International Monetary Fund

Myanmar and the IMF

Myanmar: Staff-Monitored Program: Letter of Intent and Memorandum of Economic and Financial Policies

June 12, 2013

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Myanmar—Letter of Intent

Nay Pyi Taw, June 12, 2013

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Ms. Lagarde,

The outlook for Myanmar's economy continues to improve. Macroeconomic stability, strong growth, and high investor interest are signs that the implementation of our ambitious reform program to improve the economic and social well-being of Myanmar's citizens is bearing fruit. Continued regularization of our international financial relations, aided by successful arrears rescheduling agreements with multilateral and bilateral creditors, should underpin continued growth and economic integration. Nonetheless, the liberalization of the economy and the expected inflows of capital will provide challenges to our macroeconomic management capacity and we will press ahead with rapidly building our macroeconomic management tools.

We remain strongly committed to the program of reforms detailed in our Letter of Intent (LOI) of December 28, 2012. This letter reports on the outcome of our first review of progress against the objectives of the supporting jointly-monitored program—called a Staff Monitored Program (SMP) by the IMF. The attached Memorandum of Economic and Financial Policies (MEFP) details our updated economic and institutional reform priorities through December 2013.

We have made good progress in implementing our program. All SMP quantitative and structural benchmarks for end-March 2013 were met. Reserve accumulation of the CBM significantly exceeded the target and fiscal targets were met comfortably. Payment restrictions on invisibles have been lifted, private banks enabled to offer foreign exchange operations at par with state banks, and a plan for withdrawing Foreign Exchange Certificates has been announced and is being implemented.

Our government is also on the right track to meet the quantitative and structural benchmarks for September 2013. Fiscal deficit financing targets remain appropriate for our projected deficit outturn of 5 percent of GDP. This does not take into account proceeds from the sale of licenses for telecommunications and oil and gas blocks, which we will use to build fiscal buffers and to finance spending on priority areas over the medium-term in a manner consistent with maintaining macroeconomic stability. We also expect to attain the structural benchmarks for September 2013 relating to the establishment of the Large Taxpayer Office and treasury securities auctions.

We expect the law to establish an autonomous Central Bank of Myanmar to be enacted soon. Developing monetary policy tools is critical for achieving our program goals and we intend to accelerate progress in this area in advance of the law's enactment**.** In particular, we have begun holding bi-weekly deposit auctions and propose to include their continuation as a new structural benchmark.

We remain strongly committed to reaching the objectives of our reform program, including the SMP objectives. This is also reflected in our dialogue with development partners and creditors, and in their endorsement of our Framework for Economic and Social Reform in the Nay Pyi Taw Accord in January 2013, as well as in the agreement reached with the Paris Club on rescheduling of arrears in the same month.

We believe that the policies and measures set forth here and in our LOI dated December 28, 2012 and the accompanying MEFPs, will allow us to achieve the objectives of our program. However, we will take any additional measures that may become necessary for this purpose. We will continue to consult closely with IMF staff on our adoption of such measures, and in advance of any revisions to the policies contained in the MEFP. The government will provide IMF staff with all the information it requests to assess implementation of the SMP.

Our government authorizes the IMF to publish this Letter of Intent, and the attached MEFP.

Sincerely yours,

/s/	/s/
U Win Shein	U Than Nyein
Union Minister of Finance and Revenue	Governor, Central Bank of Myanmar

Attachment I. Myanmar—Memorandum of Economic and Financial Policies

I. INTRODUCTION

1. **Economic activity in Myanmar has been robust.** Growth is estimated to have risen to 6½ percent in 2012/13, driven by gas production, construction, and services. Inflation rose to 6 percent (y/y) in December 2012, but has since declined to 4.7 percent in March 2013. International reserves, some of which are still held by state banks, have increased to $4.6 billion at end-March 2013, covering 3¾ months of prospective imports. The fiscal deficit in 2012/13 is estimated at 3¾ percent of GDP, slightly lower than envisaged earlier, largely as a result of large increases in tax collections.

