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MYANMAR AWAKENS: UNEARTHING ASIA'S HIDDEN GEM

SPECIAL REPORT

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Introduction

Myanmar Awakens: Unearthing Asia's Hidden Gem

BMI View: After a number of false dawns, Myanmar's latest political and economic awakening appears to be the 'real deal' and – as with any 'new' investment story – foreign interest is likely to reach fever pitch in the coming years. We acknowledge the country's formidable long-term potential, albeit with the caveats that severe pitfalls are likely to persist and that there remains a scarcity of tangible assets in which to invest. As seen in other resource-rich frontier markets, we expect infrastructure, mining and oil & gas to dominate investor attention in the short term, whereas sectors such as financial services and telecoms look set to be more long-term plays (and still fraught with risk).

Having spent the best part of half a century in self-imposed isolation, Myanmar has started to show concrete signs of political and economic reform. Since the inauguration of ex-general Thein Sein as president of a nominally civilian government in March 2011, we have seen more than 6,000 political prisoners (including renowned opposition leader Aung San Suu Kyi) freed as part of a general amnesty, the passage of new labour laws allowing for unions, the easing of media restrictions, and a flurry of ceasefire agreements with minority rebel groups. The government's willingness to loosen its political grip has, in turn, been welcomed by the global community, culminating in an official visit by US Secretary of State Hillary Clinton in December 2011 – the first trip by the top American dignitary in more than 50 years. More importantly perhaps, Aung San Suu Kyi will be contesting by-elections on behalf of the opposition National League for Democracy (NLD) in April, and it is widely believed that a fair and transparent electoral process could pave the way for a relaxation of US and EU economic sanctions.

TABLE: MYANMAR POLITICAL TIMELINE

1948	Burma becomes an independent state.
1962	Caretaker government ousted in military coup led by Gen Ne Win.
1987	Currency devaluation triggers anti-government riots.
1989	Junta declares martial law, renames country Myanmar.
1990	Opposition National League for Democracy (NLD) wins landslide victory in general election, but result ignored by military.
1992	Than Shwe appointed prime minister. Several political prisoners freed in bid to improve international image.
1995	Aung San Suu Kyi is released from house arrest after six years.
1997	Myanmar admitted to ASEAN.
2004	Khin Nyunt is replaced as prime minister amid reports of a power struggle. He is placed under house arrest.
2007	Wave of public dissent sparked by fuel price hikes. Buddhist monks hold a series of anti-government demonstrations. Dozens of activists are arrested.
2008	Government publishes proposed new constitution, which allocates 1/4 seats to the military. Aung San Suu Kyi under house arrest once more. Cyclone Nargis hits; death toll estimated at 134,000.
2010	Main military-backed party, the Union Solidarity and Development Party (USDP), claims resounding victory in first election for 20 years. Opposition groups allege widespread fraud.
Mar-11	Thein Sein is sworn in as president of a nominally civilian government.
Sep-11	Government suspends construction of Chinese-funded Myitsone hydroelectric dam
Oct-11	Political prisoners freed as part of a general amnesty. New labour laws passed.
Nov-11	Pro-democracy leader Aung San Suu Kyi to stand for election to parliament.
Dec-11	US Secretary of State Hillary Clinton visits and holds talks with President Thein Sein. US offers to improve relations if democratic reforms continue.
	President Thein Sein signs law allowing peaceful demonstrations for the first time; NLD re-registers as a political party in advance of by-elections.
	Authorities agree truce deal with rebels of Shan ethnic group and orders military to stop operations against ethnic Kachin rebels.
Jan-12	Government signs ceasefire with rebels of Karen ethnic group.
Feb-12	Currency reform proposals outlined by central bank.
Apr-12	Key by-elections scheduled to take place.

Source: BMI

Have We Been Here Before?

We have seen a number of false dawns in Myanmar's political and economic development. In the early 1990s, for instance, there were similar concessions made by the ruling junta in terms of prisoner releases, which led to the country's membership of the Association of South-east Asian Nations (ASEAN). However, deep political divisions prevented a more meaningful transition at that time (see timeline). Clearly, we are mindful of history repeating itself – especially given the opaqueness of Myanmar's policymaking process. Nevertheless, **we believe that there is sufficient evidence to point to a sustained pace of reform in the coming years**. First, it is understood that the key powerbrokers in the 11-member National Defence and Security Council, led by Thein Sein himself, are reform-minded – a major change from the tenure of former head of state Than Shwe. Second, there is the issue of self-preservation. The ruling elite is concerned about a potential 'Arab Spring' scenario, having seen a number of authoritarian governments toppled in the Middle East, and tentative liberalisation may be seen as the path of least resistance. Finally, Naypyidaw appears to be worried about its growing over-reliance on China, which is one of Myanmar's largest external benefactors and creditors. Thus, boosting relations with the US, the EU and India could provide a useful counterweight to Chinese influence, and a more diversified external economic base. Given our predictions of a 'hard landing' in China, such a strategy appears astute.

Is Myanmar Worth A Punt?

In a word, yes. As a general rule of thumb, **BMI** rates the potential of an emerging market based on the following criteria: rich endowment of natural resources; strong demographics with growing consumer potential; low leverage and a well-capitalised banking system; market-friendly policy commitment with healthy public finances; and a stable net international investment position (typically we are optimistic if at least three of these five conditions are met). Judged against this checklist, Myanmar's scorecard looks pretty favourable in the context of recent reforms.

Resources: Myanmar is endowed with vast natural resources, including oil and gas reserves, minerals, gems, timber, agricultural land, fisheries and wind and renewable energy. The country produces 60% of the world's teak, and accounts for 90% of global jade and ruby output. Moreover, according to Thailand's **PTT Exploration and Production** (a major investor in the country), Myanmar's proven reserves for natural gas and crude oil stand at a respectable 26.8 years and 11.7 years respectively.

Location, Location, Location
Dawei Port Project In Myanmar

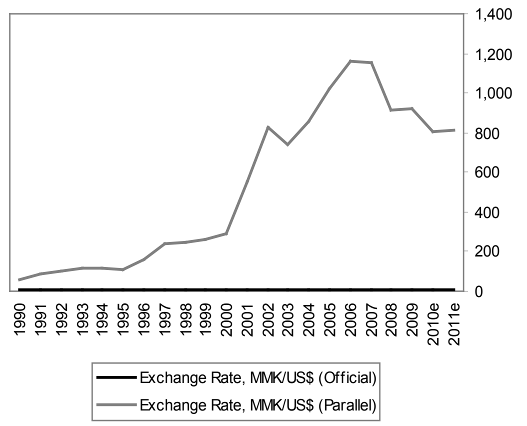
Source: BMI

Geography: Myanmar's strategic location is important from both an economic and a political standpoint. The country shares borders with Bangladesh, India, China, Laos and Thailand. Not only is it the largest (and least explored) landmass in South East Asia but it also enjoys a coastline of 2,000km with deep sea ports.

Demographics: According to our estimates, Myanmar's population is roughly 62.5mn, and is expected to grow at a healthy clip of 2% per annum over the next decade. It is also a young demographic, with a median age of 28 years. Roughly 70% of the population is in the 16-64 years age bracket, a dynamic that is forecast to remain stable through to 2040. Despite chronic underinvestment in education, the country's literacy rate stands at a high 90%. This is a major plus point given that average wages remain extremely low at approximately US$50 per month.

Leverage: Myanmar is severely under-banked, with only 2% of the population holding bank accounts. Clearly, this 'ticks' our low leverage category, although of greater concern would be the ability of the country's financial system to absorb a surge in foreign capital without stoking inflation (more on this later).

Parallel Universe
Myanmar - Official & Unofficial Exchange Rates, MMK/US$



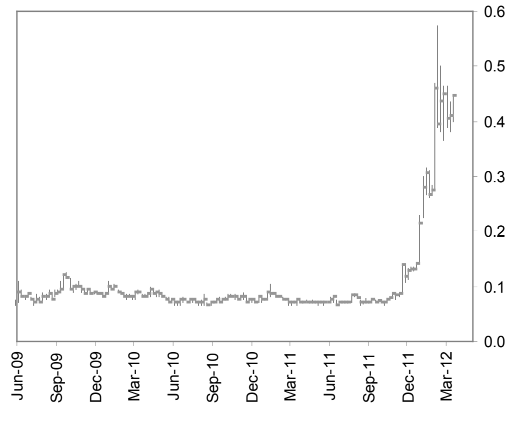
Source: BMI, IMF

Wary Of Hyperbole

As with any 'new' investment story, we expect foreign interest in the country to reach fever pitch in the coming years. Indonesia's post-Suharto resurgence, Vietnam's integration into the global economy and Sri Lanka's post-civil war recovery potential have all been past investment favourites, with the latter two witnessing huge stock market bubbles – and subsequent crashes. Ominously, we have seen anecdotal reports that new condominium prices in affluent areas of Yangon are spiking to US$2,500 per square foot – more expensive than some areas of Bangkok – while land prices have reportedly tripled over the past six months.

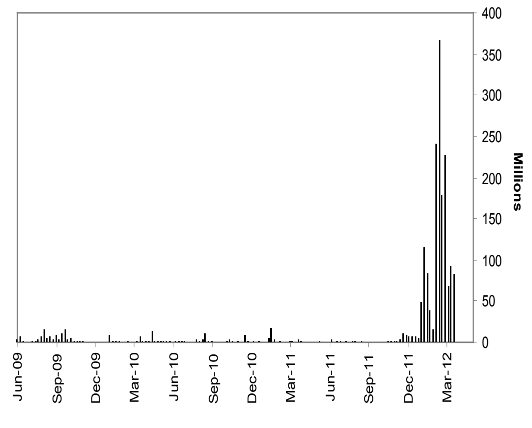
We expect to see a swathe of new investment – both good and bad – enter Myanmar in the coming years, all of which will have to contend with a still challenging business environment. Myanmar ranks a lowly 180th out of 182 globally in Transparency International's Corruption Perceptions Index. More troublingly perhaps, the country does not even feature in the World Bank's 'Doing Business' report (the World Bank and the Asian Development Bank ceased operations in the country in the mid-1980s and are still owed arrears, which have to be repaid before they return). Specifically, there are major risks from the huge discrepancy between the official and the black market exchange rates (although this is reportedly being addressed), the lack of a transparent legal framework, and the arbitrary and unpredictable fashion in which projects are awarded.

One Small Step For Myanmar, One Giant Leap For Yoma
Yoma Strategic Holdings, SGD



Source: BMI

Daily Volume, Number Of Shares



Source: BMI

For equity investors, there is also the question of market access. Myanmar has a securities exchange effectively in name only. Established 15 years ago, it has attracted just two companies to list. Even if we were to see a wave of initial public offerings in the months ahead, it would take years before the market offered sufficient liquidity to entice an international audience.

Two names that do provide exposure to Myanmar are Singapore's **Yoma Strategic Holdings** and Thailand's **Italian-Thai Development**. The former is heavily invested in Myanmar real estate (the country accounts for roughly 93% of total revenue), and its share price has surged since reforms commenced last year, up a whopping 540% from October 2011. Italian-Thai Development is the lead partner in the Dawei Maritime Hub Project; an US$8.6bn initiative to develop a deep-sea port, a resort complex and an industrial estate that includes a steel mill, an oil refinery, and a 4,000 megawatt (MW) coal-based power plant, as well as cross-border road, rail and pipeline links with neighbouring Thailand. From our perspective, both stocks are likely to remain volatile, and particularly vulnerable to political noise and the vagaries of government policy.

Where's The Action?

In terms of sector potential, **we believe that Myanmar is likely to follow the template of other resource-rich frontier markets, such as Mongolia and Kazakhstan, where investment is primarily channelled into the areas of commodity extraction and the infrastructure required to get production to market**. In this respect, we expect infrastructure, mining and oil & gas to dominate investor attention in the short term.

The aforementioned Dawei project is the central feature of our proprietary key project database for Myanmar. However, other initiatives, such as the Kyaukphyu-Kunming railway linking Myanmar to China, also offer promise (the first phase is to be carried out by the state-owned **China Railway Engineering Corporation**). Given that US sanctions remain in place, Asian majors will remain at the forefront of Myanmar's infrastructure development, with China, Thailand and, increasingly, India leading the field. Indeed, an agreement with New Delhi to construct a US$3bn hydropower plant in Ta-

TABLE: BMI KEY PROJECT DATABASE FOR MYANMAR

Project Name	Companies	Timeframe
Coal-based power plants (3x 130MW, 6x 600MW)	Italian Thai Development (ITD), Ratchaburi Electricity Generating Holding, Dawei Development	2012–2020
Kyaukpyu-Kunming railroad	na	2012-2015
RCC embankment and Yeywa hydropower plant, Mandalay region	CGGC International Sinohydro	2010
First Road Construction Project: part of the 1079km Stilwell Road	Yunnan Construction Engineering Group, Yuzana Group	2011-
Shwezaye hydropower project, Chindwin River	National Hydroelectric Power Corporation (NHPC)	August 2011-
Tamanthi hydropower plant, Chindwin river	National Hydroelectric Power Corporation (NHPC)	2011-
Ruili-Muse-Kyaukphyu railway line (part of Kyaukphyu-Kunming railroad)	China Railways Engineering Corporation	2011-
First-ever liver transplant hospital	Changi General Hospital of Singapore	June 2011 -
Htamanthi hydropower project, Chindwin River	National Hydroelectric Power Corporation (NHPC)	August 2011 -
Myanmar-China Myitsone Hydro-Electric Project, Irrawaddy River, Kachin state	China Power Investment Corporation (CPI), China Gezhouba Group	September 2011–2019
Deep-sea port, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development	2012–2015
Cross-border road link (Dawei, Myanmar to Pu Nam Ron, Kanchanaburi, Thailand)	Italian Thai Development (ITD), Dawei Development	2010–2012
Cross-border railway link (Dawei, Myanmar to Pu Nam Ron, Kanchanaburi, Thailand)	Italian Thai Development (ITD), Dawei Development, Japanese and Chinese investors	2012–2020
Coal-based power plants, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development, PTT	2012–2020
Petrochemical refineries, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development, PTT	2012–2020
Steel smelting plant, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development, Japanese investor	2012–2020
Fertliser plant, part of maritime hub project	Italian Thai Development (ITD), Dawei Development	2012–2020
Township for residential and commercial development, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development	2012–2020
Tourism, resort and recreation complex, part of Dawei maritime hub project	Italian Thai Development (ITD), Dawei Development	2012–2020
Urban railway system (elevated and underground tracks), Yangon	na	February 2012 -

As of March 14 2011. Source: BMI

manthi was signed in 2011. **BMI**'s commodities team, meanwhile, recognises that Myanmar has the potential to become a major player in copper production (see 'Chapter on Mining) . The country's Monywa copper mine, if fully developed, would have a potential annual production capacity of 200kt (thousand tonnes) of copper, making it one of Asia's largest. Finally, in terms of its oil and gas outlook, Asian and Russian firms (such as Thailand's PTT Exploration and Production, Malaysia's **Petronas**, and Russia's **CIS Nobel Oil Company**) have recently been awarded exploration rights for onshore development. Significant energy potential and close proximity to the demand centres of China and India suggest that competition for additional acreage will be fierce.

On the down side, **we do not believe that Myanmar will provide a particularly attractive consumer story for quite some time**. Firstly, even if we were to assume that US dollar incomes grew at a healthy clip of 15% per annum, GDP per capita would only reach roughly US$2,750 by 2020. Secondly, the creation of an effective regulatory and legal framework will not take place overnight.

