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ASEAN BRIEFING

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An Introduction to Doing Business in Myanmar

- **Setting Up a WFOE in China**
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About the Author

Alberto was born in Italy and educated in the UK where he spent five years obtaining a Bachelor Degree in Chinese, Economics and Management (Durham) and an MBA with specialization in Chinese law (Staffordshire). He has been a resident in China for over 14 years and speaks and writes fluent Mandarin, Italian, English and Spanish.

Alberto joined Dezan Shira & Associates as an equity partner in September 1998. From a few staff local firm in Shenzhen the company has now grown into a pan-Asia organization with over 200 professionals and 12 offices in China plus branches in India, Vietnam, and Singapore. Alberto directly oversees the four offices in Guangdong province (Guangzhou, Zhongshan, Shenzhen and Hong Kong), is responsible for the firm's overall development in China, Vietnam and Singapore, contributes regularly to the firm's publishing arm, Asia Briefing Ltd and is responsible for the technical editing of Vietnam Briefing. In 2006, the firm was appointed as the sole China member of the Leading Edge International Alliance (LEA) of global accountants and auditors. LEA is the 2nd largest tax and accounting partnership world-wide.

Alberto is currently the Vice Chairman of the European Union Chamber of Commerce in China – Pearl River Delta Chapter after having completed his three years mandate as Chairman. Under his tenure the Chamber trebled its membership base and revenues. In the past, Alberto also served for four years on the national Board of Directors of the China Italy Chamber of Commerce with responsibility for South China and he is a former Chairman of the British Chamber of Commerce, Guangdong - Shenzhen Sub Chamber.

In 2011, he was appointed International Advisor to the Guangzhou Government in recognition to his knowledge on FDIs in the region and his continuous help to make the city an even better place for foreign investments.

Alberto is experienced in corporate structuring, tax planning and legal and management issues affecting foreign-invested enterprises in China, Hong Kong and Vietnam and sits on various MNCs boards in China and Hong Kong.

Alberto has consistently contributed to the firm's Asia Briefing publishing house, which now publishes a variety of different titles in several languages. These include China Briefing, India Briefing, Vietnam Briefing and 2point6billion.com. Asia Briefing produces six different monthly magazines, and has published over 50 different books on matters of foreign direct investment legal and tax issues.

Since 2008 Alberto is also an elected member of YPO (Young President Organization), PRD Chapter in which he acts as Finance Chair.

Alberto's comments regularly appear in international publications such as The Financial Times, The South China Morning Post, Il Sole 24 Ore, China Daily and a host of other internationally recognized as well as local publications. He often delivers lectures at university and masters courses in prestigious universities in Europe.



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The land which time forgot is now open for business



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Myanmar's recent economic history

Myanmar is finally opening its doors to the rest of the world. A few months ago, the military-led government pushed political and economic reforms, attracting the attention of potential investors worldwide. The country was closed to the outside world and impoverished by embargoes and foreign sanctions until 2010, when the president of the new junta, Mr. Sein Thein, decided to cut with the past and gradually open the country to foreign capital and investors.

Myanmar's most recent economic history has gone through a roller coaster of highs and lows: during the 1950s, Myanmar was a prosperous trading hub linking the West with the rest of Asia and was an important stop for many intercontinental passenger and cargo flights from Europe going on to elsewhere in Asia and Australasia.

Its economy took a dive after the military coup in 1962 when the country's borders were literally sealed and its economic and political ties with the outside world abruptly severed. Local and foreign companies were nationalized in 1964 and, in the same year, study of the English language was cancelled from school curriculums and all classes.

After two decades of a centralized and controlled economy, 1988 brought the first signs of mild change with the adoption of a primitive market-oriented economy. Between 1988 and 2003, Myanmar underwent quiet but stable economic development and it seemed that the country would possibly alter its economy to follow in the footsteps of neighboring China and India.

Unfortunately, that did not happen, and the military lead government focused on protecting its own interests and those of its supporters in the main national industries, imposing a harsh regime and quickly eliminating any suspected dissidents.

A few months ago, the military-led government pushed political and economic reforms, attracting the attention of potential investors worldwide.

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The early years of the “Asian miracle” were among the darkest in Myanmar’s most recent economic history, as it ignored the laws of economics and closed its borders to the outside world. The United States and European Union imposed severe sanctions, which led to dramatic job loss. China, however, remained Myanmar’s “friend” – pouring money into the country through its search for natural resources while expanding its influence in the region. While it was obvious that China maintained its own agenda, money was flowing into the country with few questions asked and under only one condition: that all projects funded by Chinese money be assigned only to Chinese companies.