2. **The outlook for Myanmar's economy continues to improve.** Growth in 2013/14 is expected to accelerate slightly, led by rising gas production and investment, including in the transport, energy and telecommunications sectors. Inflation is projected to remain contained at around 6½ percent (y/y). International reserves are forecast to continue to rise. Financial intermediation is expected to increase further, with broad money and credit to the economy continuing to expand at double-digit rates. Over the medium term, we expect Myanmar's significant economic potential to be realized, with sustained growth of around 7 percent. We will continue to increase our investment in health, education and infrastructure to ensure that growth is broad based and supports poverty reduction.

3. **Our Government's overarching development goals are outlined in the Framework for Economic and Social Reforms.** To achieve these goals we have identified as policy priorities (i) sustained industrial and agricultural development to attain poverty alleviation and rural development; (ii) equitable sharing of resources among regions and states while promoting local and foreign investment; and (iii) effective implementation of people-centered development, through community-driven, participatory approaches to improve education, health, and overall living standards. Full economic integration with ASEAN in accordance with the ASEAN Economic Community schedule will reinforce these policies. Key measures to implement our policies are land reform, improving access to credit, and supporting access to both domestic and overseas job markets, as well as industrial development to provide job opportunities.

II. PROGRAM OBJECTIVES AND POLICIES

4. **We recognize that to achieve our broader goals ensuring macroeconomic stability during the reform process is critical.** Our program therefore aims to (i) maintain low and stable inflation, increase our international reserves to provide a buffer against external shocks during the reform process, and ensure debt sustainability; and (ii) lay the foundations for sustainable growth by building a macroeconomic framework and develop the institutions and instruments to use it effectively.

5. **As we continue with our reforms, we have requested IMF staff to assist us in monitoring our economic policies through December 2013**. Our work with IMF staff will focus on the following areas: (i) eliminating remaining exchange restrictions and multiple currency practices (MCPs); (ii) developing monetary policy institutions and tools to support price stability; (iii) modernizing the financial sector to facilitate macroeconomic management and growth; and (iv) laying the foundations for improving our fiscal revenues in the medium term for sustainable development spending. In all of these areas, we are requesting continued IMF technical assistance (TA).

A. Foreign Exchange Policies

6. **We have taken significant steps to improve the operation of the foreign exchange market.** We have ensured through increased interventions and the consequent deepening of the foreign exchange market that the informal market rate and the reference rate have converged further. To complement authorized dealer banks and encourage the move from informal to formal markets, we have also licensed a number of non-bank money changers. Payment restrictions on invisibles have been lifted, private banks enabled to offer foreign exchange operations at par with state banks, and a plan for withdrawing Foreign Exchange Certificates is being implemented (all structural benchmarks).

7. **We remain committed to accepting the obligations of Article VIII Section 2(a), 3 and 4 of the IMF's Articles of Agreement and level the playing field for private banks.** To further facilitate the replenishment of private banks' overseas accounts, the CBM is preparing to place banks' purchases of foreign exchange from the formal auction, upon request, directly into these accounts. We will also continue allowing profit transfers abroad after payment of profit taxes without further restriction. Furthermore, we will consolidate recently issued instructions into a consolidated set of implementing regulations for the Foreign Exchange Management Law, which will be issued by the end of 2013. We will also continue our policy of supplying sufficient liquidity to the foreign exchange auctions to avoid large deviations from the informal market, and not target any specific exchange rate level. Finally, we will seek continued approval of the IMF's Executive Board for the multiple currency practice arising from our multi-priced foreign exchange auctions, which is nondiscriminatory and will be maintained on a temporary basis until the foreign exchange market develops.