Such a backdrop is crucial for telecoms to thrive, for instance. Anecdotal evidence suggests that a mobile SIM card costs US$400, which is far beyond the affordability of the average Burmese consumer (unsurprisingly, the International Telecommunication Union reported an estimated mobile penetration rate of just 1.24% as of end-2010). Even if demand for value-added services were to pick up, a lack of clarity on how spectrum would be auctioned and distributed could be a serious sticking point. Such issues have already caused problems for foreign operators in other Asian emerging and frontier markets, such as Bangladesh and even India. As such, while we believe that companies will still jockey for first mover advantage (**Beijing Xinwei Telecom Technology Company** signed an agreement with **Myanmar Link Global Company** in early November 2011 to expand broadband coverage), we would expect return on investment to remain relatively muted in the short to medium term.

Financial services, too, remain much more of a long-term play, despite reports that UK bank **Standard Chartered** would be keen to re-enter Myanmar should EU sanctions ease. As noted earlier, the country is severely underbanked, which could lead to opportunities for rapid growth. However, there are a number of factors that convince us to hold a much more conservative stance. Firstly, we believe that preference will be given to local banks – particularly those connected to the government, which remains by far the largest consumer of credit. Secondly, much will depend on the success with which currency reforms are implemented. Thirdly, there is a chronic shortage of skilled labour required for financial services to proliferate. With these factors in mind, Myanmar's banking sector is not an investment opportunity for the faint-hearted, in our view.

Political Outlook

Sifting For Clues As Reforms Roll On

BMI View: Myanmar's civilian government is moving forward with dramatic political, military, and economic reforms at an impressive rate. We believe that the pace of reforms can continue as long as the regime's goals remain aligned with those of the international community and Myanmar grows increasingly wary of neighbouring China's growing leverage. Still, with the military-backed Union Solidarity and Development Party (USDP) likely to retain its stranglehold on the country's political system for years to come, we caution that progress towards full democracy is far from assured.

Given the lack of change in what has been one of the world's most reclusive states for more than half a century, the reform drive in Myanmar has advanced at an astounding rate. The ruling Union Solidarity and Development Party (USDP) has identified three key areas in which reforms are most necessary, or, more cynically, most likely to earn significant plaudits from the international community. These include the military, political, and economic spheres.

The USDP is particularly concerned with appealing to Western demands that its immediate predecessor, the former State Peace and Development Council, soundly ignored. While the timing of this sudden shift in behaviour remains a mystery, the intentions are clear. Myanmar is now willing to take drastic steps towards re-integration with the international community in exchange for the removal of the crippling economic sanctions imposed by the US and EU.

Promise On The Political Front

As long as the government can maintain its current pace of reform, such an outcome is increasingly likely, perhaps as early as mid-2012. The regime will need to show continued progress in each of the three aforementioned spheres, the most crucial of is political liberalisation. Since key opposition leader Aung San Suu Kyi was freed from house arrest in November 2010, the government has allowed her increased licence to both openly criticise the authorities and campaign for reforms.

This is a key development in the sense that Suu Kyi is the most internationally celebrated political figure within the country. It has been said that Suu Kyi is the gatekeeper to the West's release of sanctions, and in the realization of this the government has begun a historic shift in its policy towards her involvement in the country's politics. Suu Kyi's National League for Democracy party (NLD) is slated to run in by-elections scheduled for April 1, and her accession to parliament, an achievement considered impossible little more than a year ago, is increasingly likely.

The USDP will also be expected to continue granting amnesty to political prisoners. Following its most recent release of approximately 200 detainees in January, the US rewarded the move by immediately upgrading relations with Myanmar by agreeing to exchange ambassadors for the first time in over two decades.

Peace With Rebels Another Positive Step

On the military front, the USDP has recently sought détente with the numerous rebel groups with which it has been warring for decades. In 2004, the (KNU), the largest rebel group in the country, negotiated a partial ceasefire with the State Peace and Development Council (SPDC), only to find that the SPDC used the agreement as an opportunity to fortify its front line. However, the government on January 22 2012 struck a new peace accord with the KNU, and this time the outcome should be different, because more is at stake for the regime.

Will Reforms Hold Up?

Though implicitly backed by the military, whose representatives hold a mandated 25% of the seats in the country's parliament, the USDP appears to be genuinely seeking reform. While the reasons behind the party's sudden turn of face are nearly inscrutable, they are likely a combination of social, political, and economic factors. The four main reasons why we believe reforms will continue are as follows:

- The regime may be finding that its increasing reliance on China for both economic and political support is untenable in the long run. China surpassed Thailand as Myanmar's largest foreign direct investor in 2010-11, pledging in excess of US$15bn worth of new projects.

- Following a year of unprecedented social unrest across the Middle East, with several long-standing authoritarian regimes toppling, Naypyidaw may be looking to avoid a similar fate sometime in the future.

- Myanmar's elites (generals, former military leaders, and business cronies) have aligned their economic interests with the lifting of sanctions.

- The US' interests, too, are aligned with bringing Myanmar in from the cold.

Given Myanmar's record of violently quashing social uprisings in 1988 and 2007, we believe the primary impetus for recent change has been driven by the China factor. On this point, the USDP likely feels that its terms of trade with China will only worsen as the rising giant gains progressively more leverage over the pariah state. Furthermore, in an historical context, given the two countries' long-standing and often inimical relationship, Myanmar does not wish to become a Chinese client state. As such, it is now looking west, with the added incentive that a sustained thaw in relations with the US and EU may enrich the country's elite, which now owns the vast majority of Myanmar's wealth as a result of a massive privatisation drive that took place in the run-up to the 2010 general elections.

Economic Reforms Still In Infancy

Although the elite has in the past found ways to play Western economic sanctions to its advantage, the privatisation of state assets has aligned its interests with the removal of those sanctions. We believe that this means the government, former generals, and their business associates will now push forward with much stronger conviction than in past periods of 'appeasement' in order to have sanctions lifted.

In preparation for the opening of the economy, the government has been working with the IMF, World Bank, and ADB (among others) to unify its dilapidated dual exchange-rate system. The floating of the kyat (and the acknowledgement by the government that the official rate is completely obsolete) will be an extremely important milestone in the early stages of economic reform in Myanmar, and reports indicate that the government will begin to take concrete steps towards this goal beginning in April. Further economic reforms including the relaxation of strict rules governing the ownership of Myanmar land by foreigners are also expected in short order, and the degree to which they are implemented will be a key determining factor of the country's potential.

A Word Of Caution

Cause for optimism is abundant in today's Myanmar, but we would be remiss to omit the considerable risks that remain. Particular caution should be given towards the country's business environment and investment landscape. Well-connected business tycoons such as Tay Za and Zaw Zaw still have a firm grip on virtually every major industry, and their ability to leverage the government's favour will not dissolve overnight. This means that considerable barriers to entry will exist for even the most experienced global firms. Furthermore, Myanmar's banking sector (as well as a solid regulatory framework) is practically non-existent and will require years, if not decades, of reform before it can function to the degree seen in neighbours like Thailand and Indonesia. Lastly, the military continues to hold all of the cards. Despite all of the talk of 'irreversible reforms,' history tells us that a rapid and unforeseen regression towards the previous status quo cannot be ruled out any time soon, especially if a schism develops between the government's reformers and hardliners. While it has been decades since the country's future has looked so bright, Myanmar's enormous economic promise is matched only by its substantial hazards.

Geopolitics

Myanmar's Geopolitical Significance And Prospects In Focus

BMI View: Myanmar's tentative emergence from isolation and its rapprochement with the West are being driven by geopolitical factors, most notably Naypyidaw's desire to reduce its dependency on China, and the United States' bid to increase its influence in Asia. While recent steps are very positive for Myanmar's re-emergence, there are still considerable risks ahead.

Myanmar's tentative emergence from isolation and its rapprochement with the West since 2011 have the potential to become one of the most transformative events in South East Asia over the coming years. Myanmar has long been one of very few countries in Asia that has largely been excluded from the region's economic boom, despite its adjacency to the continent's two giants, China and India. Myanmar's isolation has been the result of decades of inward-looking economic policies and Western sanctions due to its human rights abuses and lack of democracy. This seclusion has increased the country's economic and political dependence on China. In fact, Myanmar has been a virtual Chinese satellite state for some years now, and while its reliance on China may have lifted its economy, it remains one of the least developed in Asia. However, Myanmar's transfer of power from military to civilian rule in early 2011 – although highly exaggerated, given that most top officials are former generals – and two-way outreach to the US have triggered hopes of broader political and economic liberalisation. This could make Myanmar a major economic growth story in Asia and a desirable investment destination.

The Geopolitical Importance Of Myanmar

Myanmar looks set to benefit from a growing awareness of its geopolitical importance in the region, which stems from the following factors:

Strategic location: Myanmar lies at the intersection of China and India, and has thus been the subject of competition for influence by Beijing and New Delhi. During its time in the British Empire, Burma, as it was then known, was a province of British India and had very close ties with its western neighbour, but in more recent times, Chinese influence has been stronger. China regards Myanmar as a crucial transportation corridor connecting its landlocked inner western provinces to the Indian Ocean, and thus world markets. China is building new pipelines from Myanmar's gas fields and ports to its industrial centres, so that less oil to China needs to be shipped via the crowded Malacca Strait, which is vulnerable to piracy and terrorism. China's access to Myanmar's ports could eventually allow the Chinese navy to increase its ability to project power in the Indian Ocean, which is shaping up to be a major arena of 'Great Power' competition (see our online service March 10, 2010, 'Indian Ocean: The Growing Struggle For Dominance'). If Myanmar were to align more closely with India, this would allow New Delhi to become a South East Asian power, potentially allowing it to counterbalance Chinese influence in the region.

US foothold in Asia: If Myanmar were to become closely allied to the US, this would allow Washington to increase its influence in South East Asia, a region that it has generally paid less attention to in recent years due to the wars in Afghanistan and Iraq. Like India, the US is concerned about rising Chinese influence in the region. A pro-US Myanmar would complement US Major Non-NATO Allies (MNNA) Thailand and the Philippines. Moreover, given that Vietnam is keen to strengthen military relations with the US, all five countries could find themselves working together to contain China. The Philippines and Vietnam, in particular, oppose China's growing assertiveness in the South China Sea, which Beijing claims as its own.

Regional security: Myanmar remains vulnerable to separatist pressures, and there are several rebel ethnic armies that have been fighting against the central government for decades. In the event that the regime collapses as a result of a future uprising, any violent fragmentation of the country could lead to massive refugee flows into China, India, Thailand, and Bangladesh, none of which are necessarily well-positioned to cope with them. Myanmar is also a major centre of illegal trafficking of gems, timber, drugs, and labour (including prostitutes), and organised criminal groups could increase their influence if law and order broke down.

Nuclear weapons: Myanmar has in recent years emerged as an ally of North Korea, mainly out of a shared sense of isolation. Both are repressive regimes heavily dominated by their militaries. Reports emerged in 2009 that Pyongyang was assisting Naypyidaw in developing a nuclear programme, raising the spectre of nuclear proliferation in Asia.

Factors That Could Derail The Rapprochement

Perhaps the most visible sign of Myanmar's re-emergence and desire for better ties with the West was US Secretary of State Hillary Clinton's visit there in December 2011 – which was the first trip by America's top diplomat in 50 years. Clinton met senior regime officials as well as veteran opposition leader Aung San Suu Kyi, who is expected to enter parliament after by-elections in April 2012. Also noteworthy was that ASEAN (Association of Southeast Asian Nations) leaders agreed in November 2011 to allow Myanmar to chair the organisation in 2014. Although the chairmanship rotates among member states, Myanmar was previously disallowed from holding the position because of its poor human rights record. Nonetheless, despite this progress, we caution that Myanmar's domestic political reforms have been very tentative, and there is much that could derail the rapprochement with the West and other countries. These are as follows:

Insincere liberalisation: Western and ASEAN nations will be looking for concrete signs that Myanmar is sincere about liberalising its political system and improving its human rights record. If the regime continues to implement only cosmetic changes or backtracks on reform, foreign powers could decide not to reward Myanmar any further. This would weaken the hand of moderates and reformers within the regime, led by President Thein Sein, who are currently in ascendance, and bolster the position of hardliners. The latter are said to have been paranoid about a possible US invasion of Myanmar in the early 2000s.

Future uprising: A popular uprising against the regime–of the kind seen in late 2007, which was swiftly crushed–could test the rapprochement. In the event of mass anti-government demonstrations, we would expect Western countries to publicly side with protestors. Yet, the regime would almost certainly crack down forcefully, thus returning Myanmar to pariah status. Furthermore, the regime would be angered by foreign backing for its opponents, and would thus turn back to China for support. The Libyan conflict of 2011 served as a warning to the regime. Although Western countries rehabilitated the late Muammar Qadhafi and reintegrated Libya into the global economy in the early 2000s after years of isolation, the speed with which the West turned against Qadhafi by backing his country's rebels will surely have been noticed in Naypyidaw.

Conflicts with rebels: Myanmar is a diverse country, with ethnic Burmans comprising only two-thirds of the population. For decades, Myanmar's minorities have waged insurgencies against the central government, leading to widespread human rights abuses. Consequently, peace with rebel groups is a key requirement for the lifting of US and EU sanctions. As of early 2012, the government had signed ceasefires with nine out of 16 rebel groups, and expects to sign deals with the remainder over the coming months – although it has ruled out independence for any minorities. Going forward, there is a risk that ceasefires could collapse, if rebels or the military use them as an opportunity to recover and re-arm. If Myanmar experiences new ethnic conflicts which prompt a particularly forceful response by the regime, then this could quickly jeopardise ties with Western nations.

Nuclear issue: Most observers believe that Myanmar's nuclear programme is too embryonic to pose a serious threat to other countries. Nevertheless, there is concern that North Korea could assist Myanmar to develop atomic arms. If the Naypyidaw regime does not satisfy Western concerns on this issue, then the rapprochement could turn sour.

Myanmar To Pursue Multi-Vector Foreign Policy

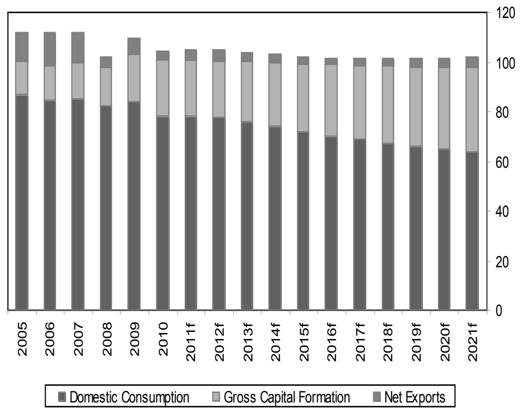
Assuming Myanmar's rapprochement with foreign countries can continue, we would not expect Naypyidaw to lean solely towards the West or India as opposed to China. We believe that China will remain a major economic partner of Myanmar for the foreseeable future as a legacy of the latter's estrangement from other countries since the 1990s. Beijing could even benefit from Myanmar's opening to the wider world, because this would reduce much of the stigma of its role in that country and hasten its development as an economic corridor. Meanwhile, we would also expect Myanmar to strengthen ties with Japan and South Korea to diversify its foreign investor base. Tokyo, and to a lesser extent Seoul, also have an interest in cultivating Myanmar as a counterweight to Chinese influence in the region. If all goes well for Myanmar, then the country could eventually find itself in a similar position to Vietnam in the mid-2000s in 10 or 15 years' time: an emerging frontier market carefully balancing its geopolitical interests between regional powers.