Perhaps it was the fear of becoming a modern-day colony of China, or maybe it was the realization that the country was being left behind as the rest of Southeast Asia thrives, but whatever the reason, Myanmar has now decided that it is time to open up its economy to the rest of the world. The task now lies in developing a country where over 70 percent of the population currently lives in the countryside, a quarter (or more than 15 million people) live below the poverty line, and almost two-thirds live without electricity.

What will happen in the future is unclear, but the current president, Thein Sein (who could step down in 2015), is an advocate of opening and reforming the economy, so it seems there is finally a light at the end of the tunnel. Apparently, the 67-year-old general’s relationship with Madame Aung San Suu Kyi (making headlines around the globe for her most recent political success following two decades of imprisonment and house arrest) is rather good and there is good chemistry in place, giving us reason to believe that the country will not regress back towards its old economic patterns. How to manage the relationship between the military and other parties will be of paramount importance and many stumbling blocks still lie ahead, including an article in the constitution stating that at least 25 percent of parliamentary seats must be assigned to the military.



The beautiful Shwedagon Pagoda in Yangon

In spite of the political struggles, things seem to be changing for the better in Myanmar. The most recent political elections show us that even a military regime cannot indefinitely silence increasingly louder cries for democracy. The National League for Democracy or NLD won 43 out of 44 contested seats during the election and even though this represents less than 10 percent of the 664 seats in parliament, the way this result was achieved remains remarkable. The true importance of the win is in the four seats that the NLD won in Nai Pyi Taw - the administrative and political capital of Myanmar and a stronghold of military technocrats.

Another important aspect of these elections is that they appear to have been performed in a clean and transparent manner, without anyone illicitly securing votes. Interestingly, in Myanmar, which is not a communist country, free press is legally accepted and censorship is virtually non-existent.

The winds of change are blowing and Madame Suu Kyi will have three years to prepare her party and herself for a high position in the future government. The current president is set to leave office in 2015, but whether the NLD is ready to lead the country remains to be seen. Having seen how the rest of ASEAN is developing, even the military has realized they need to change their ways to boost the economy and open Myanmar to the rest of the world.

Madame Suu Kyi advocates introducing the country to the rule of law, market reforms and democracy. She plans to eventually amend the constitution and has already brought in external industry advisors to ensure that change towards a more open economy can take place in the immediate future.

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Economy

The EU sanctions on Myanmar set an arms embargo and prohibited business in various sectors and with certain companies and individuals. On April 23 of this year, the EU lifted these trade sanctions, with the exception of the one on arms dealings, and is now encouraging member states to do business with Myanmar and to invest in the country.

The United States followed swiftly with President Obama's announcement on May 17 that the investment ban will be relaxed and that a U.S. ambassador to Myanmar will be named for the first time in 22 years. However, despite the announcement, U.S. firms are still prohibited from doing business with companies associated with the military-led regime. Furthermore, getting Myanmar-made products directly into the United States will still be virtually impossible (not to mention related international payments and settlements).

The Asia Development Bank projects Myanmar will grow 6 percent this year and 6.3 percent in 2013. The Economist Intelligence Unit reiterated those numbers in a recent announcement, suggesting that the economy will continue to open up and the government will not hinder such development.

Myanmar is already a WTO member and will have the ASEAN chairmanship in 2014-2015, just one year before the country's next elections. This will be a monumental chance for Myanmar to prove to the rest of the world that it is committed to changing for the better.

Ensuring this happens in an orderly fashion is in the country's best interest, given that it needs international organizations, such as the IMF and the World Bank, to come in and contribute project financing towards the country's much-needed infrastructure development. Positive signs emanating from the country will also spur on private foreign investors who are curious about Myanmar and its potential as an alternative to other Asian countries where costs are rising and many industrial sectors are starting to become unprofitable or over-saturated.

The big question is whether the government already has a clear and well thought out master plan for the country's overall development.

