



# Foreign Direct Investment (FDI) Environment in Myanmar – Critical Factors

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## **Abstract**

*After years in the economic exclusion, Myanmar is recently gaining attention from Western countries and Japan. Speculation is gathering that Myanmar is about to see more and more economic and political reforms and with that increase of Foreign Direct Investments (FDI). Though Western economic restrictions existed, the data over 20 years, since government introduced a market-oriented FDI law in 1988, shows that there were other countries that were willing to invest in Myanmar due to various factors. While Myanmar's yearly FDI data is available from government sources, the authors found that they differ with the FDI data available from World Bank. Using data from both sources, the paper attempts to identify what factors had played any significant role in attracting FDI to Myanmar over the 20 year period for which data is available. Though researchers had attempted rationalizing Myanmar's FDI situation using descriptive arguments, this paper is the first to use empirical data and a thorough statistical analysis. While the analysis found that key economic factors play a justifiable role in the amount of FDI that Myanmar received, political risk had a significant negative impact. The paper also makes a brief comparison of Myanmar's FDI situation with Vietnam.*

## **INTRODUCTION**

It is widely accepted that the foreign direct investment (FDI) is very crucial for the economic development of a nation. FDI is especially crucial for developing and least developed countries (Proksch, 2003). According to the World Investment Report 2011, "Foreign direct investment is a key component of the world's growth engine."

United Nations had categorized Myanmar as one of the least developed countries; as such poverty eradication and economic development is very important for Myanmar. Given Myanmar's economic performance, over many decades, FDI can be the only choice for Myanmar to achieve the flow of capital, technology and other opportunities from the rest of the world.

Therefore, Myanmar has carried out a series of FDI development initiatives: (1) adoption of market oriented economy, (2) passing FDI related laws, (3) encouraging private investment and entrepreneurial activity, (4) taking necessary action for promotion of foreign investment, (5) opening of the economy for foreign trade and investment and



(6) establishing economic zones. In addition, as a member of Association of Southeast Asian Nations (ASEAN), Myanmar had signed the Framework Agreement on the ASEAN Investment Area to collaborate with the member countries and to enhance free flow of investment into Myanmar.

The roots of Myanmar's attempt to attract FDI can be traced back to the FDI Law that the country adopted in 1988 (ASEAN, 2004).

Although Myanmar has tried to enter into the integrated economic world by making many initiatives and enacting laws, trade sanctions of the U.S and its allies, following the military takeover of the country, since 1988, have deterred the Western FDI coming to the country.

Since 2010, following an election conducted under a new constitution, Myanmar has started various political reforms, including the release of democracy advocate and the leader Ms. Aung San SuuKyi of key political party National League for Democracy (NLD). The government of reform-minded President Thein Sein has "*doubled*" the efforts to attract FDI "*as a way to help develop the country fast*" (Robinson, 2012). In this regard, it is necessary for Myanmar to study the key factors that help attracting FDI.

Though not extensive in terms of numbers, the researchers have studied about Myanmar FDI, including FDI relations between Myanmar and ASEAN (Khine, 2008), and Trade, Foreign Investment, and Myanmar's Economic Development during the Transition to an Open Economy (Kudo and Mieno, 2007). A review of Myanmar's past perspective on FDI and why the country was late compared to some other Asian neighbors such as Malaysia, Singapore, and Thailand, are comprehensively discussed in Thein, 2004. However, none of the existing studies provide an empirical analysis with actual data. Khine, 2008, presents descriptive analysis with graphs and tables.

Perhaps one reason for lack of empirical studies is the availability and credibility of data, especially the FDI data. The Central Statistical Organization (CSO), which comes under the Ministry of National Planning and Economic Development of Myanmar government, has been publishing FDI data since 1989. However the government data and the FDI data published by World Bank through its economic database of all the countries are not in complete agreement. For a thorough analysis of FDI and to find out the possible factors, one needs many other data, such as Gross Domestic Product (GDP), labor force, education level etc. as well. One has to spend considerable time and effort to collect such data because of the non-centralized way of making data public in Myanmar.



Myanmar, as a least developed country, still confronts a number of problems including transportation, infrastructure, electricity supply, and currency convertibility issues, to name a few. Political factor of course has been a barrier because it had been one of the root causes for the economic sanctions. Often, researchers site such factors as playing key role in attracting FDI (Asian Development Bank, 1997, and Neuhaus, 2006).