Economic Outlook

Finally Poised To Meet Its Enormous Potential?

BMI View: We have materially revised up our economic forecasts for Myanmar in order to take into account the country's soaring prospects as a result of its ongoing reform drive. Rich in natural resources such as natural gas, copper, tin, timber, and gems, and with a large, widely literate population, Myanmar's growth potential is enormous. Against our previous growth forecast of 5.0% per annum over the coming decade, we now see Myanmar growing at a faster average clip of 7.0% through to 2021 on the back of an investment-led growth boom which will later lead to growing manufacturing and export sectors.

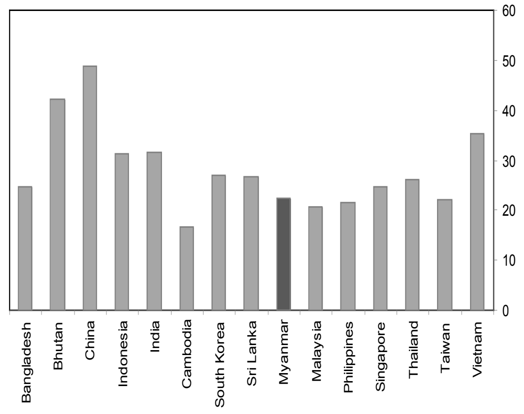
An Investment-Led Boom
Myanmar - Net Exports, Gross Capital Formation, & Domestic Consumption, % GDP



Source: BMI

Myanmar's economy stands on the brink of what could be one of the most dramatic liberalisations in recent history. Largely isolated from the global economy since Ne Win and the Revolutionary Council seized power in a coup in 1962 and unleashed the disastrous 'Burmese Way To Socialism,' major political reforms beginning in 2011 have now set the pariah state on the path towards reintegration. Boasting an incredible wealth of natural resources such as natural gas, timber, gems, tin, and copper (to name only a few), many expect to see an explosive investment drive into Myanmar over the coming years.

Lagging Behind
Myanmar - Gross Capital Formation, % GDP



Source: BMI

Models For Success

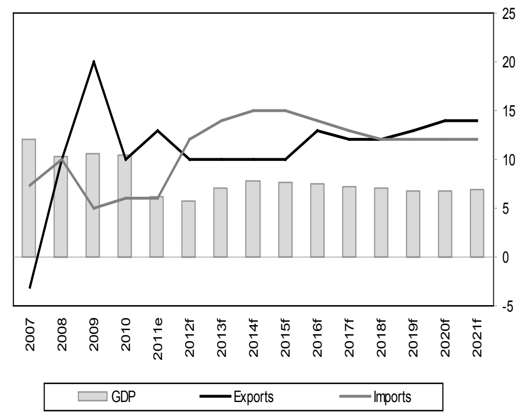
Myanmar boasts the potential to follow in the footsteps of other regional success stories like Indonesia and Vietnam. However, before it can begin to meet that potential, the country must overcome myriad unique challenges. Most importantly, political reforms must continue at a rapid pace. Myanmar's government has constrained the country's potential for decades with failed policy. Furthermore, as a result of its atrocious human rights record, the US and EU have not yet removed harsh and wide-ranging sanctions against the government and re-

TABLE: MYANMAR–ECONOMIC ACTIVITY

	2011	2012f	2013f	2014f	2015f	2016f
Nominal GDP, MMKbn [1]	46,931.7	54,202.6	63,425.8	74,659.1	87,787.1	101,424.1
Nominal GDP, US$bn [1]	57.9	68.2	81.5	97.9	117.4	135.7
Real GDP growth, % change y-o-y [1]	6.2	5.7	7.1	7.7	7.6	7.5
GDP per capita, US$ [1]	928	1,072	1,254	1,477	1,737	1,968
Population, mn [2]	62.4	63.7	65.0	66.3	67.6	68.9

Notes: e=BMI estimates. f=BMI forecasts. Sources: 1 Asian Development Bank. 2 World Bank/UN/BMI lated business interests which effectively prohibit nearly all forms of Western investment into the country. The removal of these sanctions is the single most important pre-requisite for the economy to get off the ground.

Strong Prospects
Myanmar - Exports, Imports, & GDP, % chg y-o-y



Source: BMI

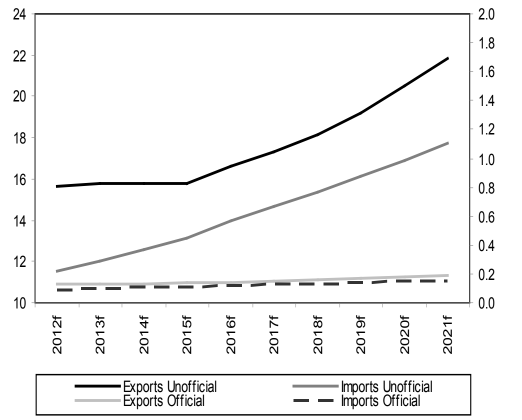
Once sanctions have been lifted, we expect the floodgates that have until now constrained foreign investment to open in a major way. Myanmar is extremely lacking in the domestic capital needed to develop its sorely underdeveloped infrastructure, meaning that capital inflows will surge in the early stages. We expect this process to play out in a similar fashion to that seen in Indonesia during its boom years from the late 1980s to the 1990s, one notable effect of which will be sustained inflationary pressures.

Such capital inflows are inherent to undeveloped countries with a wealth of resources, whether they are commodities like natural gas or a large, young, and untapped workforce (Myanmar, like Indonesia, has both). As such, we are very likely to see such a phenomenon play out in Myanmar over the coming decade.

Expect Immediate Impact On Imports, Not Exports

Before Myanmar can begin to realise the breadth of its export potential, capital goods imports will have to soar. As a capital poor state, Myanmar will need everything from foreign expertise to external financing and equipment in order to begin to develop and prepare its vast natural resources for export. The depth of Myanmar's capital deficit is exacerbated by the fact that it lacks even the most basic infrastructure in most regions. In order to bring exports to market, a vastly improved transport system will be necessary. This includes viable highway and rail corridors, the development of which should become a major focus over the coming decades. Further development of Myanmar's natural gas fields, many of which are found off of its southern coast in the Bay of Bengal, will also be necessary in order for its export boom to begin.

A Considerable Discrepancy
Myanmar - Exports & Imports at Official and Unofficial Exchange Rate, % GDP



Source: BMI

For this reason, we believe that Myanmar's first stop towards economic development will be an investment-led boom. As we have seen in other fast-developing Asian economies, gross capital formation (GCF), which currently comprises only 22.5% of the economy (versus a regional average of 27.0%), should sky-rocket as a percentage of GDP, providing myriad opportunities for foreign infrastructure firms. We are currently forecasting that GCF will make up a much higher 33.8% of Myanmar's GDP by 2021.

Manufacturing Sector To Build Slowly

The development of a manufacturing sector will be similarly reliant on external capital, and is a process that will be measured in decades rather than years. Although foreign direct investment into Myanmar grew exponentially in 2010-11 to approximately US$20bn, less than 1% went towards manufacturing and agricultural industries, while 58% went to extractive industries and 41% to power (the bulk of which will be sent to neighbours Thailand and China). While we expect these numbers to shift as foreign firms begin to take advantage of Myanmar's large, young, inexpensive, and widely literate population, development of Myanmar's infrastructure will have to come first.

As capital begins to flow more freely into Myanmar, we expect imports to average brisk real growth of 14.0% through to 2016, while export growth will trail at a still-strong 10.6%. With the economy beginning to shift from an investment-led boom to a more sustainable and balanced one with stronger export and consumption growth, we see export growth beginning to outpace import growth only towards the end of the decade.

Consumer Boom Still Beyond The Horizon

A boom in domestic consumption will only be sustainable once Myanmar's economy has undergone a major transformation towards one with the aforementioned manufacturing, extractive, and transportation capabilities. We believe that such a transformation remains years away, and thus do not see such heady growth numbers in the country's domestic consumption growth, which we expect to average an underwhelming 4.9% through to 2021.

Statistical Discrepancies Underscore Challenges

Mmention of Myanmar's trade balance brings us to a unique statistical quandary that the country's official accounts present. Although Gross Domestic Product (and all of its underlying expenditure categories) in Myanmar are accounted for by the government and organisations such as the Asian Development Bank (ADB) using the unofficial kyat exchange rate (currently near MMK800/US$), external trade appears to be recorded utilising the official exchange rate (approximately MMK6.4000/US$). This, of course, creates a major statistical discrepancy, as the two rates have not been the same since at least the 1980s, and the unofficial rate is now approximately 125 times the official rate.

As such, we have seen fit to recalculate Myanmar's trade numbers based on the unofficial exchange rate, as the official rate is completely obsolete and generally only used as an accounting gimmick by the government and state interests. Needless to say, such a recalculation has a considerable impact on GDP figures as well as balance of payments accounts, as is reflected in the chart on p.15, where three expenditure categories amount to more than 100% of GDP. We expect the official exchange rate to be abolished by mid-2013, which should lead to better business practices by the government as well as greater data clarity. Nevertheless, such a major discrepancy (we estimate that exports will comprise 15.7% of the economy in 2012, versus official data of 0.1%) underscores the difficulty in assessing such a frontier market.

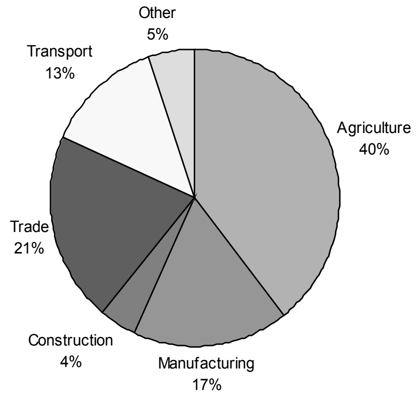
Infrastructure

Greatest Rewards Lie With Commodities-Driven Infrastructure

BMI View: With Myanmar set to genuinely open its doors to foreign investment after decades of self-imposed isolation, it is our view that the country is likely to follow the template of other resource-rich frontier markets such as Mongolia and Kazakhstan, where investment was first channeled into the areas of commodity extraction and the infrastructure required to get production to market. This would present numerous greenfield opportunities for investors across the entire infrastructure spectrum. However, we believe that there are several pertinent pitfalls that need to be recognised in this extreme frontier market.

In the absence of competition from the West, the demand for commodity-based infrastructure has been met by China over the past decade, with Chinese companies snapping up the majority of the infrastructure and power contracts thus far in Myanmar. However, should international sanctions be lifted, greater access to global markets could accelerate the commodity extraction process and present other Asian and Western companies with numerous greenfield opportunities across the entire infrastructure spectrum.

No Longer Just For China
Myanmar - GDP, By Industrial Origin, %



Source: BMI

Furthermore, Myanmar is already looking towards moving up the value chain, setting up special economic zones (SEZ) to process its raw commodities into higher

TABLE: DAWEI MARITIME HUB PROJECT–KEY FACILITIES

Project	Cost (US$mn)	Capacity	Parties (Actual And Potential)	Status
Deep-sea port	2500*	na	ITD	Seeking partners; Thailand-India partnership formed; Construction to start in 2012 and be completed by 2015
Cross-border road link (Dawei, Myanmar to Pu Nam Ron, Kanchanaburi, Thailand)	1000*	132km	ITD	Almost completed
Cross-border railway link (Dawei, Myanmar to Pu Nam Ron, Kanchanaburi, Thailand)	2000	132km*	ITD, Japanese and Chinese investors	Japanese and Chinese financial institutions expressed interest
Coal-based power plants (3x 130MW, 6x 600MW)	6000	4000MW	ITD, Ratchaburi Electricity Generating Holding, Japanese and South Korean investors	MOU signed; 3,000 rai of land sold to Ratchaburi Holding for construction; Project halted by government
Coal-based power plants	4000	3000MW	ITD, PTT	Potential partnership reported
Petrochemical refineries	na	na	ITD, PTT	Undergoing negotiations
Steel smelting plant	9480	10mn tonnes/yr	ITD, Japanese partner	To sell 12,000 rai of land to partner; Partner finalised in H1 2012
Fertliser plant	na	na	ITD	Seeking partners
Township for residential and commercial development	na	na	ITD	Seeking partners
Tourism, resort and recreation complex	na	na	ITD	Seeking partners

**BMI estimate. Note: rai = 1600sqm. Status correct as of January 2012. Source: BMI, Reuters, Bangkok Post, Italian-Thai Development (ITD)* value products such as petrochemicals. These SEZs would require a variety of infrastructure facilities to maximise their potential, creating more greenfield opportunities. The Dawei Special Industrial Zone, for example, is expected to develop around US$8.6bn worth of infrastructure projects such as a deep-sea port, a resort complex, an industrial estate, a 4,000 megawatt (MW) coal-based power plant, and cross-border road, rail and pipeline links.

Building A New Economy
Myanmar – Construction Industry

Source: BMI

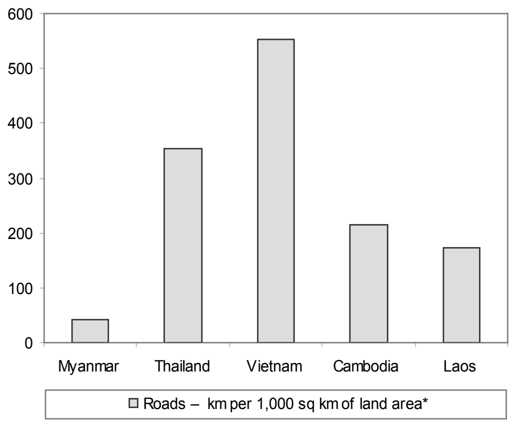
In this analysis, we will highlight some of the opportunities and potential competitors in the various infrastructure sub-sectors as well as discuss the key pitfalls in Myanmar's business environment.

Opportunities

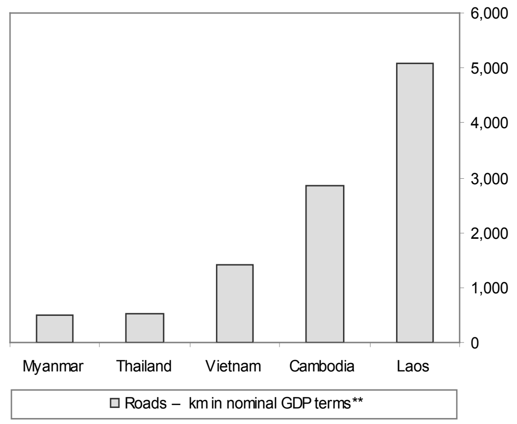
Roads: We believe that roads offer the greatest potential for greenfield projects among the various transport infrastructure sub-sectors. Compared with its regional peers, Myanmar's road network significantly lacks coverage, and this deficit is already a key hindrance to economic development – about 50% of all freight in Myanmar is transported by river barges that are heavily affected by seasonal changes in water levels. This bottleneck is very apparent when we compare Myanmar's total road length in terms of a country's land area and nominal GDP, with the country achieving the lowest score among its regional peers. Furthermore, apart from a few highways, most of Myanmar's roads are in poor condition, with only 12% of its roads paved, according to latest data from the CIA World Factbook.

