Influx of Foreign Direct Investment into Myanmar

Dr. Khin Thida Nyein
Professor, Department of Economics, Monywa University of Economics

Abstract: This study aims to investigate the reasons for the fluctuation of the inflows of direct foreign investment into Myanmar. Employing the data on the influx of foreign direct investment into the country from 1989/90 to 2016/17, the possible causes of increasing and decreasing inflows of FDI into Myanmar are observed. According to this study, the factors such as Asian economic crisis, U.S federal sanctions, lack of infrastructure (particularly poor electric power condition), weak telecommunication services and expensive charges, unstable macroeconomic environment, frequent changes of rules and regulations and lack of transparency in its administration over the study period may be the reasons for the fluctuation of FDI inflows into the country. The existence of such factors may be difficult to encourage the willingness of foreign entrepreneurs to invest. If these factors fade, therefore, the inflows of direct foreign investment into Myanmar are likely to improve. The volume of FDI into Myanmar enormously increased in 2010/11; the reason may be the removal of economic sanctions at that time. The findings of the paper suggest that the authorities should strive to sign a large number of bilateral investment treaties (BITs), and the country should consider giving more priority to cooperative frameworks, encourage inter-regional trade and investment linkages instead of attracting FDI individually and competitively.

Keywords: FDI, Market Size, Exchange Rate, Inflation Rate, Openness

I. Introduction

1.1. Background

Every government of many nations has been trying to achieve direct investments from foreign countries. The reason is that foreign direct investment (FDI) provides many beneficial effects to host countries such as the promotion of employment, the improvement of human resources, the transfer of superior technology, and so forth. All of these factors contribute to development of a nation's economy, and enhance welfare of the citizens. Many theoretical literature states that many variables such as market size, degree of development, labor cost, economic growth, openness, trade barriers, trade balance, exchange rate, tax, natural resource variables, infrastructure development, macroeconomic stability, political instability, return on investment in the host country, human capital and Bilateral Investment Treaties are the determinants of direct foreign investment inflows. With an effort to stimulate direct investment from foreign countries, the governments of many developing countries have been offering several effective national and international policies to be their investment environment more attractive for foreign investors. These policies were privatization, trade openness, providing attractive incentives and so forth. Myanmar has also been trying to achieve foreign direct investments by using several attractive incentives. This paper presents both several attractive incentives for achieving foreign direct investments and the situation of foreign direct investment in Myanmar.

1.2 Aim of the Paper

This study examines the inflows of direct foreign investment into Myanmar in the 1989-2017 periods. This study will try to determine the reasons why the volume of FDI inflow into Myanmar has fluctuated significantly. The finding of the paper will be expected to aid the authorities in conducting the next step as an attempt of encouraging the inflows of direct foreign investment into the country.

1.3 Structure of the Paper

The structure of the paper is designed as follows. Part I introduces background, aim of the paper and structure of the paper. Some variables that determined the influx of foreign direct investment into the countries are reviewed in Part II. Part III provides Myanmar investment environment, and the situation of foreign direct investment in Myanmar is described in Part IV. The last part is a brief discussion about findings, and suggests some comments which may be useful to the authorities of the country.
II. Literature review

A number of empirical studies which have analyzed the determinants of foreign direct investment inflow (FDI) have been conducted by a number of scholars. There are many variables which determine direct foreign investment inflows according to many scholars and researchers. Among many variables in determining FDI inflows, market size, usually measured by gross domestic product or per capita GDP in considering actual market size, is a significant determinant of FDI flows. There is a strong and positive relationship between market size and FDI inflows, especially for market seeking FDI, which aims to set up enterprises in a particular country to supply goods and services to the local market. (Schmitz & Bieri (1975), Swedenborg (1979), Dunning (1980), Kravis & Lipsey (1982), Culem (1988), Sader (1993)) As potential market size, growth rate of GDP is considered by many scholars. Bandera & White (1968) and Culem (1988) reported a significantly positive impact of growth on FDI.