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Geographical and logistical advantage

Myanmar represents the second largest landmass in Southeast Asia and has the 40th largest population in the world. It neighbors five countries, India and Bangladesh in the Northwest, China and Laos in the Northeast and Thailand in the South. Its geographical location makes it the ASEAN link to China and India - the two largest, most dynamic and most rapidly developing emerging markets in the world. This combined with the ASEAN block, which contains over 600 million people, means Myanmar will have a bordering market of almost 3 billion people. Because of this, Myanmar is likely to compete with Vietnam as a preferred alternative to China and India-based manufacturing producers. At the moment, China offers the best and most efficient supply chain alternative for traders and manufacturers who rely heavily on mass-market, fast, and efficient subcontracting facilities – though not the cheapest. The price of efficiency and reliability is high and industries whose labor costs are a significant component of the overall product cost have to look elsewhere, such as Cambodia, Vietnam, Bangladesh, and India – which have all been viable options for some years now.

After infrastructure development takes place, Myanmar will also be a solid option for those in need of inexpensive manufacturing services. Furthermore, with its borders now open, it will serve as a more convenient transportation route between China and the Middle East, allowing goods to travel directly over land rather than having to circumnavigate the Malaysian Peninsula and Singapore.

Myanmar also has the potential to become a massive base for manufacturing end-products that require raw materials, such as textiles and fabrics, from either India or China. This is something that is already happening, albeit at a small scale, in many industrial parks around Yangon.

Myanmar could also play an important role in the future economic development of Thailand, which is currently Myanmar's largest trading partner and accounts for 40 percent of Thailand's exports. Thailand, like most Asian countries, is dealing with a series of rising costs. Discussions about Thai businesses eventually relocating to Myanmar have already been taking place. In fact, in order to lower some of the production costs following a recent 40 percent raise of the daily minimum wage to 300 baht (almost US\$10), companies have no choice but to move inland or to less expensive countries. Cost pressures combined with a possible shortage of laborers, should the hundreds of thousands of immigrants from Myanmar decide to return home, will likely have a negative impact on prominent Thai industries.



A typical production line of a local garment factory in the outskirts of Yangon

Furthermore, with Myanmar's huge variety of flora and fauna, 300+ islands (the majority still unspoiled), and snow-capped mountains, it has massive potential as a tourist destination within Asia. There are daily flights into Yangon from Bangkok, Kuala Lumpur and Singapore. Flights are also available from China - mostly from Guangzhou and Beijing (with a stop-over in Kunming). Beginning in October, there will also be a direct Dragon Air flight from Hong Kong to Yangon. Expect many more international carriers to open up passenger and cargo routes into the country in the months and years ahead.



Natural resources and imports of strategic goods

Myanmar is extremely rich in natural resources, both above and underground. At the top of the list, we find natural gas (over US\$3 billion in sales last year and Asia's largest natural reserve), jade (US\$2.8 billion), rice, beans (US\$500 million), seafood, garments (US\$500 million), timber, rubber, corn, sesame, rubies (US\$300 million) and teak (the country has the largest teak forest in the world). Rare earths, different types of woods, zinc, tin, platinum, gold and precious gems are also important components of Myanmar's exports.

Despite its abundant resources, Myanmar's exports are still lagging behind its neighbors. In 2011, the total export value was around US\$6 billion, a drop in the ocean compared to Thailand's more than US\$150 billion worth of exports. However, the gap will likely be filled quickly given the current regulatory changes and the country's enormous potential. Myanmar has plenty of catching up to do, but its strategic location and abundance of natural resource will quickly push it up the rankings of export countries in the region. For example, the country exports US\$300 million worth of goods in the fisheries and seafood sector - a small amount when compared to the over US\$3 billion worth of similar exports from Vietnam.

Many imports, such as raw materials or semi-finished goods, are instrumental in the local production process of exports given that Myanmar does not currently have or produce certain items like fabrics, petroleum, gasoline, machinery and spare parts, iron and steel.

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Real estate

Foreigners cannot directly own property in Myanmar. Nominee structures with trust arrangements can be used, like in many other Asian countries, to hold assets in the name of foreign owners. This involves having faith in the local government and hoping that it will not eventually nationalize and re-possess the assets as before. Discussions have been held about allowing foreigners to own apartments (only) under their own names and a law regarding this is being drafted. This will put Myanmar on the same level with other countries in Southeast Asia that allow foreign ownership of selected apartment complexes.

Lease restrictions have been eased and now foreigners can rent directly from private owners or from the State. Leases normally last 30 years with two further extensions allowed of 15 years each.

Typical of developing countries, luxury developments are flanked by slums and shoddy huts where people still live as if time stopped a few decades ago (almost two-thirds of locals still live without electricity). Some of the top real estate developments in Vietnam, Laos, and Cambodia have managed to spur development in the areas surrounding their luxury complexes.

