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## **Expanding Cooperative Credit in Myanmar: Renaissance or Regression?**

*By Sean Turnell\**

### EXECUTIVE SUMMARY

- In late 2013, Myanmar's Cooperatives Minister announced a dramatic expansion of the country's cooperative credit system.
- Funded partially by a loan from China, the declared intention is to extend cooperative credit institutions into each of Myanmar's 60,000 villages.
- The historical record of cooperative credit in Myanmar is not a happy one. Used for the most part as populist devices to dispense largesse and political favour, such institutions have proved unstable and financially unsustainable.
- There is little to suggest this latest expansion of cooperative credit in Myanmar will defy the historical trend. Founded upon state direction and provision, the sector's surge threatens to undermine nascent efforts otherwise to create viable rural financial institutions built upon more effective methodologies.

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- Rural indebtedness and a chronic lack of capital are endemic in Myanmar, but such maladies will not be alleviated from an expansion of cooperative credit as it is currently constituted.
  - Myanmar needs a self-sustaining, commercially-focused financial system built upon a range of institutions that history and practice reveal as necessary for truly transformational growth. Plans to expand cooperative credit in Myanmar are, at best, a diversion from this task.
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## INTRODUCTION

In late 2013, Myanmar's Ministry of Cooperatives announced highly ambitious plans for the expansion of its portfolio of village-based financial institutions. These plans, which aim to dramatically increase the amount of funds made available by the Ministry to financial cooperatives, as well as to expand their number to at least 'one per village', are ostensibly part of an effort to both revive Myanmar's debt-laden rural economy, and to finance the importation of new machinery and equipment. To kick off all of this, Myanmar is to borrow \$100 million from the Export-Import Bank of China. In reaction to the latest of the Cooperative Ministry's announcements, Phyo Win, an MP with the National League for Democracy (NLD), noted that cooperative enterprises had 'always been a failure' in Myanmar.<sup>1</sup> Other MPs took a similar line, with representative Tin Nwe Oo rhetorically asking 'how many times has the cooperative system succeeded in our country?', while also noting in passing the high interest rate China was charging for its initiating credit.<sup>2</sup> Upper house MP, Phone Myint Aung (of the New National Democracy Party) opined that the loan programme 'won't really change the lives of the farmers'.<sup>3</sup> The Minister of Cooperatives, Kyaw Hsan, himself acknowledged that 'the cooperative system has not succeeded in the past', before adding, 'but we will try to learn from our mistakes'.<sup>4</sup>

The MPs cited here are right to be concerned. Put simply, cooperatives *have* always been a failure in Myanmar.<sup>5</sup> Established initially by the British colonial authorities to dilute the dominance of the *Chettiar* moneylenders, as well as to curry favour with the local populace, the first iteration collapsed in the 1920s amidst both economic depression and a widespread lack of faith in the system. The revival of the cooperatives post-independence (when they were seen as an acceptable device existing somewhere in 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. Following 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 petty (and not so petty) corruption, before disintegrating into effective irrelevancy. Up until the recent

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<sup>1</sup> 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.mmmtimes.com/index.php/national-news/7947-mps-approve-loan-despite-concerns-over-interest.html>> accessed January 3, 2014.

<sup>2</sup> Tin New Oo is cited in 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>> accessed January 2, 2013.

<sup>3</sup> As above.

<sup>4</sup> Kyaw Hsan cited in Win Ko Ko Latt, "MPs Approve Loan Despite Concerns Over Interest", *The Myanmar Times*, August 20, 2013 <<http://www.mmmtimes.com/index.php/national-news/7947-mps-approve-loan-despite-concerns-over-interest.html>> accessed January 3, 2014.

<sup>5</sup> For details on the long history of financial cooperatives in Myanmar, see Sean Turnell (2009), *Fiery Dragons: Banks, Moneylenders and Microfinance in Burma*, NIAS Press, Copenhagen.

pronouncements it is perhaps fair to say that the consensus amongst financial sector stakeholders in Myanmar is that the cooperative credit system, as it existed, was essentially moribund, an artefact of history unsuited to modern financial practices.

## CONTEXT

Precise data with respect to the current cooperative credit system in Myanmar are not available. That caveat in place, according to the *best* sources available, there are around 1,650 or so 'Financial Cooperatives' in Myanmar.<sup>6</sup> These have around 500,000 members, have loans outstanding of about K17 billion, and have total deposits of around K25 billion. The average cooperative loan is currently around K35,000 (around \$US40).

In order to get some sense of magnitudes, the largest (and very dominant) microfinance scheme in Myanmar, that operated by the US NGO 'PACT' in collaboration with the United Nations Development Programme (UNDP), has around 420,000 members, K60 billion in outstanding loans, and K11 billion in deposits.<sup>7</sup> In short, the PACT microfinance scheme is a more focused and larger lender than the cooperative system, which otherwise has more members and accumulates more in deposits. The numbers might seem doubtful, but note that a sizeable number of cooperative members are likely to be marginal participants at best.