B. Monetary Policy and Operations

8. **Strengthening our capacity to conduct monetary policy is a critical prerequisite for macroeconomic management.** To this end, we are in the process of preparing a revision of the definition of required reserves to include only current account balances with the CBM, lengthen the reserve maintenance period to two weeks, and adjusting the required reserve and liquid asset ratios, in line with previous IMF TA recommendations. We have also begun to forecast liquidity and reserve money, and conducted several deposit auctions, but our ability to conduct monetary operations is constrained by the limited budget allocated by the Hluttaw for this purpose. Nonetheless, we have begun holding deposit and credit auctions regularly every two weeks with small volumes, and will

step up volumes to sterilize our foreign exchange operations once budget constraints are eased. To strengthen monetary policy transmission, we have also removed the ban on interbank trading.

9. **Final enactment of the new law to give greater autonomy to the CBM has been delayed.** While the law was approved in March 2013, legal considerations necessitate revisions before it can be enacted. Once the law is passed, we intend to fully use our monetary policy tools.

10. **We will reinforce our efforts to establish effective control over monetary conditions, even ahead of the implementation of the new CBM law.** To this end, we will continue to gradually transfer international reserves from state banks to the CBM. We will also continue our bi-weekly deposit auctions (continuous structural benchmark), and will ease budget constraints in the supplementary budget until they are lifted with the implementation of the CBM law. We will also further strengthen our capacity to forecast key monetary aggregates, making use of IMF TA. We continue to aim to move to a reserve money targeting framework during 2014 following the establishment of a track record of deposit auctions and the revision of reserve requirements for private banks, which we intend to implement without waiting for the CBM law to come into force. The revised reserve requirements will be extended to state banks when sufficient capacity is developed. To better manage foreign exchange risk, we have abolished the mandatory surrender requirement for foreign exchange and, with IMF TA, will develop instructions on limiting banks' net open foreign exchange position

C. Financial Sector Modernization

11. **A modern well-regulated financial sector is important to support monetary policy transmission and finance public sector deficits without recourse to monetization.** To promote the expansion of financial services, we have eased capital requirements for opening new bank branches, and abolished the capital-to-deposit ratio. We have also permitted the Myanmar Economic Bank (MEB) to purchase treasury bills to reduce its excess liquidity, but this has not been sufficient to eliminate it. We have begun to develop a draft regulation that will establish treasury security auctions (structural benchmark) and will move toward implementation with IMF TA support.

12. **Modernizing prudential regulations and developing supervisory capacity are critical prerequisites for further liberalization of the financial sector.** Once IMF resident advisors on bank regulation and supervision are in place, we will bring the definitions of bank capital and nonperforming loans closer to international standards; strengthen the enforcement of connected lending limits to contain risks to financial stability during the modernization process of the financial sector; and improve banks' risk management as a precursor to liberalization of lending rates and maturities. These changes will be implemented step by step, in line with the development of needed supervisory capacity.

13. **We will also prepare to integrate the MEB more fully into the nascent market-based financial system.** To this end, we will, once the new CBM law is promulgated, the new reserve requirements are applied to the MEB, and treasury securities auctions started, consider options for

fully absorbing MEB's remaining excess liquidity (e.g. through a swap against treasury bills held by the CBM) and allowing the MEB to freely participate in treasury securities auctions.

14. **The increasing role of private banks in foreign exchange operations and the ongoing transfer of reserves to the CBM necessitate a reconsideration of the role of the Myanma Foreign Trade Bank (MFTB) in the financial system.** We will therefore begin to consider options for MFTB reform, and will request IMF TA to help us in developing and assessing alternatives.

D. Fiscal Policies

15. **Our fiscal policy is geared toward maintaining macroeconomic stability, especially as monetary policy tools are still being developed, while addressing the large development needs of our country.** To this end, we have passed a budget for 2013/14 that envisages further growth in education and health current expenditure. Reduced allocations for capital arise from the near-completion of several projects for the 2013 South East Asia Games. We also expect the need to increase spending on security, due to continued ethnic and religious unrest, and intend to increase allocations for priority sectors in the forthcoming supplementary budget. Nonetheless, we will ensure that the overall budget deficit (IMF definition) will remain around the 5 percent of GDP we believe is consistent with macroeconomic stability. We aim to keep the deficit around this level over the medium term while continuing to increase allocations for health and education as well as infrastructure investment. Nonconcessional financing will be used only for economically viable projects in priority sectors such as energy and infrastructure, at levels consistent with maintaining debt sustainability and low risk of debt distress.