We believe that viable financial opportunities in the road sector would first arise from the expansion or development of road links with Myanmar's chief trading partners – ie, China, India, Thailand – as they are most likely to benefit from a boom in Myanmar's commodity sector. At present, the most developed cross-border roads are the links with China – ie, the Mandalay-Lashio-Muse road. Although this road has been extensively renovated in the past decade, there is scope for expansion, with plans already in the pipeline to develop the Mandalay-Lashio-Muse link into an expressway and link it to the Kyaukphyu deep sea port.

Short On Coverage
Myanmar - Roads In Land Area



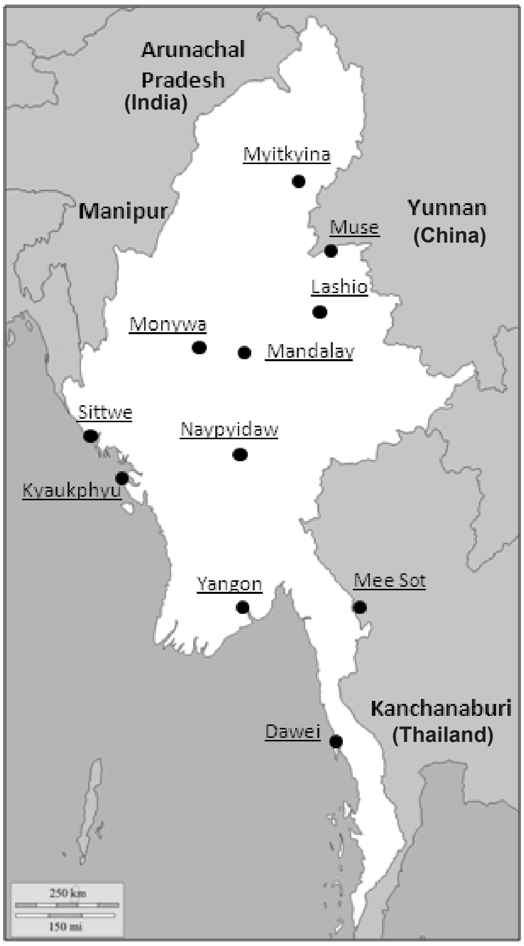
Roads In Nominal GDP



*Based on latest available information. **Nominal GDP based on 2011 figures. Source: BMI, CIA World Factbook, Asian Development Bank, UN Data

On the other hand, road links with India and Thailand are minimal and poor in quality. There have been plans to increase the number of these cross-border roads. In January 2011, Chinese firms **Yunnan Construction Engineering Group** and **Yuzana Group** won a contract to build the 312km Myitkyina-Pangsau Pass (the latter in India's Arunachal Pradesh state) section of the 1,079km Stilwell Road, while **Italian Thai Development** recently completed a road linking the city of Dawei with Thailand's province of Kanchanaburi. These new cross-border links could be expanded into expressways along with existing road links such as the Mandalay-Impahal (Manipur state) road and the Yangon-Mae Sot (Tak province) road.

Opportunities Lie In Cross-Border And Resource-Based Links
Myanmar - Major Cities And Neighbouring Countries' Provinces

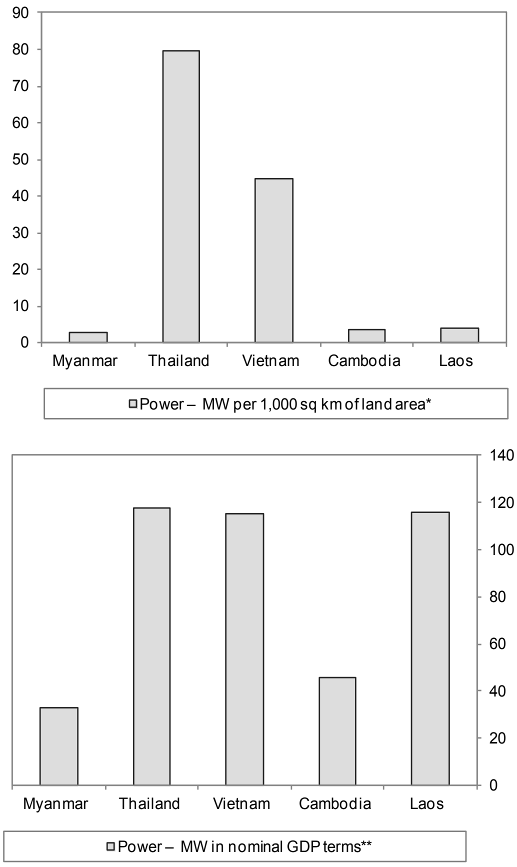


Source: BMI

Apart from cross-border links, roads to key resource nodes could be financially viable as well. For example, the Monywa copper mine complex, potentially one of the largest copper mines in Asia, is located less than 100km from the city of Mandalay and would require roads to maximise its potential.

Power: Myanmar has a clear deficit in electricity generation, with its total capacity underperforming its regional peers in terms of land area and nominal GDP. This deficit needs to be addressed as affordable and reliable access to electricity is a major criterion in achieving sustainable economic growth and carrying out commodity extraction and production.

Clear Deficit
Myanmar - Electricity Generation Capacity In Land Area And Nominal GDP Terms



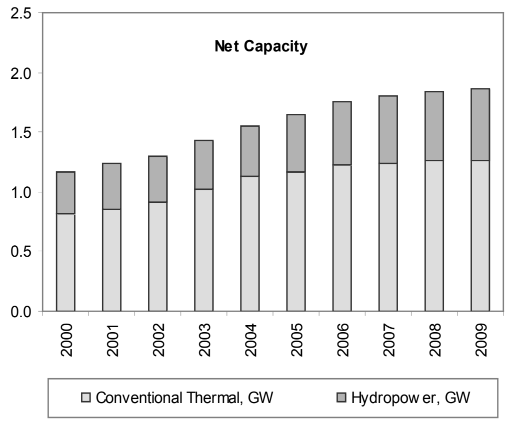
*Based on latest available information. **Nominal GDP based on 2011 figures. Source: BMI, CIA World Factbook, Asian Development Bank, UN Data

We expect the initial demand for electricity to come from remote mines, and given the abundance of oil and gas resources in Myanmar, off-grid generation sources such as conventional thermal power plants would be the most financially viable option to meet their electricity demand. Renewable power plants such as wind and solar farms could also be financially viable at these off-grid sites. Although they have a lower generation capacity, they can be completed within shorter timeframe, allowing them to meet the electricity needs at the initial stage of the commodity extraction process.

In terms of constructing on-grid generation sources, the viability of these projects, particularly large-scale hydropower projects, is uncertain at the moment. Although the electrification rate in Myanmar is around 13%, the country appears to have some excess conventional thermal capacity. Latest data shows that there is a clear divergence between electricity capacity and generation, where hydropower generates more electricity, but has a lower total capacity than conventional sources. We believe that there are three reasons for this divergence:

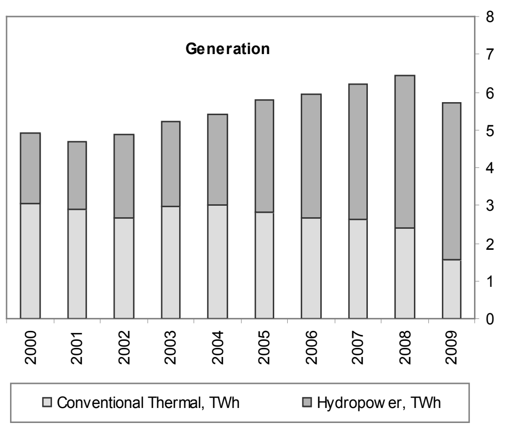
Capacity/Generation Divergence

Myanmar - Electricity Capacity, By Type, Gigawatt



Source: BMI, EIA

Electricity Generation, By Type, Terawatt-hour



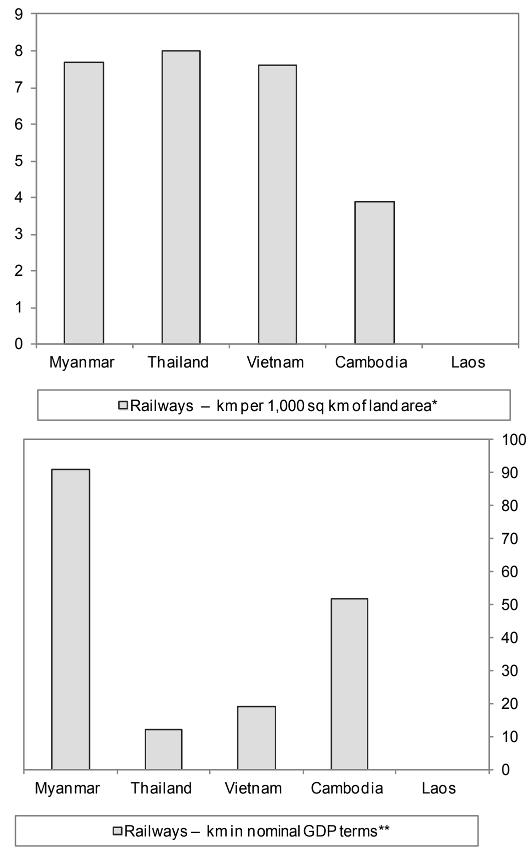
Source: BMI, EIA

- Conventional thermal plants are ageing and require upgrades or replacements;
- There are insufficient transmission lines connected to the national grid;
- Insufficient oil and gas resources are diverted to domestic consumption.

These points suggest that instead of constructing new plants, opportunities could lie in the rehabilitation of

Scope For Double-Tracking

Myanmar - Railways In Land Area And Nominal GDP Terms



*Based on latest available information. **Nominal GDP based on 2011 figures. Source: BMI, CIA World Factbook, Asian Development Bank, UN Data

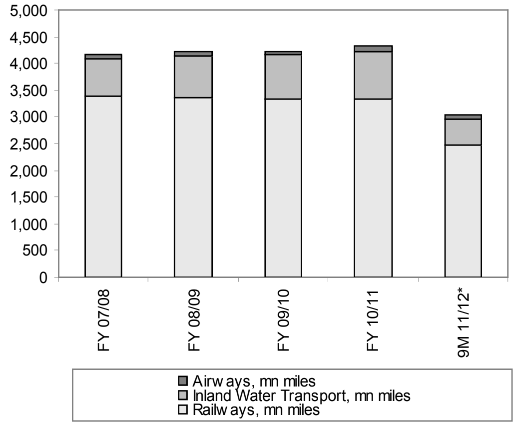
existing thermal plants or the construction of new transmission lines. Furthermore, large-scale hydropower projects have increasingly fallen out of favour with the Myanmar government. The government is pushing for a more libertarian stance and has halted plans by China to build the 6,000-megawatt (MW) Myitsone plant and another six hydropower plants with a combined capacity of 7,360MW in Kachin state.

This particularly concerns India-based **NHPC**, as the company is planning to develop three hydropower projects in Myanmar – the 660MW Shwezaye, the 1,200MW Tamanthi and the 1,200MW Htamanthi power facilities.

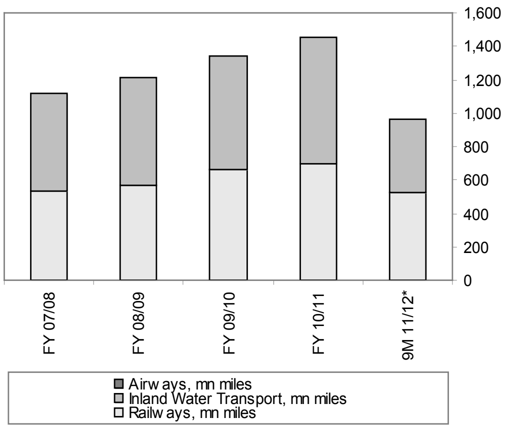
Railways: Myanmar appears to be well endowed with railway lines, with the country's rail capacity exceeding its regional peers in terms of land area and nominal GDP. However, the entire network is based on narrow-gauge tracks rather than broad-gauge tracks, which have a higher haulage capacity and allow for greater speeds than narrow gauge lines. Most of the network is also in poor condition and only has single track, making the whole network susceptible to delays if a single train breaks down.

Railways Dominate Domestic Transport

Myanmar Internal Public Transport, By Mode Of Transport - Passenger, mn miles



Myanmar – Freight ton, mn miles



***Fiscal year from April - March. Source: Immigration and National Registration Department, Ministry of National Planning and Economic Development, Central Statisticial Organization, Myanma Airways, Myanma Railways, Inland Water Transport, Customs Department**

Therefore, we see significant scope for expansion, with these rail projects becoming increasingly viable once Myanmar's commodity industry starts to mature. Myanmar's railway system is also not connected to its neighbours, and just like roads, we expect increased trade activity in commodities to boost the viability of these cross-border links. There are currently no plans to build a cross-border rail link to India, but there are plans to build a 1,215km railway line between Kyaukphyu and Kunming, the capital of China's Yunnan province, and a 132km railway line between Dawei and Thailand's Kanchanaburi province.

While not related to the commodity sector, it is worth discussing Myanmar's urban transport sector as the country is planning to construct its first urban railway system in Yangon under a Build, Operate, Transfer (BOT) model. We are skeptical about its financial viability as large portions of the population are unlikely to be able to pay to use the system over the next decade. We estimate that about 20% of Myanmar's urban population is below the poverty line, while GDP per capita, a measure of standard of living, is just US$890 in 2011 and forecast to reach US$2,606 by 2021, way below the regional average of US$3,609 for emerging Asian countries in 2011. Therefore, we believe that the urban railway system constitutes a relatively high-risk, high-return venture for any interested companies, with the pay-back period for the project potentially extending beyond a decade.

Oil & Gas Pipelines: We see a lot of financially viable opportunities in the construction of oil and gas pipelines in Myanmar. The combination of huge, untapped energy potential – Myanmar's proven reserves for natural gas and crude oil stand at a respectable 26.8 years and 11.7 years respectively, according to Thai major **PTT Exploration and Production** – close proximity to major energy users (China, India, Thailand and Bangladesh), but also crucially, the opportunity to by-pass the Malacca Straits, means that there will be a robust demand for pipelines to these demand centres. A lifting of international sanctions could also see a flurry of investment in the development of Myanmar's reserves for international export, creating project opportunities in the development of pipelines to major ports in Myanmar.

Most of the pipelines are currently been developed by South Korean and Chinese companies – **Hyundai Heavy Industries** and **China National Petroleum Corporation** have won contracts to build parts of an oil and gas pipeline from Myanmar to China – because these countries have won the exploration rights to Myanmar's oil and gas fields. However, other companies such as Malaysia's **Petronas** and Russia's **CIS Nobel Oil Company** are winning these rights from the government, and these companies could similarly award contracts to their domestic construction partners.