## THE 2013/14 EXPANSION PLAN

As declared in a series of speeches by the Minister of Cooperatives, Kyaw San (the former Minister for Information), as well as by the Deputy Minister, Than Tun, Myanmar's cooperative credit system is to be dramatically expanded. According to their announcements, the number of cooperative societies will increase by 5,000 and, subsidiary to these, 'borrowing 'groups' (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.<sup>8</sup>

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<sup>6</sup> Probably the best data source for Myanmar's cooperative credit system is the microfinance sector assessment undertaken by the International Finance Corporation of the World Bank. See Duflos, E, Luchtenburg, P, Li Ren and Li Yan Chen, *Microfinance in Myanmar: Sector Assessment*, International Finance Corporation/Consultative Group to Assist the Poorest, Washington D.C. The Report can be found at <<http://www.cgap.org/sites/default/files/Microfinance%20in%20Myanmar%20Sector%20Assessment.pdf>> accessed January 2, 2014.

<sup>7</sup> Duflos, E, Luchtenburg, P, Li Ren and Li Yan Chen, *Microfinance in Myanmar: Sector Assessment*, International Finance Corporation/Consultative Group to Assist the Poorest, Washington D.C. The Report can be found at <<http://www.cgap.org/sites/default/files/Microfinance%20in%20Myanmar%20Sector%20Assessment.pdf>> accessed January 2, 2014.

<sup>8</sup> The comments of the Deputy Minister were made before an international conference on microfinance in Myanmar, held in Naypyitaw on May 9-10, 2013. The conference proceedings, "Emerging Microfinance Sector in Myanmar: Regional Lessons on Selected Issues" <[http://www.mm.undp.org/UNDP\\_Publication\\_PDF/MFWSReport.pdf](http://www.mm.undp.org/UNDP_Publication_PDF/MFWSReport.pdf)> accessed January 3, 2014.

The Ministry promises to supply each of the village borrowing groups with K100,000 in start-up capital. From this point, savings mobilisation 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.<sup>9</sup>

Under the new system loans can be used for a number of *business* purposes, but the expectation is that farmers will use borrowings to go towards buying 'tractors, tractor trailers, trucks, engines, generators, water pumps and motorbikes'. Urban borrowers are expected to purchase 'taxis, sewing machines, trishaws and motorbikes'.<sup>10</sup>

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.

Meanwhile, cooperative credit amongst eight townships of Myanmar's capital, Naypyitaw has been expanding—something of a pilot project for the broader system. This involves the provision of K7 billion in funds, spread amongst 205 cooperative societies and their roughly 12,500 members. Loans are up to K500,000 (in line with the broader scheme) and are meant to be used for the purchase of 'agricultural vehicles and machinery'.<sup>11</sup>

## FUNDING

According to Minister Kyaw Hsan, the cost of expanding Myanmar's cooperative credit system in the ways outlined above would ultimately amount to between K600 billion and K3 trillion (around \$US630 million - \$US3.15 billion).<sup>12</sup>

To initiate the expansion, however, Myanmar has already secured a \$US100 million loan from China's Export-Import Bank. This loan has a term of ten years, the first two years of which will be free of interest, after which an interest rate of 4.5% is levied. In addition to the interest charges, an immediate 1% 'management fee' is to

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<sup>9</sup> 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.

<sup>10</sup> Statement made at the aforementioned international conference on microfinance in Myanmar, held in Naypyitaw on May 9-10, 2013. The reference to the purchase of motorcycles presumably excludes potential customers living in Yangon, within the environs of which motorcycles are effectively banned.

<sup>11</sup> For more on this pilot scheme, see Hsu Hlaing Htun, "First Phase of Ambitious Ministry Lending Program Launched in Nay Pyi Taw", *The Myanmar Times*, August 25, 2013 <<http://www.mmmtimes.com/index.php/national-news/7946-first-phase-of-ambitious-ministry-lending-program-launched-in-nay-pyi-taw.html>> accessed December 17, 2013.

<sup>12</sup> Kyaw Hsan cited in Hsu Hlaing Htun, as above.

be paid by Myanmar at the moment the loan is drawn down. The actual borrower of this US dollar loan is the Myanmar Foreign Trade Bank (MFTB), which then advances the Ministry of Cooperatives an equivalent sum of kyat, for on lending to cooperative members.<sup>13</sup> The reason the loan has been taken in US dollars appears to be because it is Chinese imported goods that are the items borrowed against by cooperative customers. As such, the whole arrangement is not unlike a vast hire purchase scheme.<sup>14</sup> The benefits to the Chinese suppliers from this is clear and apparent. Whether the arrangement locks Burmese borrowers into the purchase of items they might not otherwise freely choose is an open (and worrying) question.