16. **Modernized fiscal systems are essential to improve public service delivery and accountability.** We have developed a comprehensive strategic plan to modernize our tax administration, the centerpiece of which is the establishment of the Large Taxpayer Office (LTO). We have also formed a working group to develop reform strategies for public financial management (PFM) and serve as a tool for donor coordination, after receiving TA from the IMF and World Bank, and launched a public expenditure review (PER) with the World Bank to better inform our fiscal policies and improve the efficiency of public spending in our priority areas.

17. **We remain committed to broadening the tax base and improving compliance to raise resources for development spending and to reduce our reliance on natural resources.** We have therefore formed a Scrutinizing and Monitoring Tax Collection Board, with government and private sector participation, to advise on a tax reform action plan. Introducing a value added tax remains our medium-term goal; in the interim, we are considering reforming the taxation of special consumption goods (such as alcohol, tobacco, luxury items, and polluting goods) and expanding the taxation of services. In our tax policy strategy, while conscious of the need to attract investment, we will establish the principle of streamlining and limiting tax exemptions to ensure a broad revenue base. This principle will also inform the implementation of other planned laws, including the small and medium enterprises law currently being debated, and the revised law on special economic zones, which is currently being considered by the Hluttaw. Our short-term priority in tax administration is to ensure a successful establishment of the LTO (structural benchmark) which will

pave the way for eventually rolling out taxpayer self-assessment across the tax system. We will therefore allocate sufficient resources to the LTO in the forthcoming supplementary budget for it to adequately prepare for taking over the administration of large taxpayers at the beginning of 2014/15.

18. **Improving public financial management is crucial for successful development outcomes and enhancing transparency.** To this end, we will finalize our PFM strategy and disseminate it to development partners in July 2013. The strategy will focus on key priorities including: (i) budget formulation; (ii) strengthening fiscal discipline and expenditure control; and (iii) fiscal accounting and reporting. An early action will be establishing a treasury department with cash and debt management functions in the Ministry of Finance and Revenue during 2013 with TA from the IMF and other partners. We also expect to finalize the PER during 2014 and will use the early analysis to inform the preparation of our 2014/15 budget.

E. Policies for Growth

19. **The ultimate goal of our economic policies is to attain sustainable growth and poverty reduction.** In addition to the institutional and macroeconomic policy reforms outlined above, the focus of our reforms is on improving health and education, and attracting domestic and foreign investment to enhance human capital and attain higher growth. In addition to increased allocations for health and education in our budget, we are also working with our development partners to build strategies to maximize the impact of our expenditure, and obtain additional funding. To promote investment, we have issued implementing regulations for the foreign investment law passed last year, and laws on special economic zones and small and medium enterprises, which are key to supporting industrialization, are expected to be passed by the Hluttaw in 2013. We are also focusing on attracting international investment to develop critical infrastructure, including energy, transport and telecommunication. Transparent tendering processes have been adopted in these areas, as demonstrated by the recent auctioning processes for telecoms licenses and oil and gas blocks. To support agricultural development we are giving high priority to implementing the new land and microfinance laws recently passed by the Hluttaw.

F. Statistics

20. **We continue to place high priority on improving the accuracy and timeliness of our statistics.** We have already accelerated the provision of monetary data to the IMF, and have re-estimated GDP for 2010/11 and 2011/12. With assistance from our partners, including the IMF, we intend to move forward in developing an updated national accounts series with broader coverage, an updated CPI, and enhanced coverage of the balance of payments. We will also strive to improve fiscal and monetary statistics, including through more timely provision.