Securing Energy
Myanmar's Gas Pipelines

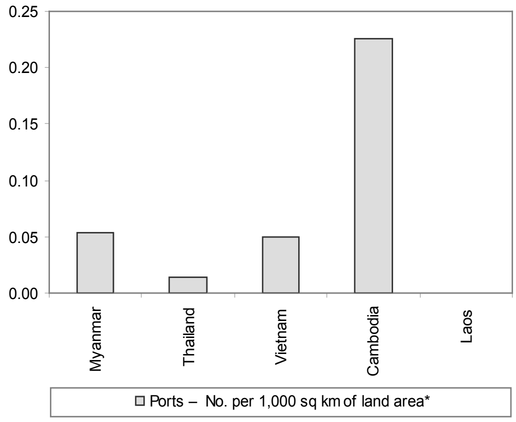
Source: BM

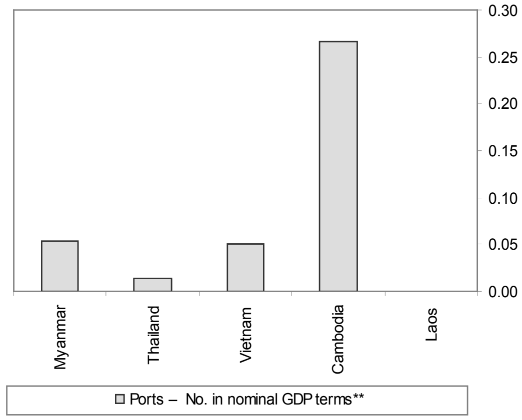
Ports: We do not see a lot of financially viable opportunities in the construction of new ports in Myanmar. Not only is the country already developing a new deep sea port in Dawei (worth around US$2.5bn according to our estimates), but Myanmar's port sector is not a clear underperformer among its regional peers when compared in terms of land area and nominal GDP, suggesting that Myanmar has sufficient coverage to meet trade activity.

Instead, we believe that financially viable opportunities would come from investing and expanding the Dawei port and Myanmar's existing ports – the country's main ports are situated in the cities of Yangoon, Sittwe and Mawlamyine. These ports would need a variety of facilities to adequately export Myanmar's different resources, from container wharfs to oil and gas terminals.

The construction of port facilities has been primarily dominated by South Korean and Chinese companies in the past, but the country is increasingly opening to investments from other countries. Hong Kong-based port operator **Hutchinson Port Holdings** fully owns and operates the Myanmar International Terminals Thilawa near Yangon, while the Dawei port project is headed by Thailand-based construction company **Italian Thai Development** .

Need Diversity, Not Quantity
Myanmar - Ports In Land Area And Nominal GDP Terms

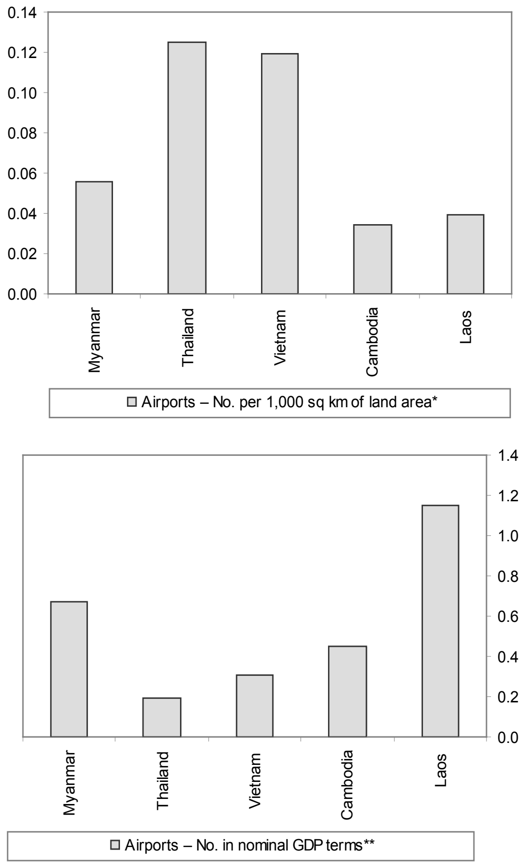




*Based on latest available information. **Nominal GDP based on 2011 figures. Source: BMI, CIA World Factbook, Asian Development Bank, UN Data

Airports: Given that airports play a minimum role in the commodity sector, we do not see a lot of financially viable opportunities in the construction and management of airports in Myanmar over the next decade. Furthermore, when we compare the country's total number of airports in terms of land area and nominal GDP, Myanmar is not a clear underperformer among its regional peers, suggesting that its existing airports are sufficient for its current state of economic development. Therefore, even though Myanmar is keen on private investment in this sector – Myanmar had announced plans to privatise all domestic airport management businesses in September 2011 – the rewards from this sector are very uncertain for the next decade and would depend on several long-term factors such as a general rise in incomes within Myanmar and the development of a vibrant tourism sector.

Lacking Viability
Myanmar - Airports In Land Area And Nominal GDP Terms

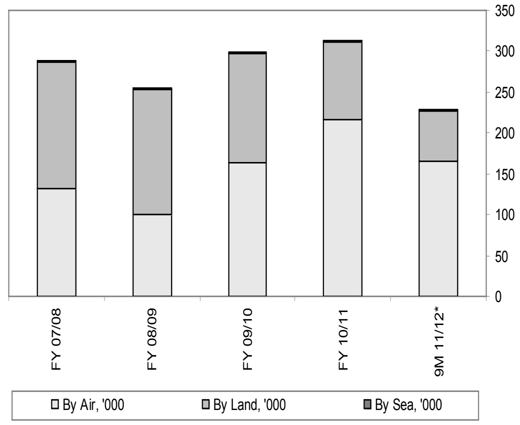


*Based on latest available information. **Nominal GDP based on 2011 figures. Source: BMI, CIA World Factbook, Asian Development Bank, UN Data

Having said that, although tourist arrivals into Myanmar are on the rise (see chart), we believe that most of this traffic is taking place via the Yangon International Airport, the country's primary airport. Any financially viable opportunities would be focused on expanding or complementing Yangon airport. Plans to expand the airport are already in the pipeline, with Myanmar looking to increase the capacity of Yangon airport by 40%, from 2.7mn passengers a year to 3.8mn a year.

Investment into Myanmar's airport sector would likely require a partnership with **Asia World**, the builder and operator of the Yangon airport. Asia World is the dominant player in Myanmar's airport industry and is currently constructing the new international airport in Naypyidaw.

Growth Mainly Through Yangon
Myanmar - Tourist Arrivals By Mode Of Transport, '000



*Fiscal year from April - March. Source: Immigration and National Registration Department, Ministry of National Planning and Economic Development, Central Statistical Organization

Business Environment

Highly Centralised Government: Despite a move to a civilian government, Myanmar's system of government remains highly authoritarian, with the reins of power mainly held by the 11-member National Defence and Security Council (NDSC), led by President Thein Sein.

The NDSC takes a hands-on approach in awarding and reviewing infrastructure projects. This is both an upside and downside risk for investors. While it could lead to a swift resolution in critical obstacles for an infrastructure project with government support (eg land acquisition, environmental and regulatory clearances), there is almost little or no legal recourse for companies should the government choose to remove its support and halt the project.

The importance of government support in Myanmar has been recently highlighted by the suspension of the coal-fired power project in the Dawei Special Industrial Zone, where the Myanmar government arbitrarily halted the project without consultation with the Thai companies involved.

Domestic Partnerships Unavoidable: Since 2010, the Myanmar government has been divesting state infrastructure assets such as ports and airports to domestic private companies. As such, we believe that these domestic companies hold a lot of influence in Myanmar's infrastructure sector and are key to winning the concessions to major projects.

One such company is Asia World Company, which is the largest conglomerate in the country and is involved in all types of key infrastructure projects. The company is currently constructing a new international airport in Naypyidaw, Myanmar's capital, while its subsidiary, **Pioneer Aerodrome Services,** manages handling services at Yangon International Airport. Asia World was also the domestic partner involved in the construction of the China-led Myitsone dam and is set to make an investment into the multi-billion dollar Dawei martime hub project.

Risks All On Investors: Given that the government lacks the funds to finance its infrastructure needs – Myanmar's reserves are estimated to be about US$6bn, approximately 12% of its nominal GDP – we believe that most of the new projects would be financed by official development assistance loans or awarded under a Build, Operate and Transfer (BOT) model.

This means that companies which are able to provide expertise and financing from their domestic governments and banks would be in pole position to win these contracts. Chinese companies have been highly successful in using this approach to snap up infrastructure and power contracts in Myanmar and, as such, we expect other companies, particularly Japanese, to follow suit. The Japanese government is planning to start providing loans to Myanmar for the first time since 1987 and this could start as early as April 2012, after a planned meeting by both countries on April 21 2012.

However, this means that governments with limited fiscal strength to extend loans to Myanmar would find it difficult for their companies to compete for contracts. This has been the case for Indian companies, which have lagged behind Chinese companies in terms of projects awarded in Myanmar.

In addition, companies awarded BOT projects would have to bear all of the risks, as unlike other risky countries (eg Indonesia), no guarantees are provided to cover the risk of financial losses that could arise from Myanmar's business environment. Some of these projects, such as the construction of an urban railway system in Yangon, present notable downside risks to investors as they hinge on a broad-based increase in the economy over a long period of time to recoup their investments.

Mining

Copper: Myanmar's Hidden Gem

BMI View: Recent improvements to Myanmar's political and economic climate could help spur additional investment into the country's nascent mining sector. The country enjoys vast, untapped mineral wealth best exemplified by the Monywa copper mine, which has the potential to become one of the largest in Asia.

Letpadaung Potential

Contained Copper Metal In Select Frontier Market Mines

	Copper Grade, %	Contained Metal, Kt
Monywa (Myanmar)	0.37	5,428
Aynak (Afghanistan)	2.34	5,616
Tampakan (Philippines)	0.62	10,500
Oyu Tolgoi (Mongolia)	1.33	18,452

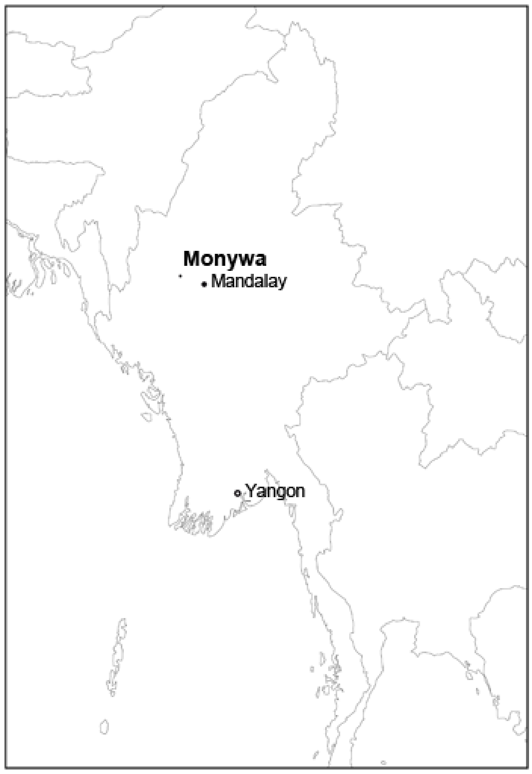
Source: Company reports and websites, Afghanistan Ministry of Mines and Industry

Myanmar has the potential to become one of the largest copper-producing countries in Asia through the development of the Letpadaung copper deposit in the country's Monywa copper mine complex. Before divesting their stake due to human rights concerns in 2006, Canadian firm **Ivanhoe Mines** estimated that the Monywa copper mine, if fully developed, would have a potential annual production capacity of 200kt (thousand tonnes) of copper. This would make Monywa one of the largest copper mines in Asia.

The Monywa mine's copper deposits delineated back in 2007 were estimated to be large enough to support production for more than 30 years.

One Of Asia's Largest Untapped Mines

Location Of Monywa Copper Mine



Source: BMI

The mine is composed of three main copper deposits; namely, the Sabetaung, Kyisintaung, and Letpadaung.

TABLE: PER CAPITA FOREIGN DIRECT INVESTMENT, US$

	2003	2004	2005	2006	2007	2008	2009	2010
Myanmar	96	105	102	113	127	147	158	172
Philippines	139	152	175	194	231	241	253	267
East Timor	20	19	19	27	34	66	108	304
Laos	114	115	118	149	201	236	284	337
Cambodia	150	158	185	219	280	335	370	421
Indonesia	47	71	181	237	344	307	456	507
Vietnam	338	354	374	399	474	580	661	747
Thailand	749	805	906	1,144	1,388	1,370	1,596	1,841
Malaysia	1,644	1,682	1,703	2,020	2,801	2,676	2,823	3,568
Brunei	24,764	25,190	25,472	26,124	26,297	26,409	26,844	27,577
Singapore	35,425	40,727	45,612	54,778	70,444	68,478	69,475	92,378

Source: UNCTAD, BMI

The Letpadaung deposit holds over 4.3mnt of contained copper metal resources, 79.4% of the total reserve. Compared to copper assets of other frontier mining markets across Asia, the Monywa's total contained copper metal (from its measured and indicated resources) of 5.4mnt is approximately the same size as that of the 5.6mnt Aynak copper project in Afghanistan. In May 2010, **China North Industries Corporation** (Norinco), a Chinese weapons manufacturer, secured the rights to the Letpadaung deposit. The company plans to spend US$997mn developing the asset over the coming years.

200ktpa Capacity Can Be Built In Four Years

In Ivanhoe's development plan for the Monywa copper mine in 2005, the company originally planned to ramp-up production at the mine to 200kt by 2010 of which 150kt will be from the Letpadaung deposit and 50kt will be from the Sebataung and Kyisintaung deposits. Access to power is a key concern in the project and the installation of a 215 kilometre transmission line from Thazi (located south of Mandalay on the main national electricity distribution grid) to Letpadaung was considered. The alternative option was the construction of a coal or natural gas-fired power plant in the area. Stage 1 of the expansion plan would have required 40MW (megawatts) in standing electrical capacity. Stage 4 would have required anywhere between 60 to 80MW in standing electrical capacity.

Cautious Optimism Appearing

Ivanhoe Mines confirmed its intention to divest its Myanmar assets in October 2006 due to concerns over the ruling military junta's human rights record. The company relinquished ownership of the asset to the Monywa Trust and was only able to sell the stake in July 2011. Phase 2 of Ivanhoe's plan for the Monywa copper project, which would have involved the development of the Letpadaung deposit, was never initiated.

Myanmar severely lags behind its regional peers in terms of per capita foreign direct investment. The country's per capita FDI of US$172 in 2010 ranks last in the South East Asian region. East Timor and Indonesia, which lagged behind the country in 2003, have overtaken Myanmar on that measure. The largest mining investment in recent years was the US$997mn plan from Norinco. The imposition of EU sanctions leading to Myanmar's relative economic isolation, is the major reason why the country has struggled to attract the levels of FDI seen across its regional peers.

Given that Myanmar still has a significant number of other undeveloped mineral assets, recent improvements in the country's political and economic climate are encouraging, and could potentially pave the way for further growth in the industry. In 2010, the military-dominated country held its first elections in two decades, putting in place a civilian government. Along with opposition leader Aung San Suu Kyi's announcement to re-enter politics, the junta recently pardoned and freed more than 6,300 prisoners, many of whom had been held on political grounds (see 'A Myanmar Spring', October 20 2011). In a symbolic move, the Association of Southeast Asian Nations (ASEAN) has agreed to let Myanmar take over the group's rotating chairmanship in 2014, while US Secretary of State Hilary Clinton visited the country early December 2011. While it is still early days in terms of political and economic liberalisation, we believe that the US government may look to ease, or even remove, sanctions on the country in 2012. Such a scenario could see a surge in FDI inflows, with the mining sector likely to be a key beneficiary.