High standard apartments and expansive estates are on sale for about US\$1,500 per square meter, with villas starting at over US\$2,000 per square meter. While this is nothing compared to prices in Hong Kong or Singapore, it is already out of reach for the majority of Myanmar's population.



One of the many beautiful old buildings along the streets of downtown Yangon. An ideal spot for a luxury hotel?

Sim Cards in Myanmar

Only a few years ago, the cost for a mobile phone sim card ranged between US\$1,500 and US\$4,500. In spite of the extreme price, it was (and still is) a hot commodity. At the moment, the going rate for a sim card for locals is still very high at US\$250-300, but there are plenty of local customers and the demand is growing rapidly. Foreigners can use a pre-paid sim card valid for one month for US\$20 (GSM phones). There are still no roaming networks in the country so your usual mobile number will not work.

Good hotels are a scarce commodity in the country, which does not come as a surprise considering hotel construction stopped over 10 years ago. According to local statistics, there are over 8,000 rooms in the country but less than 2,000 are considered suitable for hosting foreigners. Given the scarcity of supply and the overnight rise in demand, room rates have gone through the roof and are currently around US\$200 per night for foreigner-friendly 4 and 5 star establishments.

Knowing that airlines are looking to establish direct flights to Myanmar and the fact that tourism increased by 26 percent last year, the hotel, management, catering, and staff-training sectors are looking to embrace this opportunity for growth. Without a doubt, investments into China, India and other ASEAN countries have a quicker and higher return on capital at the moment, but looking at the near future, it is clear that Myanmar could be a potential gold mine.

The property law of Myanmar is based on common law. Land-use rights are valid for up to 60 years and can be renewed up to 80 or 100 years. Freehold properties are extremely rare and sell at a premium. As previously addressed, foreigners cannot own land directly. Furthermore, unlike local companies, foreign companies cannot receive financing or set mortgages with local banks.

House of Jade

Myanmar sells almost US\$3 billion worth of jade every year. This business is in the hands of a few well-connected families and traders. Given the economic sanctions and the difficulty of converting foreign currency, let alone transferring money overseas, these wealthy families could not do much with their growing cash-profits. Real estate investments seemed to be the most viable solution, which led to a sharp increase in property prices around the central lakes and downtown Yangon. They have already reached western-level prices if not skyrocketed even higher.

Interestingly, and maybe not surprisingly, Chinese buyers massively contribute to the purchases of jade. With gold or cash investments under more and more scrutiny and control by the authorities in China, the “green gold” is becoming a very useful commodity as a gift, wealth reserve, security and well-accepted “hidden” investment.



One of the many private villas bordering Yangon's busy central streets

Stock market

Myanmar has had a stock exchange (called the Myanmar Stock Exchange or MSE) since 1993. It is a joint venture between the Myanmar State Bank and Daiwa Securities of Japan. It is not an active stock exchange as only two companies are traded on it and only 10 transactions have been made since when they were "listed!"

High stamp duties, administrative issues, massive differences between official rates and unofficial rates, and a lack of records and laws to facilitate listings have been enormous obstacles to overcome.

With the country opening up, the need to have a functioning stock exchange is of paramount importance. The date set for the "new beginning" of the Myanmar Stock Exchange is 2015 and a consortium of financial organizations from Korea, Japan and Singapore are already involved in the planning. Foreign investors in the financial sectors could benefit by this opening up and are now sitting on the fence looking at what opportunities and restrictions the new investment law will bring.

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Infrastructure

The geographical advantage of the country cannot be fully exploited if roads, highways, railways, ports and airports are not there to support its industrial development. Virtually every sector - roads, schools, industrial zones, hospitals, water treatment plants, and power generators - will require foreign investment to enable Myanmar to play a small, but evolving, role in the Asian (and eventually global) supply chain. Local companies are unable to do this on their own as they need funding and the government simply does not have the capital required to finance such projects. Once larger international financial organizations start to finance projects and companies in Myanmar, it will be easier to raise capital for smaller, but equally important, projects in the services sector and other supporting industries.

The lack of a constant supply of electricity is of major concern. All companies in Myanmar must have their own generators as the power supply is unreliable and during many summer months the national grid only supplies energy for a few hours a day. Hotels face the same problem and blackouts occur frequently.

The cost of running a generator for a medium plant in one of the industrial zones in the outskirts of Yangon is only about US\$100 per hour (or 22 gallons per hour for an electric power generator).

Electricity, when available, is US\$0.12 / kwh while water costs 0.014 kyat per m³ (always referring to the same industrial zone outside Myanmar's economic capital).

