportunities by the banning of foreign firms is little understood in Myanmar, certainly by the government, but also more broadly among the country's business commentators. To most in these cohorts, insurance is necessary to help individuals protect themselves against some of the vicissitudes of life. Without available insurance services (few Myanmar people hold insurance of any kind), other financial instruments—primarily savings and debt—must be used to self-insure in order to manage risk.

Less understood, however, is the role of insurance firms around the world as instruments in capital accumulation. Unlike the liabilities of banks and most other financial institutions, the liabilities of insurance companies are long-term. Accordingly, their assets to match them must also be long-term. This presents an ideal scenario for a country such as Myanmar whose needs for long-term funding of physical infrastructure is critical. Bonds issued for infrastructure financing are the foundational investment class of the global insurance business. It would seem a pity if the funds and experience of foreign insurance companies were not exploited by a country needing both capital and improved infrastructure.

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As with foreign banks, foreign insurance companies bring with them methods and practices—informed both by competitive efficiencies *and* home country regulators—that can be emulated in Myanmar. This is technology and best practice transfer at little to no cost.

15. RECOMMENDATIONS

This review of Myanmar's financial sector points to the need for reforms that, if implemented, will create the financial institutions and instruments the country needs for economic growth. Items listed in italics refer to practical measures that can be immediately applied under existing arrangements and under existing laws. Here are proposed reforms, laid out in the order of discussion in this study:

CENTRAL BANKING

- Deliver genuine the CBM independence by properly funding Myanmar's budget deficits by the sale, through competitive tender, of treasury bonds and bills. Among other things, this will require the removal of current caps on the yields of such tenders.
- Create a fully functioning interbank market for liquidity. At present there is little interbank activity in Myanmar. This will require making access to the CBM's discount window more expensive than is currently the case.
- *Widen the bands of the administratively determined deposit and lending rates, with a view to removing them completely in the short to medium term. Following this, and with the creation of (marketable) treasury instruments and with interbank liquidity in place, market-based monetary policy becomes possible.*
- Commit to a plausible and viable monetary policy target. For the short term this should simply be reserve-money targeting, a simple measure largely controllable by Myanmar's monetary authorities. Longer term, and with all the reforms above, more sophisticated metrics could be targeted with a view to achieving the ultimate goal of price and monetary stability.
- Appoint a credible and experienced person to the position of governor of the CBM. This simple, early step could be undertaken by the new government.
- Modernize and computerize internal systems within the CBM.

EXCHANGE RATE

- Move closer for now to a true managed float, with the CBM intervention only taking place in disorderly market conditions, since it is unlikely that Myanmar will possess foreign reserves sufficient to support and defend any form of fixed, or quasi-fixed, exchange rate in the foreseeable future. Opportunities for buying foreign exchange by the CBM during periods of (often seasonal) upswings in the market value of the kyat should be exploited to build a larger foreign exchange buffer.
- Allow basic instruments, such as swaps and forwards agreements, for all real-sector foreign exchange transactions. At present, these cannot be offered by Myanmar's banks.

BANK SUPERVISION

- Expedite the promulgation of the new *Financial Institutions Law of Myanmar*. Initially use this as the legal basis for the implementation of simple prudential rules, approximating Basel I, and

incorporating straightforward leverage, liquidity ratios, and the like.

- Start a rolling audit of all private banks, beginning with the largest, with a view to ascertaining their true state of health. Possibly conduct rudimentary stress tests.
- Review the *Mobile Banking Directive* with a view to expanding the range of activities that telecommunications firms can undertake.
- Extend banking hours. Current arrangements restrict hours to 9:30 a.m.–3:00 p.m., Monday to Friday. These are inconvenient to many enterprises in Myanmar and are an unnecessary obstacle to business.
- Issue a new CBM directive on collateral replacing the current array of directives and instructions that cause confusion and reinforce the view that land is the only acceptable collateral.

REFORMING STATE-OWNED BANKS

- Rectify a significant oversight of the new FIL, which does not include state-owned banks under its regulatory umbrella. In the interests of prudence and competitive neutrality, this needs to be addressed.
- Review the findings of the multilateral agencies' comprehensive diagnostic studies of the state-owned banks. From this information, consider closing the Myanmar Foreign Trade Bank or merging it, possibly with the Myanmar Investment and Commercial Bank. The resulting entity should be put on a strict commercial footing, an equity stake sold to a foreign buyer (in the manner of the strategy employed in Vietnam) and, ultimately, privatized.
- Consider, as some international agencies recommend, preserving the MEB as a safe savings vehicle in the medium term, against a broader financial context that is both likely to remain highly volatile, and yet is one in which savings mobilization is critical. The bank's current condition is difficult to judge without a review of the multilateral agencies' diagnostic studies mentioned above.
- Review the new policy banks with a view either to closing them or merging them with other banks, including private ones, where applicable.

FOREIGN BANKS

- Allow foreign banks to make kyat loans to Myanmar enterprises and provide a full range of other financial services as befits their business operations in the country.
- Let foreign banks buy Myanmar government bonds, both for their own sake (as institutions that will have increasingly longer-term kyat liabilities), and as the sources of needed longer-term capital for Myanmar.
- Permit a multilateral interbank currency swap market to enable foreign banks to lend in kyat and participate in treasury bill and bond auctions.