TABLE: 2005 MONYWA EXPANSION PLAN

Stage	Production	Description
1	50ktpa	Construct 10ktpa expansion to the S&K mine tank house
2	100ktpa	Construct 50ktpa SX-EW module, expand power supply and construct leach pads and solutions handling pond no.3 at Letpadaung
3	150ktpa	Construct 50ktpa SX-EW module, crushed ore leach pads, tailings dam facilities at Letpadaung
4	200ktpa	Construct 50ktpa SX-EW module, crushed ore leach pads, tailings dam facilities at Letpadaung

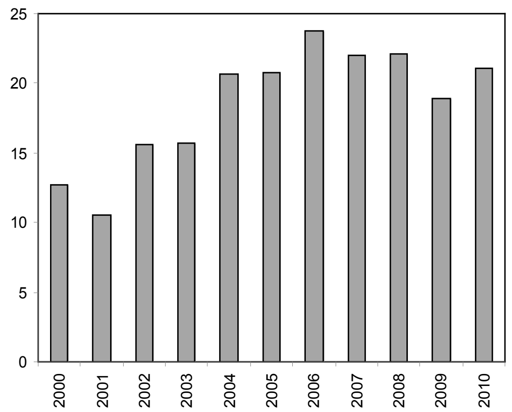
Source: UNCTAD, UNCTADstat

Oil And Gas

Frontier Characteristics And Geographic Advantages Bolster O&G Outlook

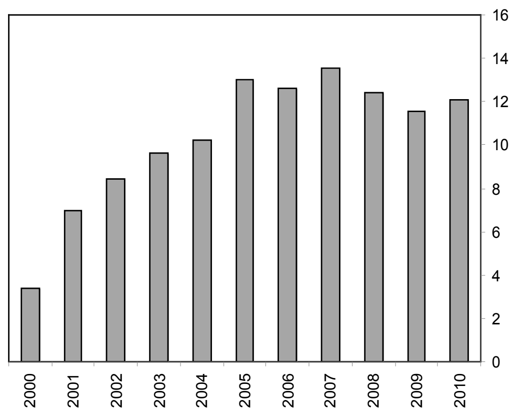
BMI View: The latest licensing round for Myanmar's onshore acreage highlighted that the status quo is still in place with Asian IOCs dominating the tender. However, the industry is evolving and we expect the transformation to intensify in the coming years.

Frontier Energy Plays
Myanmar Crude Oil (000s b/d)



Source: EIA

Natural Gas (bcm) Production

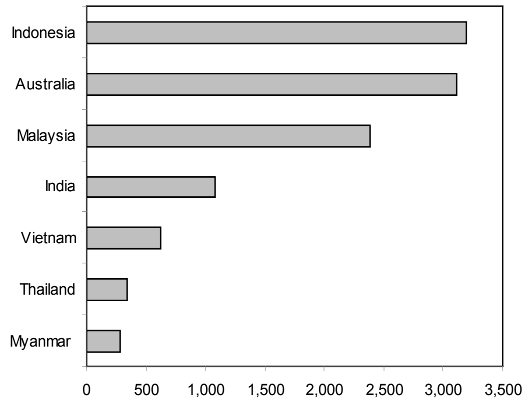


Source: EIA

Domestic demand will increase as the productive capacity moves up the value chain into processing and refining; the competitive landscape will deepen, and we do expect Western, frontier-focused independents will try and carve a place in the market; exports could diversify into other Asian markets (infrastructure permitting).

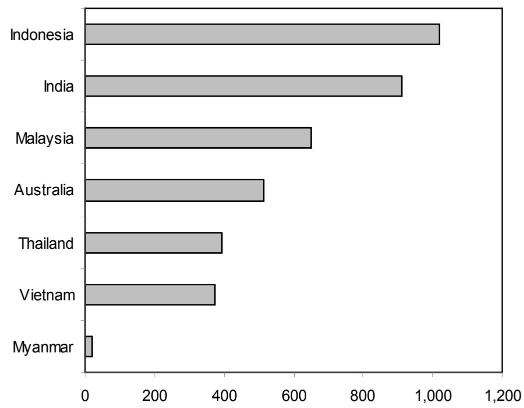
As is highlighted in this report's Infrastructure section, we believe that Myanmar will remain a commodities-driven market in the coming years. Oil and gas will feature prominently in the commodities arena, even though the known endowment is not as large as other regional markets.

In Perspective
2010 - Proven Gas Reserves (bcm)



Source: EIA

Daily Oil Production (000s b/d)

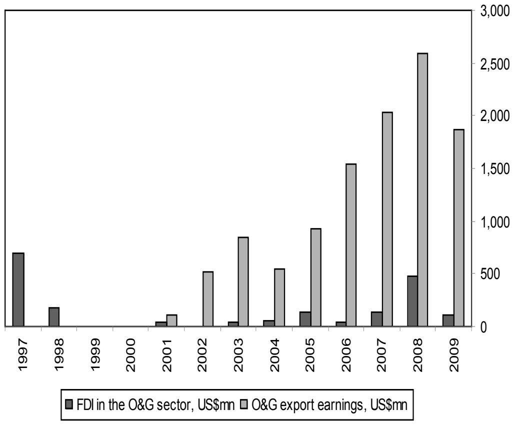


Source: EIA

Myanmar has been a producer for the past 25 years and its reserves -especially the noteworthy gas reserves- will prompt competition amongst foreign producers for exploration in the coming years, thus possibly unlocking further reserves. We see Asian companies in a strong position to maintain their "first mover advantage" in

Myanmar's oil and gas sector, with Malaysia's NOC **Petronas** and Thailand's **PTTEP** already intensifying their ventures in the market, before more outside players move in. At the moment, outside Asia, different layers of sanctions still prevent European and/or North American-based and listed independents and IOCs from becoming heavily involved in the market.

Asian-Dominated FDI
Myanmar FDI and O&G Export Earnings Data



Source: BMI

Assessing future prospects for the sector, we see scope for domestic consumption to increase, in line with **BMI**'s view that the productive capacity will move up the value chain, pertinently for oil and gas, into petrochemicals and refining. If the major Dawei Special Industrial Zone is set up then a far greater quantity of hydrocarbons, especially crude oil, will need to be allocated to the domestic market.

Rich Pickings

Myanmar has 19 onshore and 3 major offshore fields. Given the closed nature of the regime, reserves and resources estimates vary significantly, with the available reserves data for oil looking especially dubious.

The US Energy Information Administration (EIA) data suggest daily production of nearly 21,000 barrels per day (b/d), with crude oil reserves of 50mn barrels (giving the market approximate 7 years of remaining reserves in 2010). In terms of natural gas, the EIA data show daily production of 12.1 billion cubic meters (bcm), and reserves of 280 bcm, putting reserves at 23 years.

According to Thailand's PTT Exploration and Production (a major investor in the country), Myanmar's proven reserves for natural gas and crude oil stand at a respectable 26.8 years and 11.7 years respectively.

Meanwhile, Myanmar's sources, claim that the country has recoverable reserves of 510bcm from a total proven resource of 2.54trn cubic metres (tcm), plus 3.2bn bbl of oil. These figures should be treated with caution. As far as output is concerned, data from the country's Central Statistical Organisation show that in FY2006-2007 Myanmar produced 21,290 b/d of oil and 13.039bcm of gas.

Natural gas production figures however will be ramped up in the coming years as production at the offshore fields A-1 (Shwe) and A-3, operated by a consortium led by South Korea's **Daewoo**, is due to commence in 2013. Estimated daily production will be nearly 6.1bcm annually; of which, 5.2bcm will go to China via a new natural pipeline; Myanmar's first exports to a market other than Thailand.

Asian NOCs have long been the main international players in Myanmar's energy sector and this trend looks set to continue in the latest licensing round, although smaller independents could also look to snap up acreage.

Myanmar first entered into joint ventures (JVs) with IOCs in 1988 and since then has granted 91 licences 47 onshore and 44 offshore. In January 2012, the government completed a tender for 18 onshore oil blocks, the largest single licensing offer in recent years. Although the country is effectively a no-go area for many Western companies due to international sanctions on Myanmar's government, it has provided rich pickings to a number of state-run Asian companies. As we had expected, the tender was dominated by Asian companies, though two small European independents also grabbed some secondary contracts (**Geopetrol International Holdings** was awarded a marginal oil field, while **CIS Nobel Oil Company** secured a production sharing contract (PSC) for one oil and gas field.)

Despite significant oil and gas potential, Myanmar has historically failed to attract commensurate investor interest from international oil companies (IOCs). The chart on page 28 shows the volatility in FDI flows into the oil and gas sector in the past decade; an unsurprising volatility given the nature of the regime and the investment climate.

Although French major **Total** has long been involved in the country, few other IOCs have joined it, leaving the oil and gas industry largely controlled by state-run Myanmar Oil & Gas Enterprise (MOGE) and a host of national oil companies from China, India, Thailand, Malaysia and South Korea.

Malacca Bypass Advantage

Myanmar's main advantage offsetting its rudimentary investment climate is its large areas of underexplored acreage and its proximity to major Asian markets, particularly China. With the inauguration of the twin oil and gas pipelines to China, Myanmar will be able to act as

PLAYERS IN MYANMAR'S UPSTREAM

Company	Nationality	Involvement in the market–Offshore	Involvement in the market–Onshore
Danford Equities Corp.	Australian	Yatagun East field operator	
CIS Nobel Oil Company	Azerbaijan		
A, B–1 onshore concession // 1 new onshore concession (January 2012 licencing round)			
China National Petroleum	Chinese	China–Myanmar Pipeline onwer and operator // A-4 offhsore field partner // AD-1, AD-6, AD-8 field operator	C-1, C-2 onshore fields partner
Golden Aaron	Chinese	A-4 offshore field partner	C-1, C-2 onshore fields partner // Kyaukphyu onshore field partner
Tianjin New Highland	Chinese	1 onshore concession (January 2012 licencing round)	
EPI Holdings	Chinese	1 onshore concession (January 2012 licencing round)	
CNOOC	Chinese	M-10 offhsore field operator	C-1 , C-2 onshore field operator // Kyaukphyu onshore field operator
Sinopec	Chinese		
Mahudaung onshore field operator			
Jubilant Energy	Dutch	1 onshore concession (January 2012 licencing round)	
Geopetrol International Holdings	French	1 onshore concession (January 2012 licencing round)	
Gail India	Indian	A1–A3 offshore field partner	
ONGC Videsh (OVL)	Indian	A1–A3 offshore field partner // AD-2, AD-3, AD-9 offhsore field operator	
Essar Oil	Indian	A-2 offshore field concession	Sittway onshore concession
Istech Resources Asia	Indonesian	1 onshore concession (January 2012 licencing round)	
Nippon Oil	Japanese	M-12, M-13, M-14 (Yetagun) offshore field partner	
Petronas	Malaysian	M-12, M-13, M-14 (Yetagun) offshore field operator // M-15, M-16, M-17, M-18 offhsore fields operator	
Myanmar O&G Enterprise (Myanmar NOC)	Myanmar	A1–A3 offshore field partner // Apyauk, Latpando, Myanaung, Shwepyitha, Thargyitaung and Nyaungdon field operators	
Eden Group	Myanmar	M2 offshore field partner	
Zarubezhneft	Russian	M2 offshore field partner // M-8 offhsore field operator	
Rimbunan Retrogas	Singapore	M-1 offhsore field concession	
UNOG	Singapore	M-1 offhsore field concession	
Silver Wave Energy	Singapore		
B-2 onshore field operator			
Daewoo International	South Korean	A1–A3 offshore field operator // AD- 7 osshore field operator //	
Kogas	South Korean	A1–A3 offshore field partner	
PTTEP	Thailand	Thailand–Myanmar pipeline owner and operator // M-3, M-4 offshore fields operator // M-5, M-6 (Yadana) offshore field partner //M-7, M-9 offshore field operator // M-11 offhsore field operator // M-12, M-13, M-14 (Yetagun) offshore field partner	
PetroVietnam	Vietnam	M2 offshore field operator	
Total			

Source: BMI; Blood Money – A Grounded Theory of Corporate Citizenship; Myanmar (Burma) as a Case in Point. University of Waikato, NZ an entry point to the Chinese market, and possibly in the future wider SE Asia, by-passing the Straits of Malacca.

The natural gas pipeline's capacity will be one of the largest in the region, carrying 12bcm annually from Myanmar's Shwe (A-1) and A-3 offshore gas fields to China's Yunnan province. Construction is due to be completed in 2013, to coincide with the commencement of production from the Daewoo operated fields. The Daewoo-led consortium agreed to supply **CNPC** with 5.16bcm of gas per annum via the China-Myanmar gas pipeline for 30 years, starting in 2013.

Alternatively, the Myanmar-China oil pipeline is designed to reduce the journey time for imports of crude oil from the Middle East. At present around 80% of China's crude imports are transported via tanker through the heavily congested Malacca Strait. The pipeline will transport crude oil 771km from Kyaukphyu on the coast of Myanmar to the Chinese city of Kunming, capital of Yunnan province. The pipeline is expected to be built in two phases, with an initial capacity of 240,000b/d rising eventually to 400,000b/d (equivalent to 3% of total forecasted Chinese oil consumption in 2020). Work on the US$1.5bn pipeline officially began in June 2010.

CNPC owns 50.9% of both pipeline projects, with Myanmar's state-owned **Myanmar Oil & Gas Enterprise** (MOGE) holding the remaining 49.1%.

Given the scope for infrastructure development in the country, the development of midstream infrastructure to serve China and other SE Asian markets like Laos and Vietnam would leverage Myanmar's position in the Bay of Bengal as a bypass route to the Malacca Strait. The savings and security advantages therefore make new pipeline projects likely to proliferate in the future.

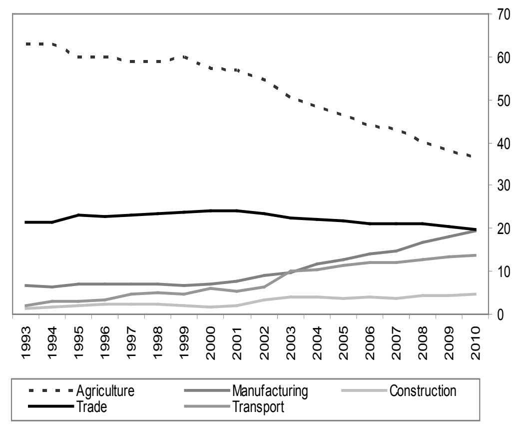
Agriculture

Unearthing Massive Potential

BMI View: With the agriculture sector contributing close to 40% of the country's nominal GDP, Myanmar remains largely an agro-based economy. In the following article, **BMI** will discuss the broad trends within the industry thus far and provide our outlook for the sector, with emphasis placed on the rice industry.

While Myanmar's agriculture sector has represented a decreasing proportion of the country's economy over the past few decades, we highlight that it is still the mainstay of nominal GDP, accounting for roughly 36.4% in 2010 according to World Bank data. Moreover, agriculture commodities were also equivalent to 15.5% of total exports in 2009.