As previously mentioned, mobile phones will not work since no roaming agreements exist between Myanmar and other nations. However, internet access is available in all major hotels. Myanmar's information technology, both cable or mobile, is probably the most outdated in Asia with the likely exception of North Korea. However, with a growing population and demand, the use of phones, internet and mobile devices is bound to grow exponentially.

Even the largest and richest investors could face problems

The mammoth Myitsone Dam Project, made with Chinese money on the Irrawaddy River, has been put suspended by the government until further notice. As one of the most controversial investments in Myanmar, the massive project started a few years ago under the assumption that 85 percent of the electricity generated would be sent back to China. It is unclear whether the supply allocation or discouraging news from feasibility studies and impact assessments were what disgruntled the government. After vociferous local protests, the government had to stop the project indefinitely. This is a clear indication that exploitation and scarce returns for the local community will no longer be tolerated in the country.

Currency

Myanmar has not been affected by the Asian Financial Crisis in the late 1990s and the more recent Global Financial Crisis which, at different times during the past two decades, have plagued its neighbors. In fact, because it is almost entirely a cash economy and has many restrictions against foreign banks and international lenders, Myanmar has been largely immune to these financial shocks that have negatively affected other emerging Asian economies.

However, with sanctions lifted and restrictions on international payments and transfers eased, Myanmar's financial isolation should come to a close by the end of next year, if not earlier.

From a fixed exchange rate, which lasted 35 years, the country moved to a managed float of the kyat introduced on April 1 with an exchange rate pegged to the U.S. dollar at 818/820 kyat to the dollar. Previously, there were different exchange rates depending on the note you were changing or which entity was doing the transaction.

Myanmar currently has five state-owned banks, 20 privately-held banks and 13 representative offices (including foreign banks). Foreign banks are not allowed to conduct any transactions in the country yet.

Myanmar will surely see an influx of foreign currency given the surging exports of its natural resources to new markets, which will strengthen the currency and the country's foreign reserves. The government will need to carefully manage this large influx of money in order to control inflation. A gradual and managed opening is necessary to ensure local small businesses are protected for a certain period of time against cheap imports from neighboring countries. There are already provisions within ASEAN and other international agreements to do so. This could also benefit current foreign investors as they will have a grace period in which their local production will be cocooned against the influx of competing overseas products.

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It is expected that the kyat will strengthen with the inflow of FDI. If the government manages this transition well, inflation should not be too great of a concern for the future (according to the Asian Development Bank, inflation slowed to 4.2 percent in 2011 from 7.3 percent in 2010). Having said that, we have seen how the situation can swiftly get out of control as it did recently in Vietnam. Therefore, a prudent approach is ideal in order to ensure the hard foreign currency continues to come in for viable and productive projects. With the stock exchange projected to open in 2015, which will result in a multi-fold increase of foreign capital, the government has a few years to prepare itself and ensure that the base of Myanmar's economy is sound and that the new wealth can be enjoyed by the largest percentage of its population as possible.

At the moment, international transactions are still a nightmare. It is impossible to send U.S. dollars from the United States to Myanmar without having the bank account frozen by the monetary authorities in the United States. Sanctions have limited, but not totally cancelled, trading activities with Myanmar companies and individuals. Due to currency restrictions in international trade, 90 percent of exporters in Myanmar have opened Singaporean companies in order to conduct international transactions.

Myanmar is a cash-based society. Credit cards are popular in most high-end hotels, but are not widely used and attract a 6 percent transaction fee on top of the original amount to be paid.

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A “love-hate” relationship with China

It appears that Myanmar, in spite of its love-hate relationship with China, is increasingly looking at the Middle Kingdom to learn how, in less than 30 years, it moved from a closed, agricultural-based society to overtaking Japan as the second largest economy in the world. Myanmar could emulate China in planning, developing and managing a market economy with “Myanmar characteristics.” This is certainly more appealing than the “Russian model” involving a brutal and complete opening of perestroika which put the country’s economy through a couple of roller coaster decades. Myanmar’s late arrival on the international stage gives the country the opportunity to analyze which economic model works best and how to apply some of the most successful concepts to its own economy.