The statistical analysis of the FDI data of Myanmar, carried out in this paper, started with about twenty factors that were normally cited by the past researchers as important (Proksch, 2003, Neuhaus, 2006, Khine, 2008). However, preliminary analysis excluded many such due to lack of statistical significance or due to lack of complete data.

The paper first reviews the Myanmar's FDI history, with an overview of FDI legal system. This is to be followed by a description of the key variables that are considered for analysis within explanation of the statistical model that would be tested for finding the key factors effecting FDI inflows to Myanmar. Two models-- one with Myanmar government data from CSO and another with World Bank data -- are tested. The paper then reviews the statistical results.

Following the rationalization of the statistical results, a comparison is made with the FDI situation in Vietnam. The comparison perhaps makes better sense when one understands the fact that Vietnam was also under Western economic embargo for almost 20 years until US sanctions were lifted in 1994.

The conclusion at the end summarizes the key findings of the paper.

## **MYANMAR'S FDI HISTORY**

After the revocation of centralized planning economic system, Myanmar transformed its economy into market oriented system in 1988. To become a more liberalized economy, the government allowed foreign direct investment and encourages the private sector development. The Union of Myanmar Foreign Investment Law (FIL) was promulgated in November 1988 and its procedures were prescribed in December 1988. The Myanmar Investment Commission (MIC), which is the initial approving authority for investment proposals, was responsible for overseeing and administering the foreign Investment Law.

Myanmar's foreign direct investment policy is a component of the overall restructuring and development policy of the Government. The main components of the policy are:

- Adoption of market oriented system for the allocation of resources.
- Encouragement of private investment and entrepreneurial activity.



- Opening of the economy for foreign trade and investment.

To undertake and implement Myanmar foreign investment policy successfully, the FDI law has been adopted with the following objectives:

- a) promotion and expansion of exports,
- b) exploitation of natural resources, which require heavy investments,
- c) acquisition of high technology,
- d) supporting and assisting production and services involving large capital,
- e) opening up of more employment opportunities,
- f) development of works which would save energy consumption, and
- g) Regional development.

Indeed, Myanmar's economic policies have changed between market system and socialist system alternately. Myanmar practiced open economic system from 1948 to 1962. Then it has been in the socialist system for more than twenty years even resisting FDI completely. Myanmar transformed to open market system again in 1988 and practiced many reforms for overall economic development of the country. Among these reforms, the initiatives to attract foreign investment had been the government's priority and it adopted the following acts and laws for investors to do business in Myanmar:

- 1) Myanmar Company Act (1914)
- 2) Special Company Act (1950)
- 3) Myanmar Companies Regulations (1957)
- 4) Myanmar Companies Rules
- 5) The partnership Act (1932)
- 6) The Republic of the Union of Myanmar Foreign Investment Law
- 7) Myanmar Citizen's Investment Law (1994)
- 8) The Myanmar Special Economic Zone Law (2011)

Myanmar Foreign Investment Law allowed 100% foreign equity ownership for foreign investors, with a minimum amount of foreign capital US\$ 500,000 for an industry and US\$ 300,000 for services. A tax holiday of three years and exemption of customs duty and other internal taxes have granted on imported capital equipment and materials. MIC also provides various other incentives, along with guarantees against nationalization for enterprises operating under the FDI Law.

**Figure 1: Major FDI Countries (1989-2010) (Source: CSO, Myanmar Government)**

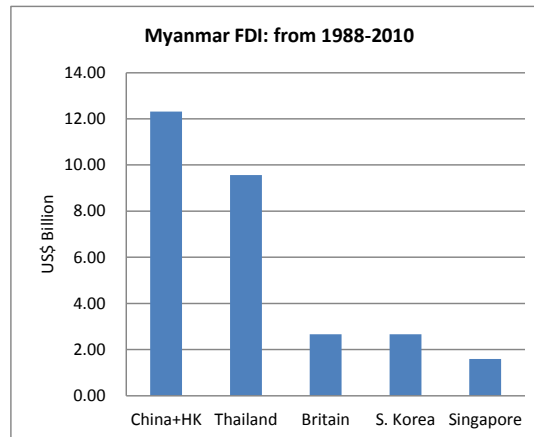


Figure 1 shows the major FDI countries in Myanmar; up until July 2010, China accounted for more than one third of the total FDI of US\$ 32 billion. Though Myanmar government has some preferred areas for FDI investment, the most particular sectors invested by the foreign countries had been in power, oil and gas, manufacturing, hotel & tourism, real estate, and construction. For example, of China's investments, \$4 billion has gone to power and energy sectors while rest gone to oil, gas and mining,

