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## **Improving the Performance of the State Economic Enterprise Sector in Myanmar**

*By Lex Rieffel\**

### **EXECUTIVE SUMMARY**

- The Myanmar economy virtually became one big state economic enterprise (SEE) in the Ne Win era beginning in 1962. The failure of Ne Win's socialist path to development eventually led to the popular uprising that prompted Ne Win's resignation in 1988.
- The military junta that crushed the uprising declared its support for market-based economic growth and began a process of privatizing state enterprises that proceeded in waves over the next 23 years. Nevertheless, the SEE sector remained significant at the end of the junta era in 2011 when former general Thein Sein was elected president.
- The Thein Sein government promptly launched an ambitious programme of peace building, democratic institution building, and economic reform. Privatization of SEEs was one of the government's priorities, but its implementation has been mixed. Every part of the government is actively engaged in privatization activities, but each in its own way. No common policies or procedures exist.
- With less than one year remaining in its 5-year term, there may be little the Thein Sein government can do to improve the performance of the SEE sector as a whole. The following actions could make it easier for the next government to achieve better results:

- a) Increase the transparency of the SEE sector. Posting a list of all SEEs on a dedicated website would be a useful first step. A separate web page for each SEE could provide the following minimum information: responsible ministry, name of Chief Executive Officer, scope of operations, actual budget revenue and expenditure for the last fiscal year, projected revenue and expenditure for the current fiscal year, and contact information for the SEE home office.
  - b) Proceed with the corporatization of all enterprises that appear to have the potential of operating profitably. This is probably best done not by a broad fiat from above but selectively where the stakes are high or where the managers seem inclined toward this move.
  - c) Establish a dedicated SEE policy unit to provide consistency in managing the government's SEEs, and develop preliminary guidelines for the unit. The unit could be located in the Finance Ministry, the Ministry of National Planning and Economic Development, or the President's office. The guidelines would set forth the scope of the unit's work, procedures for coordinating with relevant ministries and agencies and the legislature, principles for privatization actions, and near term priorities.
  - d) Recruit two or three outstanding CEOs to turn around two or three visible, mid-sized SEEs, and give them the support they need to succeed.
  - e) Design a scheme for buying out redundant SEE employees. This action might be the single most important contribution the Thein Sein government can make to improve SEE sector performance. Multilateral and bilateral aid agencies could provide matching financing for the scheme.
- Each of these actions has a cost. Each is easier said than done, and successful approaches in other countries may not work in Myanmar. In the absence of reliable data, good judgments by policy makers are likely to be the key to success in Myanmar.
  - The best intentions of the Thein Sein government or its successor may not yield results that meet the elevated expectations of Myanmar's population or those of foreign investors and friendly governments. State capacity in Myanmar is low. Success in improving the performance of the SEE sector is likely to come faster and better if expectations are lowered to match the slow-growing ability of the government to manage the sector effectively.

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## **INTRODUCTION**

Like many countries now and in the past, Myanmar has a substantial state economic enterprise (SEE) sector that is underperforming in two major ways. First, its financial returns are well below potential. Second, the quality of its goods and services is generally inferior to the quality of those offered by private sector competitors.

Myanmar inherited a number of important SEEs when it gained its independence from Great Britain in 1948. More SEEs were created in the period of parliamentary democracy (1948-1958). The economy virtually became one big SEE sector in the period of General Ne Win's rule (1962-1988). Almost all modern production units were nationalized as Ne Win pursued a socialist path to development.

As the SEE sector grew in the Ne Win period, the per capita income in Myanmar sank, contrary to the trend in the rest of East Asia. A popular uprising in 1988 forced the resignation of the socialist government and the junta that took power abandoned the socialist path in favour of market-based economics. Naturally part of the new strategy included the privatization of SEEs. This process proceeded in waves over the next 23 years, but the SEE sector was still at the heart of the Myanmar economy when former General Thein Sein became President in 2011.

Privatization of SEEs has been part of the Thein Sein government's ambitious economic reform programme from the beginning, but its implementation has been mixed. The rent-seeking nature of the deals carried out under the previous government has not changed much. Every part of the government is actively engaged in privatization activities, but each in its own way. No common policies or procedures exist. As a result, it is likely that substantial values that could be retained by or accrue to the government are being captured by narrow private interests.

## **THE SEE SECTOR IN EARLY 2015**

The SEE sector in Myanmar is vast and diverse. Describing it is made difficult by the absence of any official list of SEEs. The starting point for the present study was the *Yangon Directory 2014*, the main English-language "yellow pages" for Myanmar. It includes a section with the phone numbers for the main administrative units in the ministries and agencies of the central government, including many "enterprises". With a number of adjustments based on interviews and news reports, a list of 44 SEEs was arrived at. (See Appendix.)