The Chinese border is “only” 1,300 kilometers away from Yangon and Myanmar could be considered the “western exit” for China’s three southern provinces of Yunnan, Sichuan and Guizhou. China is continuously seeking access to natural resources and new markets. Furthermore, Myanmar’s imports from China are increasing exponentially. This corridor will likely turn into a busy entry-exit hall for China, the rest of Asia, and the Middle East. In this regard, Kunming could play a strategic part as a logistical center between China and the western hemisphere. A pipeline to transport natural gas from Myanmar into China will soon be operational, making the current round trip between the Bay of Bengal and the Thai Gulf a thing of the past, and there are also talks about a potential railway linking Yangon, Nai Pyi Taw and Kunming. China is also investing in the deep port of Kyauk Phyu, located next to the proposed pipeline in order to build a logistical base for petroleum and other commodities directly imported from the Middle East.

Myanmar could emulate China in planning, developing and managing a market economy with “Myanmar characteristics.”

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Labor cost and salaries

Myanmar has a population of over 60 million, with 70 percent being of working age. Some 45 percent of the population is under the age of 40 and the literacy rate is at 90 percent. The country could become an alternative to Asia's increasingly expensive manufacturing centers like China, where labor costs at operator and junior management levels are set to rise by at least 15 percent to 20 percent a year over the next five years.

Myanmar has plenty of laborers available and over the long term this may give it an edge over Cambodia (15 million people) and land-locked Laos (just over 6 million people). Bangladesh (almost 160 million people) may compete to attract investors in the more traditional low-end industries like textiles, garments and shoes as it has a much larger population and an abundance of natural resources, however it does not border directly with China.

Massive investments are still required in professional training and education, but Myanmar can count on a hardworking, fast-learning and young population. English was removed from curriculums years ago, but is now being re-introduced at all levels. Myanmar can also count on hundreds of thousands of its citizens who left the country during the dark years of the repression and are now in managerial positions across industries in Singapore, Thailand, Australia, the United States and the United Kingdom. All have a great desire to come back and join some of the family businesses and be part of the unprecedented economic boom that the country is about to experience. The financial crisis, job losses and insecurity in the West are also incentives for Myanmar's expatriates to return home.

Another important point is that Myanmar has never been under communist rule or had over-regulated HR frameworks and protection, which means workers are more likely to be creative, motivated, have a proactive attitude in the workplace, and the ability to manage the workforce themselves.

The cost of labor is among the lowest, if not the lowest, in Asia. The average salary is US\$70-80 per month for operators, and this goes up to US\$100-120 once you add insurance and overtime. Social security allocation is 4 percent of the salary - with employers contributing 2.5 percent and individuals contributing 1.5 percent. Workers tend to be loyal and obedient. In many cases the labor supply comes from neighboring villages so there is no need to build dormitories for most workers. Instead, many companies arrange for buses to pick up workers at pre-defined collection points.

Massive investments are still required in professional training and education, but Myanmar can count on a hardworking, fast-learning and young population.

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Wage Overheads in Emerging Asia

Country	Avg. minimum annual salary (worker, intl. dollar)	Avg. mandatory welfare (% against salary)	Total labor cost (intl. dollar)
Bangladesh	798	n/a	798
Cambodia	672	n/a	672
China	1,500	50	2,250
India	857	10	943
Indonesia	1,027	6	1,089
Laos	1,057	9.5	1,157
Malaysia	4,735	23	5,824
Mongolia	2,004	n/a	2,004
Myanmar	401	n/a	401
Nepal	1,889	n/a	1,889
Pakistan	984	7	1,052
Philippines	2,053	9.4	2,246
Sri Lanka	1,619	n/a	1,619
Thailand	2,293	6.9	2,451
Vietnam	1,002	15	1,152

Source: IMF World Economic Outlook Database, October 2010

Foreign direct investment in the country

Myanmar is set to be the new “darling” of foreign investors, following the sudden but relentless pace at which the country is opening its doors and the frenzy it has stirred up in the international media. Both economic and political openings are making headlines across the globe, luring potential investors. In 2010 and 2011, total FDI into the country already totaled US\$20 billion, which is not bad for a virtually closed economy. At the top of the FDI list is China (which has invested US\$20 billion since the 1980s), Thailand, Hong Kong, Korea, the UK and Singapore. Not surprisingly, all are Asian countries with the exception of the UK.

Almost two-thirds of FDI has been concentrated in the oil, gas, power and mining sectors involving some of the largest players in the respective industries. Chinese investors also have the lion’s share in other sectors, including low-end and low-margin production activities, mainly for export back to China or elsewhere in Asia.