III. PROGRAM MONITORING

21. **We will continue to closely monitor the implementation of our program.** In addition to the structural benchmarks for end-September already set in our MEFP of December 28, 2012, we

have also introduced one new benchmark to reflect the need for additional measures to ensure that intended program outcomes are achieved (Table 2). The definitions of the relevant variables remain as outlined in the Technical Memorandum of Understanding attached to our MEFP of December 2, 2012. However, the target for net domestic financing of the nonfinancial public sector deficit will be adjusted downward by the amount of proceeds from telecommunications licenses, which we will report to the IMF's Asia and Pacific Department. Also, we will henceforth report to the IMF's Asia and Pacific Department the receipts, payments, and the balances of the State Fund Account and all its sub-accounts on a monthly basis, no more than six weeks after the end of each month.

22. **Our SMP Monitoring Committee continues to monitor implementation of our program.** It includes senior representatives from the CBM, Ministry of Finance and Revenue and the Ministry of National Planning and Economic Development and reports regularly to the Minister of Finance and Revenue on progress in the implementation of our program. The Committee also works with IMF staff in conducting formal reviews of progress; the next review is due to take place in January 2014.

Table 1. Myanmar: Quantitative Benchmarks 1/

	Sep 2012	Dec 2012	Mar 2013	Jun 2013	Sep 2013	Dec 2013	Mar 2014
Net international reserves of the CBM (floor) 2/							
(cumulative flow from end-September 2012; in millions of US$)							
Target/Projection 3/	...	...	**705**	1,300	**1,504**	1,916	2,125
Actual	...	974	**948**				
Target met			Yes				
Net domestic financing of the NFPS deficit (ceiling) 4/							
(cumulative flow from the beginning of the fiscal year to end-period; in billions of kyat)							
Target/Projection 3/	...	...	**1,921**	343	**1,053**	1,523	1,815
Actual	-346	-390	**952**				
Target met			Yes				
Net CBM financing of the NFPS deficit (ceiling) 4/							
(cumulative flow from the beginning of the fiscal year to end-period; in billions of kyat)							
Target/Projection 3/	...	...	**960**	31	**191**	314	794
Actual	-453	-914	**645**				
Target met			Yes				
Accumulation of new external payment arrears by the non-financial public sector (ceiling) 5/							
(ceiling on stock at end-period; in millions of US$)							
Target/Projection 3/	0	0	**0**	0	**0**	0	0
Actual			**0**				
Target met			Yes				
Contracting or guaranteeing of nonconcessional external debt (ceiling)							
(cumulative flow from the beginning of the fiscal year to end-period; in millions of US$)							
Target/Projection 3/	...	...	**2,000**	2,000	**2,000**	2,000	2,000
Actual			**0**				
Target met			Yes				

1/ Fiscal year begins April 1.
2/ Includes SDRs and gold. Valued at program exchange rate of US$/euro=1.27 and a gold price of US$1,750 per troy ounce.
3/ Targets are set for September 2013.
4/ The nonfinancial public sector (NFPS) comprises the Union government and state economic enterprises. A program exchange rate of 850 kyat/US$ applies.
The target will be adjusted downward by the amount of proceeds from the auctioning of telecommunications licenses.
5/ Excludes accumulation of new arrears on debt already in arrears.

Table 2. Myanmar: Structural Benchmarks

Actions	Macroeconomic Objective	Date	Status
For first review			
Eliminate exchange restrictions on payments and transfers for invisibles (¶6)	To eliminate Article VIII restrictions	March 2013	Met
Announce plan for phasing out Foreign Exchange Certificates (¶6)	To eliminate a multiple currency practice	March 2013	Met
Remove restrictions that prevent private banks from conducting foreign exchange operations at par with state banks (¶6)	To help unify informal exchange	March 2013	Met
For second review			
Conduct bi-weekly deposit auctions (¶10) (new benchmark)	To help establish control over monetary aggregates	Continuous from June 2013	In progress
Prepare regulations to introduce treasury securities auctions (¶11)	To facilitate market-based deficit financing	September 2013	In progress
Establish an operational large taxpayer unit (¶17)	To improve tax administration and increase tax revenues	September 2013	In progress