To get around the infrastructure problems and attract other industries, such as manufacturing and information and telecommunications technology, Myanmar government has started developing Special Economic Zones (SEZs).

While Myanmar has been taking many initiatives to attract FDI, the events unfolding at present – US and its allies, including Japan, lifting of most of the economic sanctions – had prompted unprecedented interest by business and the investor community. This perhaps underscores the one of the most critical factors important for attracting FDI – The political stability and respect for democracy. However, analyzing empirical data requires a reasonable measure for accounting for such; in this regard, this paper included the “political risk” as one of the factors to be considered in the statistical model and the data analysis part to be explained in detail next.

### **FDI DATA ANALYSIS**

The purpose of this study is to examine the factors that had historically affected the FDI inflows to Myanmar. In order to study the causal relationship between, linear regression models will be used. Though twenty some variables were initially considered, it turned out that many variables did not show statistical significance. Among the time-series data, growth of trade, total labor force, political risk, inflation, exchange rate, population growth rate and export were selected to be



investigated in detail. It should be noted here that while most of the factors taken into consideration are economic in nature, the political risk is not. But, in FDI decisions, political risk can be a factor as well, as discussed by Hayakawa et al, 2011.

### Statistical Model

Since there is a little inconsistency of Myanmar FDI data between Central Statistical Organization (CSO) Myanmar and World Bank within the period which this paper is investigated, the data from both World Bank and CSO are used separately. This way the results obtained from two data sources can be comparatively analyzed.

The first equation for the Myanmar's investment flow analyzed with the World Bank data will be constructed based on the independent variables of the growth of trade, total labor force, political risk, inflation and exchange rate, which are obtained from other sources.

The data considered in the analysis are defined as follows:

$FDI_{t(WB)}$  = foreign direct investment flow into Myanmar (World Bank data)

$FDI_{t(CSO)}$  = foreign direct investment flow into Myanmar (CSO data)

$EXPOR_t$  = export from the host countries to the world

$GT_t$  = the growth of trade

$POLITIRIS_t$  = political risk

$Totallab_t$  = total labor force

$POPGR_t$  = population growth rate

$INF_t$  = inflation

$EXC_t$  = exchange rate

The model with World Bank FDI data for Myanmar is represented by the following Linear Regression Model (LRM):

$$FDI_{t(WB)} = \beta_0 + \beta_1(GT_t) + \beta_2(Totallab_t) + \beta_3(POLITIRIS_t) + \beta_4(INF_t) + \beta_5(EXC_t) + u_t \dots (1)$$

Similarly, by using CSO data of investment flow, the LRM equation (2) will be constructed with the same independent variables as in equation (1):

$$FDI_{t(CSO)} = \beta_0 + \beta_1(GT_t) + \beta_2(Totallab_t) + \beta_3(POLITIRIS_t) + \beta_4(INF_t) + \beta_5(EXC_t) + u_t \dots (2)$$



All independent variable data of Myanmar for the period (1989-2010) were obtained from various reliable data sources. The growth of trade is obtained from calculation: the difference of final year total trade and initial year total trade divided by final year total trade. Export and import data is obtained from the Directorate of Trade (DOT), an organization under Myanmar government. Population growth rate and inflation are obtained from World Bank. Political risk data is obtained from the International Country Risk Guide Annual, published by the PRS Group., Inc. All data used is annual and covers period from 1989 to 2010.

### **Empirical Results**

After getting all the data assembled, the analysis was done using the statistical package Stata. The estimation of the regression result is shown in Appendix 1.

In the Myanmar (World Bank) data analysis, the LRM analysis (Equation 1, model) shows that total labor force, exchange rate and inflation are significant factors for the investment flow. Although total labor force is helping the flow of FDI, inflation and exchange rate are reducing the investment flow. There are no effect of political risk and the growth of trade in this result. By analyzing Myanmar (World Bank) investment flow, therefore, it can be concluded that political risk and the growth of trade are not significantly important for Myanmar FDI inflow.