There are also a large number of local companies involved in low-end manufacturing on behalf of foreign brands that use Myanmar as a base for processing ventures to sell into non-restricted countries around the world. At the moment, given the softened economic sanctions, the same international companies are already starting to re-direct such exports to the European Union and, later on, to the United States. The new foreign investment law, which aims to level the playing field between local and foreign companies doing business in the country, will also attract a large number of potential investors.

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Forms of investment, tax incentives and restrictions

Myanmar's 1988 Foreign Investment Law (FIL) allows 100 percent foreign-owned enterprises to establish themselves in the country. The foreign investor can invest as an entity or as an individual. Joint ventures are also possible with the only limitation being 35 percent minimum foreign ownership.

A partner is still required for strategic sectors but during these early stages and in such an obscure business environment, having a partner might actually be advisable and recommended for newcomers without the time and resources to deal with the current cumbersome and bureaucratic maze of laws, permits and regulations.

The trading sector is officially still off-limits to foreign investors but FIEs involved in manufacturing can export self-manufactured products. Interestingly, foreign investors who decide to set up in Myanmar can either follow the FIL or simply register with the approval authorities. The FIL also allows for business cooperation contracts (BCCs), similar in principle and execution to the legal tools available in Vietnam. Representative offices are also allowed in the country.

According to the FIL, the minimum registered capital for a manufacturing company is set at US\$500,000 and US\$300,000 for a service company. If a foreign investor chooses to go directly to the company registration office then the capital threshold could be as low as US\$50,000 for a service company.

The time it takes to register an entity in the country has been substantially reduced from 8-9 months to 3-4 months. Still, bureaucracy remains an issue due to the lack of efficiency and, in most cases, knowledge about how to deal with registrations.

Separate laws recently promulgated in 2011 are applicable in special economic zones (SEZs) located in Dawei (southern Myanmar, bordering Thailand), Thilawa (near Yangon) and Kyauk Phyu (facing the Bay of Bengal) and offer additional advantages to those companies in export manufacturing.

Withholding 3.5 percent to 20 percent of tax is possible with certain offshore payments or business conducted by entities without a permanent establishment in the country. At the moment, it is not possible to withhold tax on dividends.

The new Foreign Investment Law is expected to offer advantageous tax breaks to investors. The corporate income tax (CIT) rate in Myanmar is 25 percent, which is the same as China and Vietnam, however tax exemptions and breaks are much more generous for newly invested foreign companies in Myanmar:

- Total CIT exemption for the first five years
 - 50 percent reduction on the following five years (12.5 percent CIT effective rate)
 - 50 percent further CIT reduction if profits are reinvested in the country for the following five years
-

In most cases, especially for manufacturing activities conducted in the special economic zones (SEZs), raw materials and equipment used in the company's own production can be exempt of custom duties (CD) and value added tax (VAT) when imported. Other CD exemptions may be granted during the construction period and the following three years.

Myanmar used to levy a 10 percent export tax, but this has been removed.

The Myanmar Investment Commission may also grant additional incentives but these are now under revision given the promulgation of a new FIL.

Personal income tax is calculated on a progressive scale from 5 percent to 20 percent of income for Myanmar tax residents.

There are still labor restrictions on hiring foreigners: at least 25 percent of employees must be local residents during the first five years, 50 percent during the second five years, and 75 percent during the third five years. The message is clear: if you want to come to Myanmar to do business you must employ local staff.

The new FIL allows private companies to rent factories and industrial land to foreigners for 50 years with a possible extension of 10 years, followed by another possible 10 year extension for a total of 70 years. Further extensions may be possible especially in distressed areas. Rental fees are very cheap in Myanmar. Recently obtained, but unconfirmed, figures indicate a range of between US\$2 to US\$4 per square meter per year. Lease contracts require a stamp duty, which can be as high as 7 percent.

Bank transactions are still problematic. Even though foreign companies can now execute forex payments within Myanmar and overseas, remitting foreign currency abroad still requires approval, so attention to detail is a must. Some local transactions are required to be done in forex and the local kyat cannot be used. Lending from local banks to FIEs is not yet possible.

There are no IPR rules or trademark laws in Myanmar yet. A trademark can be registered with local authorities but there is not yet a trademark protection law. Normally, authorities show benevolence to foreigners who register their trademarks in Myanmar and need to stop a local counterfeiter, however there is no guarantee that a trademark will be protected as it would be in the West.

Personal income tax is calculated on a progressive scale from 5 percent to 20 percent of income for Myanmar tax residents.