Smaller Now But Still The Biggest
Myanmar - Top Contributing Sectors To GDP, %

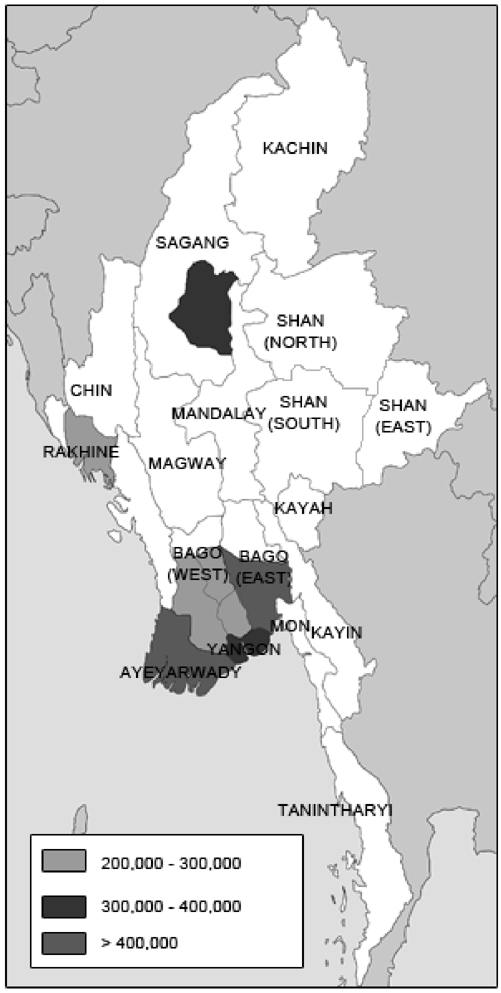


Source: BMI, ADB

Since market-oriented economic reforms were introduced in 1988, the agricultural sector has been largely market-driven, with little government intervention this is an aspect which we believes bodes well for the sector especially in terms of its appeal to the private sector and, in the future, to foreign investors. Indeed, since the before 1988 when the government dictated agricultural production for most crops as well as set fixed prices for them, farmers are now allowed freedom in agricultural production. Furthermore, since a new trade policy was announced in April 2003, paddy is also no longer sold to the government. In addition, the private sector is encouraged to procure and distribute agrochemicals, quality seeds, farm machinery and other inputs.

Following these reforms, irrigation of land has also surged, from 12.6% of total acreage in 1989 to 24.6% in 2008 (after widespread irrigation projects had been completed). To date, cereals, especially paddy, or unmilled rice, dominate the total area sown.

Concentrated In The South West
Myanmar - Rice Growing Regions, Hectares



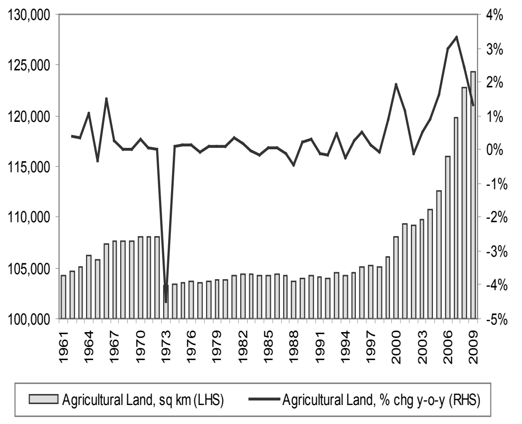
Source: BMI

The Challenge Of Yields

Despite these notable strides in agricultural development, Myanmar undoubtedly faces growing challenges in terms of boosting productivity and yields, in line with the rest of the region. In particular, we highlight the lacklustre performance in rice production and yields as a key area for improvement.

As illustrated in the chart below, rice yields and nationwide cereal yields were strongly correlated for much of the period from 1960 until the late 1990s. Since then, rice yields have started trending lower despite an overall improvement in cereal yields. We believe that this has been largely due to the scarce use of hybrid seeds which are more resilient to adverse weather conditions and yield 2.5-3 times higher output than the more commonly used High Yielding Variety (HYV).

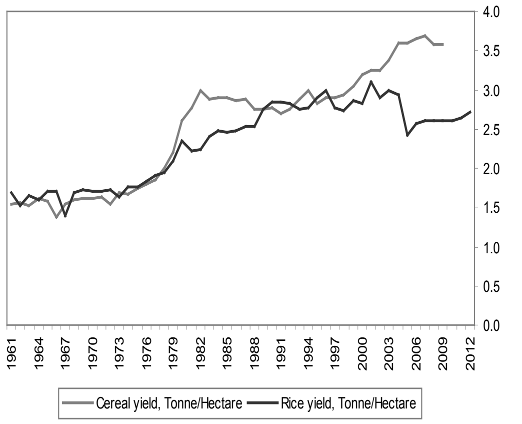
Expanding Land For Agriculture
Myanmar - Agricultural Land, Sq Km & % Chg y-o-y (RHS)



Source: BMI, World Bank

Rice hybrid seeds were introduced in the late 1990s, although by 2007/08 only 1% of total rice sown was allocated to hybrid seeds, with the rest of the area planted with HYV rice seeds. On the other hand, for other cereals such as corn, hybrid seeds comprised 54% of the total areas sown for corn and HYV seeds accounting for less than 30% by 2007/08.

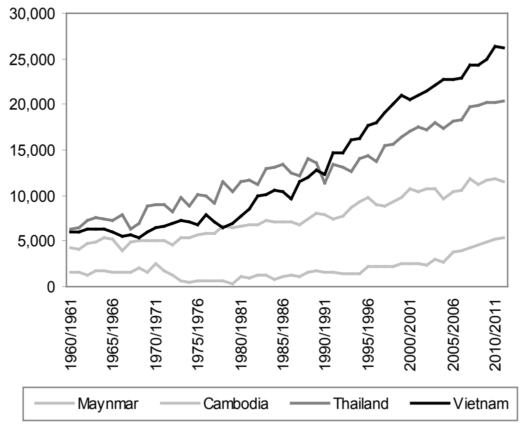
Rice Yield Growth Is Lagging
Myanmar - Cereal & Rice Yield, Tonne/Hectare



Source: BMI, World Bank, USDA

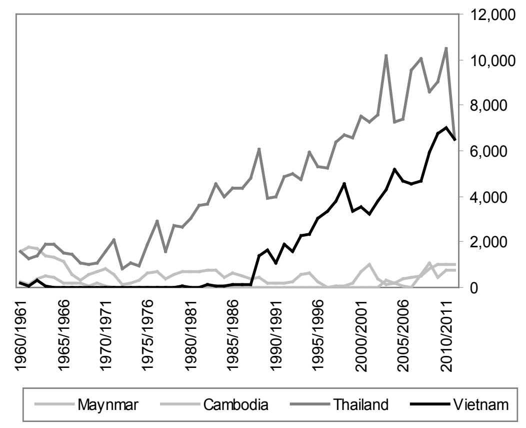
We believe that there is significant potential for increasing rice yields from the current 2.7 tonnes/hectare to the average yields of HYV (4-5 tonnes/hectare) or even to the level of hybrid seeds (10-15 tonnes/hectare), according to data from Myanmar Agriculture Service. Despite the fact that total area sown to paddy in Myanmar is comparable in Vietnam, Myanmar rice yields are just over half that of its regional neighbour. Production and yields in Myanmar and Vietnam started out at relatively similar levels in the 1960s but due to years of neglect of the sector, not least due to the closed economy under the strict military rule of the past four decades, Myanmar's agricultural performance has since been overshadowed by other regional counterparts (see chart below).

Myanmar Lagging Behind
Selected Countries Rice Production, '000 tonnes



Source: BMI, USDA

Selected Countries Rice Exports, '000 tonnes



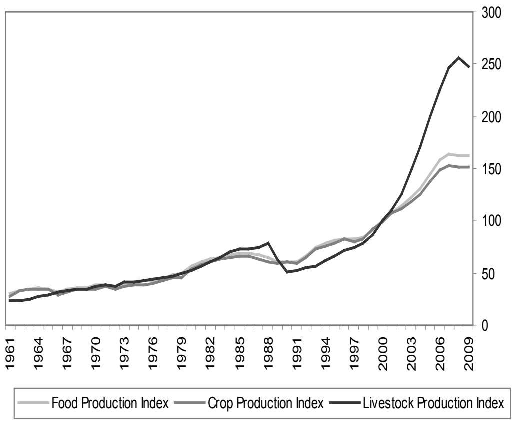
Source: BMI, USDA

Improvement Needed

We highlight a few key areas of improvement for the rice sector. **Firstly, it is clear that there is a pressing need for increased investment in the sector and sup-**

porting industries such as agriculture infrastructure. Due to a lack of a distribution network, credit, and technical support services, the extent of seed and fertiliser dissemination is severely limited. On top of that, poor infrastructure, low milling rates (58% compared to the regional average 63-65%), inadequate storage and transport systems to the ports also prevent the sector from reaching its full potential. Anecdotal reports suggest that even large and rich farmers in areas where the rice economy is well-established are unsure of the best seeds to use or where to reliably purchase them.

Making Food In Myanmar
Myanmar - Food, Cereal & Livestock Production Index



Source: BMI, World Bank, Note: 1999-2001 = 100

Low mark-up on rice prices and the fact that Myanmar mainly exports low-quality rice also suggest a still-immature rice economy. According to a 2010 research study conducted by the Harvard Kennedy School, the farm gate to export price ratio for rice was less than 20%, as compared to the typical ratio of about 90%. Some of this can be attributed to the fact that rice out of Myanmar is mostly low quality (roughly 25% is broken rice). By building better infrastructure, improved milling capacity as well as wider dissemination of high quality seeds, this is an aspect which we believe holds much room for improvement.

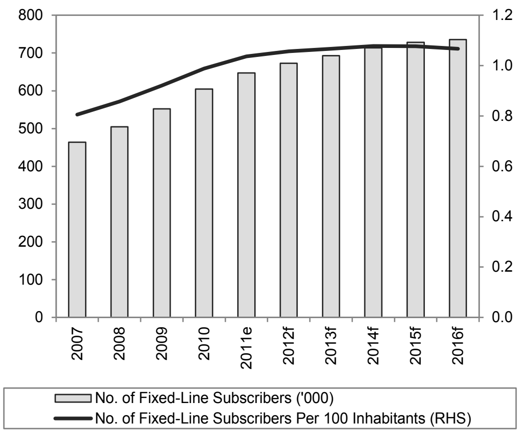
As infrastructure systems are continuously built up in the country and increased investment is channelled into the sector, we believe that there is much potential yet for agriculture in Myanmar to flourish and contribute robustly to economic growth in the foreseeable future.

Telecoms

Telecoms: Not For The Faint Hearted

BMI View: Years of isolation have had a detrimental effect on Myanmar's telecoms industry with a lack of investment and failure to keep pace with technological developments, which have caused the country to significantly lag behind regional peers such as Bangladesh, Thailand, Vietnam and Cambodia. A positive outcome following the by-elections in April 2012 could pave the way for liberalisation of the telecoms sector, thereby allowing investors to participate in the largely untapped growth opportunities. However, we foresee significant risks such as bureaucratic red tape, weak regulatory framework and a prolonged period of low profitability.

Growth Potential
Myanmar Mobile Subscriber Forecast

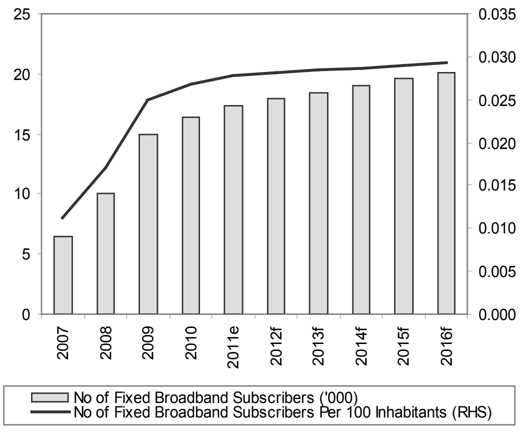


e/f = BMI estimate/forecast. Source: ITU, BMI

Market Overview

Under state laws, the government has the sole right to carry out economic activities in a number of sectors through state-owned enterprises. In the telecoms industry, this is done through the **Myanmar Posts and Telecommunications** (MPT). A lack of competition and investment, as well as the government's cautious attitude towards greater communication among its people (which could result in an Arab Spring or widespread reporting of protests such as the 2007 Saffron Revolution), has meant that telecoms penetration rates are amongst the lowest in the world.

Investment Would Push Growth Higher
Myanmar Fixed Broadband Subscriber Forecast



e/f = BMI estimate/forecast. Source: ITU, BMI

Obtaining up-to-date and reliable statistics about the Myanmarese telecoms market is a challenging task especially when the government limits information flow. According to the International Telecommunication Union (ITU), there were 604,700 mobile subscribers in Myanmar in 2010, representing a penetration rate of 1.26%. The fixed-line, internet and broadband markets were equally underdeveloped. Meanwhile, Myanmar's official data stated that there were 380,000 internet users in the country at the end of March 2011, up from

TABLE: MYANMAR TELECOMS HISTORICAL GROWTH

	2005	2006	2007	2008	2009	2010
Fixed-line subscribers ('000)	424.9	503.9	464.1	504.4	552.3	604.7
Fixed-line subscribers per 100 inhabitants	0.92	1.09	0.99	1.07	1.16	1.26
Mobile subscribers ('000)	128.7	214.6	247.6	367.4	502.0	594.0
Mobile subscribers per 100 inhabitants	0.28	0.46	0.53	0.78	1.05	1.24
Fixed broadband subscribers ('000)	0.2	4.0	6.5	10.0	15.0	16.4
Fixed broadband subscribers per 100 inhabitants	n/a	0.01	0.01	0.02	0.03	0.03

Source: BMI, ITU

28,610 in the previous year.

Services Beyond The Reach Of Consumers

The high cost of telecoms services could be seen as one of the government's means to restrict communication. According to Mizzima (a press media focusing on Myanmar news), installing a fibre cable in Yangon costs US$990 with a monthly fee of US$35-110. Consequently, most internet usage take place in internet cafes, which would also be easier for authorities to moderate and monitor internet usage

In January 2012, **Shwe Pyitagon Telecoms Company** announced that it plans to sell prepaid GSM SIM cards in denominations of MMK5,000, MMK10,000 and MMK50,000 from March 2012. The SIM cards would cost at least US$780 using the official exchange rate but about US$6 using the unofficial rate. The idea was met with scepticism from the MPT, which claimed that the MMK5,000 price line is unattainable given underlying costs, such as the deployment of network infrastructure and interconnection fees. MPT has claimed that a SIM card would need to cost at least MMK300,000 (or US$375 using the unofficial rate).

Regardless of whether Shwe Pyitagon Telecoms Company would successfully launch its affordable mobile service (Myanmarese laws prevent private companies from owning telecoms infrastructure, which is a vital part of Shwe Pyitagon Telecoms Company's plan since it plans to deploy its own), it has attracted the attention of consumers and businesses, and highlighted the possibility of cheaper services. In March 2012, MPT announced that it had reduced the cost of its 2G SIM cards to MMK200,000 from MMK500,000, while a 3G SIM card now costs MMK250,000. Nevertheless, with the price starting at US$250 (unofficial rate), this remains beyond the affordability of majority of the population. Meanwhile, a fixed-line connection costs MMK650,000.

Growth Opportunities Following Reform

In March 2012, the director-general of Myanmar's Post and Telecommunications Department, a division of the Ministry of Communications, Posts and Telegraphs, said that a new communications law is being studied for the creation of four telecoms licences, which will be available to local and foreign investors. The proposal was sent to the country's attorney general in February 2012. If approved, the law would be sent to the cabinet and subsequently, to the parliament. However, a deadline for the process to be completed has not been fixed.

The Myanmarese government has set a target of 50% mobile penetration by 2015, according to the Wall Street Journal citing **Nomura**. Officials aim to introduce **Research In Motion**'s BlackBerry services as early as 2014, in time for a regional meeting of the Association of Southeast Asian Nations.