THE NEW FINANCIAL INSTITUTIONS LAW

The new FIL is itself a source of change. A number of elements within the FIL could be immediately implemented (even without the application of the entire program) to the good of the financial sector, and beyond:

- *Implement public reporting requirements on licensed banks, according to section 75d, and in particular require publication of annual audited financial statements).*
- *Implement and strictly enforce section 53, limiting the amount of lending by banks to related parties. A similar injunction was contained in the Financial Institutions of Myanmar Law (1990) but poorly enforced.*
- *Authorize, as provided under section 140, the rollout of true "mobile financial service providers," exemplified internationally by the M-PESA system and as proposed by Telenor/Yoma for Myanmar. Draft regulations for implementing this aspect of the FIL are already written and await the signature of the governor of the CBM.*

RURAL FINANCE

- Remove, quickly, restrictions on the lending by private banks to the rural sector.
- Restructure the MADB into a genuine rural bank. This action should be a priority. Diagnostics of the bank's structure, governance, operations, and performance are largely complete, and relevant international models for effective rural banks exist on which a reform package can be based.
- Reform land titling and enhance land tenure security. This has direct relevance to the financial sector because of the importance of land as collateral, especially for rural lending. In recent years attention has been drawn to Myanmar's increasingly opaque and dysfunctional land titling arrangements. As with many of the issues raised here, diagnostic studies and preliminary policy remedies have already been conducted and formulated. A new government in Myanmar should commence some of the changes recommended on this front, as circumstances allow and in ways that offer both justice (compensation for past seizures when land itself cannot be returned) and security of tenure for current, legitimate occupants.
- Encourage warehouse financing and similar innovative arrangements, and adjust collateral requirements to support them.

MICROFINANCE

- *Remove or (at least) expand the margins of allowable interest rates that MFIs must pay and can charge. Given the political sensitivities of increasing lending rates, liberalization on the deposit rate side (removing the deposit-rate floor) might be the best place to start.*
- Allow voluntary deposits from members of MFIs, whether or not those borrowers are members, if those MFIs can pass certain prudential tests. There are ample international examples of safeguards that can be employed that allow for the safe aggregation of substantial deposits by MFIs.
- Raise the minimum regulatory capital for MFIs. Capital of K15 million (non-deposit-taking MFIs) and K30 million (deposit-taking) is too low to allow for any capital cushion on losses, and opens up the sector to non-serious players.
- Audit existing licensed MFIs to determine which institutions should not be in the business.

- Permit MFIs to collaborate with telcos to offer mobile money products and services. This is allowed by the *Microfinance Business Law*, but not yet in practice.
- *Allow domestic MFIs to (effectively) borrow from the MEB by releasing the latter's collateral requirements to the microfinance sector.*
- *Allow foreign MFIs to pay more than the implicit 10 percent interest cap on loans from foreign banks and other lenders.*
- *Encourage foreign banks to lend to foreign MFIs, an allowable activity under the rules governing foreign banks, and replicate proven methodologies (not least in Myanmar itself historically) for the distribution of wholesale finance.*
- *Allow MFIs to levy fees on services beyond loans.*

COOPERATIVE CREDIT

- Undertake a diagnosis of this sector and publish the results so that it is possible to understand the true state of this sector. The need for this diagnosis is urgent. Information on Myanmar's cooperative credit societies is opaque when available at all.
- *Declare, in the interim, a moratorium on drawdowns from the China Export-Import Bank loan.*

BOND AND BILL MARKETS

- Ensure, as mentioned before, that both types of instruments are sold through open tender.
- Allow foreign banks to participate as buyers in Myanmar bond and bill markets.

STOCK EXCHANGE

- Move gradually in developing the Yangon Stock Exchange (YSX). As the examples of Cambodia and Laos attest, stock exchanges can quickly become locations of fevered speculation, insider trading, and barely veiled gambling. Myanmar needs to take care to avoid such a scenario emerging out of the YSX. Accordingly, in developing the exchange, the regulatory authorities and YSX management are urged to "hasten slowly." Initially, this might suggest a modest listing of stocks in companies beyond reproach.
- Shut down quickly any early hint of insider trading or other fraud.

INSURANCE

- *Remove restrictions that bar domestic insurance companies from competing on premiums. Under current arrangements, consumer utility from insurance is compromised, and existing firms are under little pressure to innovate or achieve operational efficiency.*
- *Remove the ban on foreign insurance companies as soon as practicable. As this study has argued, the benefits to Myanmar from the foreign investment and technical expertise for long-term capital funding would swamp what are, in any case, extraordinarily minor risks.*
- *Free insurance companies (domestic and foreign) to invest in securities that match their investment profiles and strategies. In short, they should not be restricted (as they are at present) to just the purchase of government bonds; they should be able to buy and hold their corporate equivalent. This in itself would do much to stimulate the necessary growth of the corporate bond market in Myanmar.*

16. CONCLUSION

The development of Myanmar's financial sector will be an important and necessary component of the country's hoped-for trajectory along a broader path of transformational growth. For the longest time a source mostly of instability and underperformance, under the Thein Sein administration the first shoots of financial sector revival have emerged. Driven by reforms, albeit incomplete, to Myanmar's exchange rate arrangements, banking regulations, and microfinance laws—and even more so by technological and methodological initiatives launched by private financiers in a more liberal economic environment—the country's financial sector has exhibited strong, if uneven and unstable, growth. Nevertheless, the sector does not yet provide the financial intermediation, nor the financial access, Myanmar needs to join the development story of its peers and neighbors in Southeast Asia. For this a more concerted reform surge is required, one that must include transforming the state's role in the financial sector. Such transformation must include reducing the state's own claims on Myanmar's financial resources, creating a regulatory environment that instills trust along with greater freedoms to transact, and greatly curtailing the role of state-owned institutions in a sector that needs to respond to the needs of free and private actors.

In 2009 this author wrote a book that attempted to tell the history of Myanmar's bankers and financiers. The book was called *Fiery Dragons* in homage to the entrepreneurs who were greatly responsible for Myanmar's emergence as the world's largest rice-exporting nation at the dawn of the twentieth century. For the past 50 years the fires of Myanmar's bankers have been doused. May the future bring them roaring back.

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