However, the same LRM analysis using Myanmar's CSO data for FDI (Equation 2, model) showed an interesting result. In this analysis, the political risk becomes significant, in addition to the factors that were significant in former analysis with World Bank data -- labor force is helping the flow of FDI, while inflation and exchange rate are reducing the investment flow. In addition, the effect of political risk is negatively significant as expected.

Accordingly, significance political risk varied based on the data sources. However a close look at the Stata result in Appendix 1 shows that even with World Bank data, the effect of political risk on FDI is still negative. Table 1 shows the investment flow of Myanmar's FDI obtained from the two sources, World Bank and CSO (Myanmar Government).

For both result, total labor force is the catalyst for development of investment flow. Inflation, exchange rate and political risk are the impendence factors for Myanmar's foreign investment flow. However, political risk is not significant in Myanmar (World Bank) investment flow analysis. According to this finding, the conclusion can be drawn that the importance of political risk is changing based on the sources of data. The growth of trade is also not important in both models.



**Table 1 The FDI flow of Myanmar from two sources, World Bank and CSO**

Year	US \$ Million	
	World Bank data	CSO data
1989	7.890	449.487
1990	162.788	280.573
1991	240.411	5.893
1992	173.340	103.785
1993	105.745	377.184
1994	126.910	1352.295
1995	279.922	668.166
1996	313.413	2814.245
1997	390.814	777.394
1998	317.834	54.396
1999	255.618	58.150
2000	258.266	217.688
2001	210.318	19.002
2002	152.085	86.948
2003	251.452	91.170
2004	213.548	158.283
2005	237.243	6065.675
2006	278.634	719.702
2007	257.686	205.720
2008	283.455	984.764
2009	322.976	329.580
2010	756.323	19998.965

*Source: World Bank, CSO(Myanmar)*

Although Myanmar has faced trade sanctions from western countries, it still conducted considerable trade with neighboring countries, particularly China, whose economy had been growing rapidly. This perhaps provides a reasonable explanation as to why growth of trade became unimportant in both models.

#### **MYANMAR VS. VIETNAM**

However, Myanmar's FDI is still not up to its potential. With sizable natural resources, such as oil, gas, minerals, and agricultural land, Myanmar had great potential. One way to look at Myanmar's FDI situation is to compare it with Vietnam, a country which also suffered from US-led economic sanctions for twenty years, until 1994.

The comparison of foreign investment flow into Myanmar and Vietnam is provided in table 2, with and figure 2

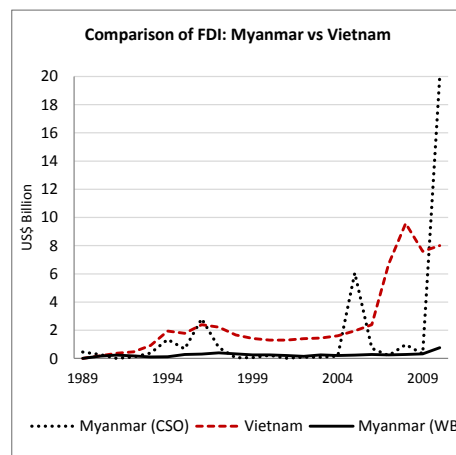


**Table 2: Comparison of FDI inflow into Myanmar and Vietnam (1989-2010)**

Year	Myanmar (US\$ Million )	Vietnam (US\$ Million)
1989	449.487	4.070
1990	280.573	180.000
1991	5.893	375.190
1992	103.785	473.946
1993	377.184	926.304
1994	1352.295	1944.516
1995	668.166	1780.400
1996	2814.245	2395.000
1997	777.394	2220.000
1998	54.396	1671.000
1999	58.150	1412.000
2000	217.688	1298.000
2001	19.002	1300.000
2002	86.948	1400.000
2003	91.170	1450.000
2004	158.283	1610.000
2005	6065.675	1954.000
2006	719.702	2400.000
2007	205.720	6700.000
2008	984.764	9579.000
2009	329.580	7600.000
2010	19998.965	8000.000
Total	35819.065	56673.426

Source: Myanmar (CSO), Vietnam (World Bank)

**Figure 2: Comparison of FDI inflow into Myanmar and Vietnam (1989-2010)**



Source: Myanmar (CSO, WB), Vietnam (WB)

Though recent figures show sudden upsurge of FDI into Myanmar, historically Vietnam had received consistent inflow of FDI, especially since 1994, when US lifted economic sanctions. Somewhat unaffected by US, is the intra-ASEAN FDI; in 2008, the



figures show Vietnam attracting almost 10 times the FDI that Myanmar received, ASEAN Statistical Year Book (2008).