These can be divided into eight categories for analytical purposes:

1. *The Petroleum Sector Giants.* The most important SEE by far is the Myanmar Oil and Gas Enterprise (MOGE) under the Ministry of Energy. It is the biggest single source of revenue for the government, derived primarily from the export of natural gas to Thailand and China. Two related SEEs under the same ministry are the Myanmar Petrochemical Enterprise (refinery production) and the Myanmar Petroleum Products Enterprise (wholesale marketing).
2. *The Major Mining Enterprises and the Timber Enterprise.* There are three separate mining enterprises under the Ministry of Mines overseeing dozens of different mining operations. The Myanmar Timber Enterprise under the Ministry of Environmental Conservation and Forestry is another major source of government revenue (from exported timber).
3. *The Public Utilities.* These include electricity generation, transmission and distribution, postal services, and transport services (road, water, air).
4. *The Main Industrial Enterprises.* There are three “heavy industry” enterprises under the Ministry of Industry. Three separate groups of light industries produce a wide range of products from paper to pharmaceuticals.
5. *Other Smaller Enterprises.* These are scattered among half a dozen ministries: agriculture, cooperatives, hotels and tourism, information, and livestock, fisheries and rural development.
6. *The State-Owned Banks and Financial Firms.* Four state-owned banks dominate the banking system (Economic, Foreign Trade, Investment and Commercial, and Agricultural Development).
7. *The Military-Controlled Enterprises.* Union of Myanmar Economic Holdings (UMEHL) and Myanmar Economic Corporation (MEC) are large conglomerates. They operate independently from the government to the extent of being perceived as being not state-owned.
8. *The Mysterious Enterprises.* The Myanmar Gems Enterprise may generate more “financial surplus” (especially from jadeite extraction) than all other mining enterprises combined, but its financial profile is opaque and it appears that only a small fraction of its surplus goes to the government budget.

A general problem with the list of 44 SEEs is that quite a few of them are not single coherent operating units. Instead, they are a collection of production and service units with no consistent form or mandate. A narrower but probably more important problem is that an enormous amount of privatization of government assets has been occurring outside the SEE sector as it is understood in Myanmar. Much of this privatization has been in the form of land concessions for commercial agricultural uses such as oil palm and rubber plantations.

It would be nice to show the size of the SEE sector in terms of contribution to GDP or share of employment, but the data are not good enough to produce a respectable estimate. One concern is that the SEE sector is impeding private sector growth. A surprising finding from interviews for this study was that leading Myanmar businessmen considered the SEE sector to be a low-level problem. They were more concerned about competition from foreign investors.

## **POLICIES AND IMPLEMENTATION**

The policies of the Thein Sein government for improving the performance of the SEE sector have been clear and consistent, beginning with the President's "second wave" speech in June 2012 when he said "we must trim down uneconomical and redundant enterprises and cut expenses, while shrinking the state-owned business sector and encouraging privatization." Specific actions were spelled out in the Framework for Economic and Social Reforms (FESR) presented to aid donors at the first Myanmar Development Cooperation Forum (MDCF) in January 2013. The FESR refers explicitly to the corporatization of the SEEs and the objective of keeping the government's "fiscal regime in order".

Another strong statement of policy is found on the Budget Department page of the Ministry of Finance website. Here it spells out that beginning with FY 2012-13, the SEEs no longer have automatic access to the budget to cover their deficits. Any deficit financing requires cabinet approval and enterprises incurring chronic deficits are to be privatized.

The FESR was designed as a link between the five-year plans of previous governments and a new 20-year National Comprehensive Development Plan (NCDP). The NCDP is expected to include ambitious measures for improving the performance of the SEE sector, but no details have been made public yet. It is scheduled to be presented to the legislature for approval around September 2015.

Implementation of the government's SEE sector policies has been mixed. Here are the main findings from the research carried out in the first quarter of 2015:

1. *Phasing in a Hard Budget Constraint.* The SEE sector as a whole is contributing the bulk of the consolidated public sector revenue, roughly 60 percent in FY 2014-15, while absorbing considerably less (roughly 45 percent) public sector expenditure. Thus the objective of having a hard budget constraint does not apply

to the SEE sector as a whole. Instead it applies to the many individual enterprises that have historically been operating at a loss and have relied on budget subsidies or borrowing from banks for their survival. None of the SEEs appear to be publishing their financial accounts so it is not possible to assess the effectiveness of the hard budget constraint policy. Perhaps more importantly, it is widely assumed that a large amount of “leakage” is associated with natural resource extraction. This is the amount of revenue that should be going into the government budget but is diverted to other places.