Consumer Front

With a population in excess of 60mn, Myanmar harbours significant growth opportunities in light of the low penetration rates. The high cost of telecoms services has generated a significant level of pent-up consumer and enterprise demand. Furthermore, Myanmar has a literacy rate of 90% and at least 5mn English speakers nationally (most of whom live in Yangon), which makes the market even more attractive. Assuming the situation in Myanmar's telecoms sector remains status quo, we forecast 946,000 mobile and 20,150 fixed broadband subscribers by end-2016. However, we highlight that there are significant upside risks if the MPT continues

TABLE: MYANMAR TELECOMS SUBSCRIBER FORECASTS

	2009	2010	2011e	2012f	2013f	2014f	2015f	2016f
No. of fixed lines ('000)	552	605	647	673	693	714	728	735
No. of fixed lines per 100 inhabitants	0.92	0.99	1.04	1.06	1.07	1.08	1.08	1.07
No. of mobile phone subscribers ('000)	502	594	689	772	841	892	927	946
No. of mobile phone subscribers per 100 inhabitants	0.84	0.97	1.10	1.21	1.30	1.35	1.37	1.37
No. of broadband subscribers ('000)	15	16	17	18	18	19	20	20
No. of broadband subscribers per 100 inhabitants	0.03	0.03	0.03	0.03	0.03	0.03	0.03	0.03

e/f = BMI estimate/forecast. Source: ITU, BMI to lower tariff rates and if reform materialises.

Businesses

Liberalisation of the economy would also drive demand for ICT products and services including mobile devices, desktop computers and modems from businesses. We believe that the MPT and its telecoms infrastructure would be ill-equipped to handle the surge in traffic. Myanmar would require low-cost network equipment that would be reasonably future-proof.

Like the broader economy, the telecoms sector has been dependent on Chinese firms. China's **Beijing Xinwei Telecom Technology Company** signed an agreement with **Myanmar Link Global Company** in early November 2011, which will see the former's wireless technology expand its broadband service coverage that is currently only available in Myanmar's three main cities–Naypyidaw, Yangon and Mandalay. Meanwhile, Chinese vendors **Huawei Technologies** and **ZTE** signed an agreement with the Myanmarese government in September 2011 to sell telecoms equipment such as mobile devices. Western vendor **Alcatel-Lucent** was also contracted by MPT in 2006 to build a telecoms network but this was done through its Chinese subsidiary **Alcatel-Lucent Shanghai Bell** and financed by the Chinese government.

The Myanmarese government's interest in reducing its reliance on Chinese firms could favour other international companies such as Sweden's **Ericsson** and Finnish-German **Nokia Siemens Networks** when awarding telecoms infrastructure contracts, although companies would still need to match Chinese companies' pricing.

Risks: The Long And Winding Road

BMI acknowledges the growth prospects of Myanmar telecoms industry, although we highlight that there are significant risks and obstacles. Weak regulatory frameworks have long hampered the attractiveness of several telecoms markets in emerging Asia.

Foreign companies such as UAE-based **Etisalat**, Norway's **Telenor** and the **Bahrain Telecommunications Company** were badly affected by the 2G licence scandal in India, and they had to write-down millions in investments.

In Bangladesh, the regulator has been trying to squeeze more revenue from the telecoms operators, many of which are backed by international players, in light of the high growth rates in the sector in the past few years.

South Korea's **SK Telecom**, Hong Kong's **Hutchison Telecommunications International** and Russia's **VimpelCom** (which bought the operation from Luxembourg-based **Millicom International Cellular**) have struggled to erode the dominance of Vietnam's two state-owned telecoms operators. Attempts to privatise the state entities have made little progress.

Cambodia's Ministry of Posts and Telecommunications (MPTC) continues to issue mobile licences in spite of the fact that there are 10 operators, some of which have yet to launch services. At present, the MPTC is still trying to form an independent telecoms regulator.

Thailand took many years before establishing the National Broadcasting and Telecommunications Commission (NBTC), which is finally in compliance with the country's constitution. However, the NBTC has yet to resolve past disputes and issues arising from its predecessor.

Establishing a clear and robust telecoms regulatory framework overlooking key issues such as allocating spectrum is a challenging task for a country that has been left behind by the rest of the world. While Myanmar could seek help from international bodies such as the ITU, implementing policies without the influence of government agendas, cronyism and corruption is an entirely different issue.

Consumer Story To Play Out After Infrastructure Is Laid

The telecoms sector is particularly reliant on the availability of affordable and reliable electricity. Consequently, we see that the Myanmar consumer story will only start to play out after the necessary infrastructure has been deployed, which will not happen in the near future, in addition to a significant improvement in consumers' purchasing power (or a drastic decline in telecoms tariff rates). Telecoms companies looking to enter the Myanmarese market must be prepared for a prolonged period of weak financial performances. Telenor's Pakistan unit reported five years of operating loss before generating an operating profit of NOK3mn (US$530,000) in 2010. In return, companies have the opportunity to secure a strong foothold in a nascent market with strong growth potential.

Local Partnership Is The Way Forward

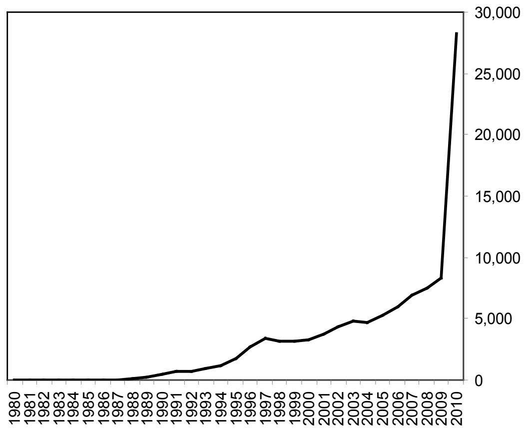
We do not foresee the Myanmarese government going from years of isolation to complete liberalisation in a short timeframe. Foreign participation will come in the form of partnering with the Myanmarese government (or state-owned investment vehicles) and local firms. The former model would enable the government to retain a certain degree of control and generate revenues, while the latter would bolster the local labour market and help in the transfer of technology and knowledge. From foreign companies' point of view, it would simply be part of the cost of operating in a high-growth market that is in the midst of reforms. By partnering with the government or domestic firms, foreign companies could benefit from having local expertise and less red tape.

A New Autos Hub In SE Asia?

BMI View: BMI believes there is considerable potential for carmakers in a market with a very low level of penetration and one of the world's oldest vehicle fleets. However, price will be an issue in a country with a relatively low GDP per capita, and efforts to increase imports of newer second-hand cars could pose threats to the uptake of new vehicles.

Reform Paying Off

Myanmar - Stock Of Foreign Direct Investment, US$mn



Source: BMI, UNCTAD, Myanmar CSO

Japan's **Suzuki Motor** has revealed plans to recommence vehicle production in Myanmar, as the government makes a concerted effort to replace one of the world's oldest vehicle fleets. There is incredible potential for carmakers in a market of nearly 60mn people, where only 370,000 cars were registered as of August 2011. However, price will be the prevailing issue in a country with a GDP per capita estimated at less than US$500 and local production could offer Suzuki some competitive advantage here.

Suzuki is considering restarting the plant of its former joint venture (JV), which operated between 1999 and 2010, until its business licence expired. Production was limited, however, as the company assembled around 6,000 vehicles and 10,000 motorcycles in that time, according to the Straits Times. Part of the issue was that only leading military figures were in a position to acquire new vehicles.

With political and economic reform gaining momentum, however, the autos sector has become an area of focus with a scheme to promote the purchase of newer vehicles. Along similar lines to the 'Cash for Clunkers' and scrappage schemes implemented in the US and Europe, the government is offering import permits in exchange for vehicles that are 40 years old or more. The replacement vehicle must have been made in 1995 or later to qualify.

The scheme is being handled in stages, with cars of 40 years or more processed first between September and October 2011, followed by cars of 30-40 in November and December. Cars of 20-30 years have been processed during Q112, which leads **BMI** to believe that at this rate of progress, it could take time for a rapid uptake in brand new vehicles. For carmakers trading in their own second-hand cars, however, there are clearly opportunities.

Indeed, the government has also stepped in to encourage carmakers from Japan, China, Thailand and South Korea to set up showrooms in the country to improve consumer access to their new and used vehicles. Japanese brands could have the biggest advantage, following an agreement by Japan to provide fresh yen-denominated loans to Myanmar, in what **BMI**'s Asia team believes is a bid to assist Japanese firms in re-entering the Myanmar market.

Keen to take advantage, Suzuki is looking for a local partner to bring capital to a new domestic assembly business. The company already has a facility in Yangon from its previous JV, in which it held a 70% stake and has the option of bring the plant back into operation. There is the potential for similar such projects by Japanese companies, as the strong yen forces them to find other more cost-effective production bases in the region. The downside risk, however, when calculating costs, is Myanmar's peculiar dual-rate foreign exchange system.

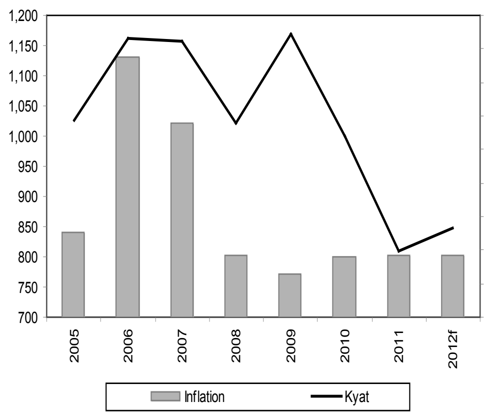
Nevertheless, Asian brands look set to steal a march as purchases of newer vehicles start to gather steam. Their US and European rivals will be held back by Western sanctions, although there have been positive signs on this front. A landmark visit by US Secretary of State Hillary Clinton in November 2011 and the news in January 2012 that the EU discussed providing financial aid worth EUR150mn (US$195.2mn) to support political reforms are indications of improving relations. For further progress to be made, much will depend on how the elections of April 1 2012 are conducted.

Banking Sector

Potential Reward, Definite Risk

BMI View: Although Myanmar's banking system remains extremely underdeveloped, opportunities for rapid growth may abound in the case that the country is able to maintain its recent reform drive and build confidence among international investors and domestic individuals alike. Still, with a decades-long legacy of myriad banking crises, inept governance, corruption, and general mismanagement, the sector will have a difficult time gaining the trust of the public to the point where it can play a constructive role in the development of the country at large. Key risks stem from an obsolete dual-rate exchange system, ongoing sanctions from the US and EU, and a considerable lack of banking and financial expertise within both the public and private sector.

Strength, But Not Necessarily Stability
Myanmar - Unofficial MMK/US$ Exchange Rate & CPI



Source: BMI

Ghosts Of The Past

It is estimated that only one million Myanmarese, or about 2% of the total population, hold bank accounts. Not only is the populace largely impoverished, with a per capita GDP of just US$890, but the nation has been so beset with banking crises since declaring its independence in 1948 that even those with a material amount of wealth often choose to either keep it in banks overseas or on their private property. The most recent of these crises unfolded in 2003, when inaccurate rumours of insolvency among a few private banks spread to the point of a full-scale panic, causing a liquidity crisis large enough to destroy even the soundest of banks.

Compounding the crisis was a ham-fisted response from the government when the Central Bank of Myanmar (CBM) instituted wide-ranging, yet uneven, account withdrawal limits and halted all account transfer transactions, further stoking the public's fear that their deposits were not safe. Prior to the crisis, the country's private banking sector had been experiencing healthy growth, and private banks were beginning to challenge the dominant state banks for share of banking activities and deposits. However, the crisis crushed private banks, as national demand deposits fell from MMK291.1bn (US$45.5bn) to just MMK84.2bn from 2002 to 2003. Following the crisis, banks ceased issuing credit cards, and ATM machines disappeared.

Finally A Light At The End Of The Tunnel?

A decade on, private banks are once again looking to gain a foothold in Myanmar. In the run up to 2010's general elections, the government began to liberalise the banking sector, allowing for a number of new private banks to be formed. Four of the newest banks – **Asia Green**, **Myanma Apex Bank**, **United Amera**, and **Ayeyarwaddy** – are owned by four of Myanmar's largest tycoons (all of whom are targeted by either US or EU sanctions) with deep government connections. These banks were formed prior to the 2010 elections, indicating that the tycoons were eager to get a jump on the market before liberalisation plans began to come to fruition. Since then, some welcome reforms have been seen. Private banks have once again been given permission to run ATM machines in Yangon, although credit cards remain anathema.

Not So Fast

Despite an improving political and economic backdrop, however, risks remain high. Local banks are likely to receive very preferential treatment, and those with crony connections will continue to be given the inside line. The regulatory environment is basically non-existent, and the government's inner workings, as well as its framework for foreign investment, are extremely opaque. Strict sanctions from the US and EU have not yet been lifted, although there is hope that the process may begin in earnest if by-elections slated for April 1 go smoothly. Sanctions currently place severe limitations on the ability of European, Australian, and American business interests to invest in Myanmar.

Business in Myanmar is still struggling under the yoke of an unwieldy dual-rate exchange system that complicates transactions and casts a pall over the kyat. While the official rate for the kyat stands at MMK6.434/US$, the unit unofficially trades closer to MMK810/US$. Government officials and well-connected business interests have in the past used the official exchange rate to underreport export earnings, but it has seen little use outside of this.

Searching For A Stable Kyat

For the banking sector to gain any sort of credibility, the exchange rate system will first need to be solved. The government has been in consultations with the IMF, World Bank, and ADB in an effort to construct a plan to unify the exchange rates. If and when such a plan goes into action, it is likely that the currency's value will reflect the unofficial rate more closely than the official rate. However, as it is now, stability will be a key issue, as Myanmar lacks the currency reserves (estimated at about US$6bn, or approximately 12% of the economy) and personnel expertise to effectively manage a fledgling currency.

Small currency reform efforts have already been noted in Yangon, where the limit for exchanging US dollars for kyat at the unofficial rate was recently raised from US$2,000 to US$10,000. Demand for the kyat, however, has been perhaps too strong, with reports of a kyat shortage emerging. Strong demand for the kyat has pushed the currency's value up approximately 20% since 2009, pressuring small Myanmar exporters who price their wares in dollars, but require kyat to conduct business domestically.

More Structural Headaches

Furthermore, only about 15% of domestic credit makes its way into the private sector, meaning that banks are still largely a piggy bank for the government. Myanmar's agricultural sector, in the past the largest in Asia, has wilted in the absence of said credit, of which it commands less than 1%. Anecdotal evidence indicates that private citizens find it nearly impossible to get credit from banks for anything from small business loans to mortgages, severely stifling economic activity and undermining the country's growth potential.

A reformed banking sector could change this, but it will be a long, arduous process. There is no doubt huge economic potential in Myanmar based on its attractive mix of a large, relatively literate population, an embarrassment of natural resources, and a geographical location that is rising in importance by the day. Indeed, over the medium term, the growing presence of international banks may place pressure on local banks to more aggressively pursue market share, which could mean a greater drive to build a functional consumer banking environment. However, banks will be challenged to overcome an innate suspicion of the sector based on Myanmar's unique history, something that will also take time to change. Combined with the still considerable political risks that will be inherent for firms doing business in Myanmar even in the event that the government's reform drive powers on, the banking environment will remain a difficult (though potentially lucrative) one for the foreseeable future.

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