Vietnam had achieved high GDP growth in recent years based on the power of FDI. Its economic development comes from the contribution of foreign investment inflow (Anwar and Nguyen, 2010, 2011, Nguyen, 2010, and Nguyen, Vu, et al, 2006).

Because of the Multinational Corporations' export and import to international market, Vietnam's trade with the world has increased. As Vietnam's foreign investment flow is larger than Myanmar, the export and import volume of Vietnam became larger than Myanmar; particularly, export became a key factor of Vietnam's FDI. Table 3 shows the comparison of trade in Myanmar and Vietnam, respectively.

**Table 3 Export and Import Comparison between Myanmar and Vietnam (US\$ Million)**

Year	Myanmar		Vietnam	
	Export	Import	Export	Import
1998	-	-	-	-
2000	1,194	2,219	-	-
2003	4,464	1,843	-	-
2008	6,621	3,795	61,778	79,579
2009	6,341	3,850	56,691	69,231
2010	7,600	4,199	72,192	84,801

*Source: ASEAN Community in Figures 2011*

## CONCLUSION

The paper discussed Myanmar's attempts at attracting FDI since the country enacted its first FDI law in 1988. Though Myanmar faced Western and Japanese economic sanctions soon after 1988, it managed to receive some FDI from few countries, particularly China, Thailand, and Korea. Thorough there are descriptive research on FDI inflows to Myanmar, this paper is the first attempt to make an empirical study to understand the key factors related to the FDI inflows to Myanmar.

The FDI data for Myanmar can be found through two sources: one is World Bank; the other is Central Statistical Organization (CSO), a Myanmar government organization. However the data do not match. This prompted the authors to conduct two sets of data analysis, using the two sources of data. The factors that showed significantly effecting FDI inflows included total labor force, exchange rate, and inflation are significant factors. The reason for these perhaps can be intuitively explained, as it turned out that total labor force is helping the flow of FDI, inflation and exchange rate are reducing the investment inflow.



The more interesting result of the study perhaps is the impact of political risk. Both data from World Bank and CSO showed (Appendix 1) political risk's negative effect on FDI. Statistically though, the Stata analysis indicated that the level of significance is significant (at 1% level) only for Myanmar government's own data. Given the political changes that Myanmar is undergoing at present, one could make a good case in support of government's initiatives as they reduce political risk, thereby helping attracting more FDI.

The paper also looked at FDI situation for Vietnam, as both countries lived through two decades of US-lead economic sanctions. Though Myanmar's population is considerably smaller than Vietnam's, Myanmar has almost three times the land area and the country is rich in terms of resources. Yet, Vietnam had consistently attracted considerably more FDI, especially after the lifting of sanctions in 1994. Vietnam's case too could prove to be positive news for Myanmar.

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## APPENDIX

### Appendix 1: Regression Result of FDI flow into Myanmar (1989-2010)

Dependent Variable: (FDI)		
Independent Variables	Myanmar (World Bank Data)	Myanmar (CSO Data)
$\beta_1$	-85.443 (394.765)	-7799.878 (9257.156)
Expor	-	-
GT(growth of trade)	17.042 (56.982)	-843.879 (1336.209)
Total Laborforce	48.056 *** (8.361)	1867.838 *** (196.056)
POLITIRIS	-0.444 (1.278)	-107.026 *** (29.977)
EXC	-120.061 * (62.751)	-4531.777 *** (1471.485)
INF	-0.130 ** (0.056)	-6.099 *** (1.303)
POPGR	-	-
* Significant at 10% level ** Significant at 5% level *** Significant at 1% level		

The numbers within parenthesis represent the Standard Error associated with the respective regression coefficient. The output is based on Stata statistical package.