2. *Corporatizing SEEs.* Corporatization is generally considered the first step toward privatization of SEEs. Five unconfirmed cases of corporatization under the Thein Sein government were found, but only one confirmed case. By contrast, there are many examples of privatization in the form of leasing, joint venture, or “BOT” arrangements.
3. *Privatizing SEEs.* A major wave of privatization occurred in the final years of the preceding military regime, with little information disclosed about the price or the buyer of each asset sold. Under the Thein Sein government, there is little evidence of outright sales. Instead privatization has proceeded primarily through leasing of enterprises (and other government assets) to private parties. This form of privatization appears to have been carried out by most if not all government ministries and in an uncoordinated manner. A major obstacle in negotiating leases favourable to the government is that the private partners are required to retain the government workers employed by these enterprises or to maintain their salaries. A more fundamental issue is the loss of value associated with allowing each ministry and agency to select the assets to lease and the partner to whom it will be leased.
4. *Privatizing Public Utilities and Infrastructure Industries.* The Thein Sein government adopted a policy of cautious privatization in this area and its implementation has been commendable. In particular, it awarded licenses through a process close to international best practice to two foreign companies to build out the country’s mobile telephone network. It has also entered into Private Public Partnerships with foreign firms for electric power generation.
5. *Making Resource Extraction a Blessing.* In the FESR, the Thein Sein government committed to more socially responsible exploitation of its natural resources. A major step in this direction was taken when Myanmar achieved “candidate” status in the Extractive Industries Transparency Initiative. It is now working on a report, due in January 2016, which would enable the country to graduate to “compliant” status. The obstacles to progress in this area are immense and the prospects for reducing the lost rents from longstanding resource extraction practices are uncertain at best.

6. *The Privatization Commission.* The FESR indicated that the Privatization Commission created by the previous government would be reinvigorated and would play an important role in privatizing SEEs through transparent and socially beneficial procedures. There is no evidence, however, that the Privatization Commission has had a significant role in the post-2011 privatizations.

## **IMPROVING PERFORMANCE**

Four options for improving the performance of the SEE sector are summarized below. Rather than selecting a single option, a combination of options could be the best strategy going forward.

### *Asset Management Approach*

The broadest and possibly most ambitious approach to improving the SEE sector is to regard it as a subset of the government's total property assets (land and buildings, including natural resources) and create a government agency responsible for managing these assets. This approach is ambitious because it would require the creation of a large administrative body to inventory the assets, revalue them periodically, identify better uses, negotiate arrangements with potential users, and monitor performance under these arrangements. The great disadvantage of this option is the difficulty of creating and staffing an asset management agency. A first step might be to enact a founding law if sufficient authority does not already exist in the Ministry of Finance to undertake this function.

### *Budget Transparency Approach*

A basic public finance principle is that all revenues to and expenditures by any of a government's ministries (or agencies or affiliates or ventures) should be made transparent in the government budget. If all of the Myanmar government's revenues and expenditures were to become transparent, various political and social pressures would develop to reduce the deficits of individual SEEs and increase their revenues. This process alone could yield substantial improvements in the performance of the SEE sector in a relatively short period of time.

### *Legal Approach*

The State Law and Order Restoration Council (SLORC; 1988-97) regime promulgated a "State-Owned Economic Enterprises Law" in March 1989, just six months after it seized power. The law is short, mostly spelling out the twelve areas reserved for state-owned enterprises, and it is clearly inconsistent with the policies of the Thein Sein government. A new SEE law could be enacted to replace the 1989 law, although the need for such a law is not obvious. Furthermore, there is a risk that any law presented to the legislature will be

watered down or altered by special interests to the point of making the cure as bad as the disease.<sup>1</sup>

### *Turnaround Approach*

No precedent seems to exist for this approach.<sup>2</sup> It is prompted by the reality that the administrative capacity of the Myanmar government will remain low for at least the next five years and probably much longer. The turnaround approach flips the conventional approach to SEE sector reform on its head. Instead of beginning with an institution it begins with an individual. In short, the government would recruit a talented, experienced individual to be the CEO of a particular SEE and provide him or her with a mandate to “turn around” the SEE at the most rapid sustainable pace. It would not be sufficient to recruit an outstanding person. To make the approach succeed, it would be necessary for the government to provide unwavering support for the new CEO.

## **CONCLUSION**

Six actions by the Thein Sein government in the remaining months of its 5-year term could go a long way to improve the performance of the SEE sector: increase the transparency of SEE operations, proceed with the corporatization of viable SEEs, establish a dedicated SEE policy unit, recruit a couple of outstanding CEOs to turn around a couple of high-visibility mid-sized SEEs, and design a scheme for buying out redundant employees.