A number of empirical studies analyzing the fact that exchange rates affect FDI flows include Cushman (1985), Froot and Stein (1991) and Kohlhagen (1977). Depreciation of the host country's currency stimulates the inflow of FDI and conversely the appreciation of the host country's currency leads to decreases in the inflow of FDI according to these studies. Macroeconomic stability of a country embodies its strong economic condition, and this factor stimulates foreign entrepreneurs to invest that country. To measure whether the country has macroeconomic stability, inflation rate is employed as a proxy. Apergis and Katrakidilis (1998) and Balasubramanyam (2001) reported that high rate of inflation is negatively related with the influx of direct foreign investment.

The degree of openness, mostly measured by the ratio of exports plus imports to GDP, may have mixed and ambiguous impact depending on the types of FDI. It has a negative effect on FDI if investment is market seeking FDI, because according to tariff jumping hypothesis, foreign firms that want to enter local markets may decide to set up subsidiaries in the host country if they have some difficulties to import their products to the country (Horstmann and Markusen; 1987, and Smith; 1987). In contract, openness has a positive effect on FDI if the nature of FDI is export oriented, since trade protection generally means higher transaction costs associated with exporting, multinational firms may prefer to locate in a more open economy. Kravis & Lipsey (1982), Culem (1988), and Edwards (1990) observed that openness has a positive effect on FDI. Political instability of a country could not be able to attract foreign entrepreneurs to initiate in that economy. Singh and Jun (1995), and Quazi and Mahmud (2004) found the significant negative impact of political instability on direct foreign investment.

III. Myanmar Investment Environment

After changing from centrally planned economic system to a market oriented economic system in late 1988, the government promulgated the Union of Myanmar Foreign Investment Law (FIL) on 30th November, 1988. The major objectives of foreign investment law are as follows:

(1) promotion and expansion of exports
(2) exploitation of natural resources, which require heavy investment
(3) acquisition of high technology
(4) supporting and assisting production and services involving large capital
(5) opening up of more employment opportunities
(6) development of works which would save energy consumption, and
(7) regional development

(Ministry of Commerce 2006, p.6).

According to Notification No (7/94), moreover, the Government of the Union of Myanmar formed the Myanmar Investment Commission (MIC) on 3 August 1994 to supervise and administer the Foreign Investment Law (FIL) and Myanmar Citizen's Investment Law (MCIL). In line with the Notification No. (59/99), the government reformed the commission on 3 December 1999. There are five full time and five part time members in this commission, and all are ministers. The commission undertakes the obligation to Trade Council and Cabinet (Ministry of Commerce 2006, p.6 and 7).

According to FIL, foreign investment activities can be made in any form of the followings:

(1) the wholly foreign – owned investment
(2) a joint venture with Myanmar citizen
(3) an individual, a private company and a co-operative society
(4) a State-owned enterprise.
In order to flow more foreign capital into the country, the FIL provides investment incentives and guarantees to potential foreign entrepreneurs. These incentives are as follows:
(a) exemption or relief from income-tax on reinvested profits within one year,
(b) accelerated depreciation rates approved by the Commission,
(c) fifty percent relief from income-tax on profits accrues from exports,
(d) the right to pay income-tax on behalf of foreign experts and technicians employed in the business, and the right to deduct such payment from assessable income,
(e) right to pay income-tax on the income of foreign employees at the rate applicable to Myanmar nationals,
(f) right to deduct Research and Development expenditures from the assessable income,
(g) the right to carry forward and set off losses up to three consecutive years from the year the loss is sustained,
(h) exemption or relief from customs duty or other internal taxes or both on import of machinery, equipment, instruments machinery components spare parts and materials used in the business during the period of construction, and
(i) exemption or relief on customs duty or other internal taxes or both on imported raw materials for the first three years of commercial operation after completion of construction (Ministry of Commerce 2006, p.10).