Investment opportunities

Earlier, we mentioned the many opportunities for foreign investors in the financial, infrastructure and tourism sectors. With the opening of the country, there will be plenty of opportunities across various other sectors as well. Here we provide a brief summary of the most promising ones.

Natural resources, their identification, extraction, and processing, as well as their upstream and downstream supply chains and all related industries are secure and strong as there will be plenty of demand both locally and internationally, with China and India leading the pack.

Investment in language training and education is urgently needed. English education will find stable ground in Myanmar due to the suspension of English classes back in the late 1960s and the rising need for English-speaking personnel to sustain both export oriented companies as well as new government posts.

Vocational, technical and professional training and coaching are good sectors in which to invest. Medical, educational and industrial establishments will absorb all new recruits as demand far outstrips the current supply. At the moment, it is not unusual to find middle and senior management from China, Thailand and other neighboring countries running factories in the country due to the lack of locally-developed talent.

Local retail is another sector with potential, both at the low-cost mass market level and at the top-end with all of the additional services along the supply chain in between.

With a population over 60 million, there is of course plenty of need for food and beverages in the country and at the moment this market is monopolized by local companies or Chinese investment. Myanmar's annual per capita income in 2011 was only US\$900, but is expected to reach India's US\$1,200 and Vietnam's US\$1,500 per capita income levels in the next few years. Thailand's (US\$5,000 per capita income) and China's (US\$5,300 per capita income) growing middle classes can also be tapped into from Myanmar.

Investment in language training and education is urgently needed. English education will find stable ground in Myanmar due to the suspension of English classes back in the late 1960s.

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Myanmar is part of ASEAN, and has favorable trading terms with all of its ASEAN neighbors as well as with China and India. The country's top earners are a minority and will likely continue shipping luxury and daily items from overseas, particularly from Singapore.

There will be a massive need for logistics, storage, packaging and freight forwarding activities to ensure goods are moved in and out of the country efficiently, rapidly and in good condition.

The telecommunications sector will boom in the years ahead. We have already seen that sim cards are selling well in the country and the need for cheaper mobiles and general electronics (likely to be imported from China and Vietnam) are bound to increase.

Manufacturing will be interesting for export-oriented, low end manufacturing enterprises who either source local products (fish, rubber, wood and other commodities) for processing and export or for those involved in vertical production using raw materials and inputs from China or India to be further assembled or processed for overseas markets. In this regard, logistics will play an important role as the cross-border flow of goods will have to be properly planned in order to avoid production downturns.

In particular, U.S. sourcing of textiles and accessories, which effectively stopped in 2003 with the embargo, could receive a massive boost later on in the year given the rising cost of manufacturing in both China and Vietnam.

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What could go wrong?

When you talk to local people as well as to government officials, you always hear the same mantra: “Myanmar is open, come to invest and you will not regret it. However, be extremely careful, as things could go horribly wrong.”

This could be a piece of advice readily applicable to all Southeast Asian countries, but in Myanmar it has added weight. While there is much hype about where the country is headed, there is no proven track record or any precedents to go by. The new government, for example, has shown great commitment to modernizing its laws, but at times it has also appeared weak and lacking of a clear agenda. Will it remain loyal to its commitment to democracy in the years ahead?

Figures, facts and feelings make me believe the country will not go back to its isolationism, but there are still risks for those coming to invest in Myanmar – at both the macro and microeconomic levels.

As in Vietnam, pressure on the currency and growing government debt following poor use of funds could occur and scare off new investors, hindering the country's economic development. Because the government lacks the necessary experience, inflation could become a serious problem, which could lead to social unrest and a resurgence of nationalistic and militaristic spirit. Social tensions might also erupt if not enough jobs are created in the short term. Unofficially, around 1 million jobs are necessary to secure stable economic development.

The government will also need to address concerns regarding the pockets of rebel forces still active in bordering areas, which, in spite of an apparent truce, may affect cross-border tourism and trade between Myanmar and its neighbors.

Corruption, ineffective rule of law, and a weak judiciary system could also dampen investors' motivations to commit to Myanmar.

Many believe Myanmar's current state of development parallels China 25 years ago and Vietnam 15 years ago. The immediate feeling when walking around the streets of Yangon is that the comparison is not far off, but the hope is that the new government will learn, at an even faster pace, what it takes to transform a white elephant into a new roaring economy.

When you talk to local people as well as to government officials, you always hear the same mantra: “Myanmar is open, come to invest and you will not regret it. However, be extremely careful, as things could go horribly wrong.”

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