Longer term, and noting the 'gap' between the size of the Chinese loan and the ultimate cost estimates of the expanded programme, Deputy Cooperatives Minister, Than Tun, made clear that the intention of the Ministry was to seek 'aid, grants, and concessional loans from international organizations'.<sup>15</sup> The quest for international funding has also been a theme in a number of the speeches made by Minister Kyaw Hsan.

## ASSESSMENT

Not least of the serious difficulties presented by the announced expansion of Myanmar's cooperative credit system is that highlighted by the MPs above – simply that such initiatives have been applied many times before, with dismal effect. Are matters different now? It is hard to see how they might be. The design of the programme outlined thus far seems probable to repeat past errors, especially in the way in which it is so overwhelmingly state-driven and operated. In this latest version, however, state direction is not only apparent in the construction and funding of the system itself, but also in the possible 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 'look in'.

Myanmar has been without a properly functioning financial system for five decades. This 'absence' remains in 2014, even as certain *potential* foundations are currently being laid. Nowhere is this nascent potential more apparent than in the microfinance sector. Newly legalised and formalised under the 2011 Microfinance Law, the microfinance sector in Myanmar has been growing strongly (there are now

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<sup>13</sup> 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>> accessed January 2, 2013.

<sup>14</sup> The 20 August report in the *New Light of Myanmar* supports the idea that this is the arrangement.

<sup>15</sup> Statement made at the aforementioned international conference on microfinance in Myanmar, held in Naypyitaw on May 9-10, 2013, see Duflos, E, Luchtenburg, P, Li Ren and Li Yan Chen, *Microfinance in Myanmar: Sector Assessment*, International Finance Corporation/Consultative Group to Assist the Poorest, Washington D.C. The Report can be found at <<http://www.cgap.org/sites/default/files/Microfinance%20in%20Myanmar%20Sector%20Assessment.pdf>> accessed January 2, 2014.

around 170 authorised schemes). This is manifested in positive ways in terms of some new and promising institutions coming along. Less positive is the probable too-rapid expansion of some less appropriate operators, including a cohort of moneylenders and others whose motivation might be questionable.

Into this mix will now come this new cooperative credit surge, potentially swamp-ing the market for micro-loans with easy credit, undermining the repayment incentives of borrowers in other schemes, and along the way introducing new avenues of over-indebtedness and systemic risk. This has been the experience in other countries (India most obviously) with the arrival of undisciplined state-backed lending schemes, as it has in Myanmar's own history<sup>16</sup>.

More than a few of the criticisms from MPs of the cooperative credit expansion plans centre on its funding via the Chinese loan. Such critics point to the relative high interest rate charges of this debt (its 4.5% per annum levy plus management fee compares especially unfavourably to concessional lending from the World Bank, Japan and others).<sup>17</sup> An issue in and of itself (Myanmar is hardly in a position to be complacent about external debt and its recurrent costs), the interest paid to China's Export Import Bank has to be met by the ultimate borrowers of the scheme – that is, Myanmar's farmers, small enterprise proprietors, and workers.

Whilst the overall volume of credit promised under the revitalised cooperative system is large, the loans available to individual borrowers are not. At the projected maximum of K500,000, they are not sufficient to be transformative, even for micro-enterprises, and are well short of the funds required for the very items held out to attract potential borrowers – that is, the 'tractors, motorbikes, taxis and sewing machines...' evoked by the Minister.

## CONCLUSION

The re-emergence of cooperative credit in Myanmar at the scale projected is not a positive development in the country's economic reform trajectory. An instrument from an earlier era when the state and its organs were central to Myanmar's reigning ideology, is not an answer to the country's problems evident from the information we have at present on the cooperative system. None of this is to say that Myanmar's farmers, business owners or people broadly have sufficient access to financial services. Indeed, far from it. However, the answer to rural indebtedness, insufficient capital and financial insecurity is not to be found by a return to an expanded cooperative

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<sup>16</sup> For more on the tribulations of microfinance in India, see Philip Mader, "Microfinance in India: The Andhra Pradesh Crisis in Perspective", *Strategic Change*, 22:1 (February 2013), pp.47-66.

<sup>17</sup> The World Bank's 40-year, \$US260 million development loan to Myanmar is charged at 0.75% per annum. For details, see the World Bank's Myanmar web pages, <<http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/0,,pagePK:64392398~piPK:64392037~theSitePK:40941~countrycode:MM~menuPK:64820000,00.html>> accessed December 24, 2013.

system. What Myanmar needs is a functioning financial system comprising a diverse range of institutions that practice and history submit are indispensable to genuinely transformational growth and development. Creating such a system will not be simple, but it is the real task at hand.

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