None of these actions, or a combination of them, will be easy to implement. Nor is the experience of other countries likely to be helpful. Decisions that would normally be informed by reliable information about the financial position of individual SEEs will, in the absence of this information, depend on the good judgment of policy makers. Moreover, even with superb judgment being exercised, the results will probably fall short of the unrealistic expectations that prevail both domestically and abroad. Success may come more quickly if expectations are lowered to match the ability of the government to implement sound policies.

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<sup>1</sup> Reports have recently surfaced that a “Corporatization Law” is being prepared.

<sup>2</sup> It is inspired by the case of Indonesia’s Garuda Airlines, which improved dramatically under a new CEO appointed in 2005.

## **Appendix A**

### **State Economic Enterprises at the beginning of 2015**

#### **Ministry of Agriculture and Irrigation**

- Myanma Livestocks And Fisheries Development Bank Ltd (1)
- Myanmar Agricultural Enterprise\*\*
- Myanmar Agricultural Development Bank\*\*\*

#### **Ministry of Border Affairs**

- Rural Development Affair Bank Ltd.

#### **Ministry of Construction**

- Public Works

#### **Ministry of Cooperatives**

- Cooperative Export and Import Enterprise

#### **Ministry of Communications and Information Technology**

- Myanma Posts and Telecommunications (2)

#### **Ministry of Electrical Power**

- Electricity Supply Enterprise
- Hydro Power Generation Enterprise
- Myanmar Electric Power Enterprise

#### **Ministry of Energy**

- Myanma Oil and Gas Enterprise
- Myanma Petrochemical Enterprise
- Myanma Petroleum Products Enterprise

#### **Ministry of Environmental Conservation and Forestry**

- Myanma Timber Enterprise

#### **Ministry of Finance**

- Myanma Economic Bank
- Myanma Microfinance Supervisory Enterprise (2)
- Myanma Foreign Trade Bank
- Myanma Investment and Commercial Bank
- Myanma Small Loans Enterprise

#### **Ministry of Hotel and Tourism**

- Myanma Hotel and Tourism Services

**Ministry of Industry**

- No. (1) Heavy Industries Enterprise
- No. (2) Heavy Industries Enterprise
- No. (3) Heavy Industries Enterprise
- Paper and Home Utilities Industries
- Pharmaceutical and Foodstuffs Industries
- Textile Industries

**Ministry of Information**

- Myanma Motion Picture Enterprise
- News and Periodicals Enterprise
- Printing and Publishing Enterprise

**Ministry of Labour, Employment and Social Security**

- Social Security Board

**Ministry of Livestock, Fisheries and Rural Development**

- Livestock Foodstuff and Milk Products Enterprise

**Ministry of Mining**

- Myanma Gems Enterprise
- Myanma Pearl Enterprise
- Myanma Salt and Marine Chemical Enterprise
- No (1) Mining Enterprise
- No (2) Mining Enterprise
- No (3) Mining Enterprise

**Ministry of Railways Transportation**

- Myanma Railways
- Road Transport

**Ministry of Transport**

- Inland Water Transport
- Myanma Airways
- Myanma Port Authority
- Myanma Shipyards\*\*\*\*

**Host Ministry Not Identified**

- Myanmar Citizens Bank LTD\*

## NOTES

Source: *Yangon Directory 2014*, except where noted.

- “Myanma” is a common variant of “Myanmar” which connotes possession (literally belonging to Myanmar).
- 44 enterprises under 17 ministries

\* Listed under Banks (Govt.).

\*\* From program for MDCF-3, Panel Session H on Rural Development and Poverty Reduction.

\*\*\* From World Bank. *Myanmar Agricultural Development Bank: Initial Assessment and Restructuring Options*. 2014. Reorganized from predecessor institutions under the MADB Law of 1990, which was amended by SLORC Law #3/1997 to move it from the Finance Ministry to the Ministry of Agriculture and Irrigation.

\*\*\*\* From *The Myanmar Times*. “Myanmar Shipyards Partners with Vietnam Company”. 9-15 February 2015, page 27.

(1) Listed under “Banks (Govt.)” but name was changed to Global Treasure Bank in 2013 or 2014. See *The Myanmar Times*, 13 May 2013. <http://www.mmmtimes.com/index.php/business/6733-bank-changes-name-aims-to-double-capital.html>(accessed 13 February 2015)

(2) Listed in *Myanmar Telephone Directory and Official Yellow Pages 2014* (competitor), but not in *Yangon Directory 2014*.

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