In 2014, the Special Economic Zone Law was enacted in order to create a center of attention of investors. At present, there are three SEZs in the country; namely, Kyauk Phyu in Rakhine State, Dawei in the Thanintharyi Region and the Thilawa in Yangon Region. Free zones, promotion zones and other zones are established in the SEZs, aiming to realizing benefits for investors.

According to special economic zone law, business related manufacturing, housing, departmental store, banking, insurance, school, hospital and recreational places are allowed to invest. The possible benefits for investors\(^1\) are made known as follows.

<table>
<thead>
<tr>
<th>FREE ZONES</th>
<th>PROMOTION ZONES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income tax exemption for the first seven years</td>
<td>Income tax exemption for the first five years</td>
</tr>
<tr>
<td>After seven years, 50% relief of current legal income tax rates for five years</td>
<td>After five years, 50% relief of current legal income tax rates for the second five years</td>
</tr>
<tr>
<td>After 12 years, 50% relief of current legal income tax for profit that is reinvested within one year as a reserve fund for the next five years</td>
<td>After 10 years, 50% relief of current legal income tax for profit that is reinvested within one year as a reserve fund for the next five years</td>
</tr>
<tr>
<td>Exemption from commercial tax or valued-added tax</td>
<td>For the first five years, exemptions from customs duties and other relevant taxation on production machinery instrument and necessary spare parts for production; construction material for building such as factories, warehouses and offices.</td>
</tr>
<tr>
<td>Exemptions from customs duties and other relevant taxation on imports of raw materials for production machinery instrument and necessary spare parts for production; construction material for building such as factories, warehouses and offices and motor vehicles</td>
<td>The customs and other taxation shall be paid for the importation of raw materials and other goods for production.</td>
</tr>
<tr>
<td>The exemptions of customs duties and other relevant taxation on the import of trading goods, consignment goods, motor vehicles and other materials which are essential for a business’s free trade goods for production, export trading and services of provision and transportation.</td>
<td>The option to apply for a refund of customs duties and other taxation paid on importing them, if the goods they help produce are exported abroad or into a Free Zone.</td>
</tr>
<tr>
<td>For the resources listed above, 50% relief of the custom duties and other taxation the next five years.</td>
<td>For the resources listed above for, the option to apply for a refund of customs duties and other taxation paid on importing them, if the goods they help produce are exported abroad or into a Free Zone.</td>
</tr>
<tr>
<td>The option to apply for exemption on import tax or value-added tax for goods imported from a local or Promotion Zone to a Free Zone for the investor of Free Zone.</td>
<td>Exemption of commercial tax and value added tax during the relevant relief period provided in the Special Economic Zone Law.</td>
</tr>
<tr>
<td></td>
<td>In all other cases, businesses shall regularly pay the customs and other taxes upon importing raw materials and other goods for production</td>
</tr>
</tbody>
</table>

In 2016, Myanmar investment law was enacted to be smooth the progress of investment environment. The objectives of Myanmar Investment Law\(^2\) are as follow:
(a) to develop responsible investments which do not cause harm to the natural environment and the social environment for the interest of the Union and its citizens;
(b) to protect the investors and their investments in accordance with the law;

---

\(^1\) Ministry of Planning and Finance
\(^2\) Ministry of Planning and Finance

Influx of Foreign Direct Investment into Myanmar

(c) to create job opportunities for the people;
(d) to develop human resources;
(e) to develop highly efficient productivity, service, and trading sectors;
(f) to develop technology, agriculture, livestock and industrial sectors;
(g) to develop various professional fields including infrastructure around the Union;
(h) to enable the citizens to be able to work alongside with the international community; and
(i) to develop businesses and investments that meet international standards.

IV. The situation of foreign direct investment in Myanmar

In late 1988, the Union of Myanmar transformed centrally planned economic system into a market oriented economic system. Accordingly, the government introduced a foreign investment law, which provides potential foreign entrepreneurs with several attractive investment inducements. After introducing Myanmar foreign investment law, the influx of foreign direct investment started in Myanmar from 1989 onwards. The influx of direct investment into the country presents at Table (1).

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI flows (US $ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989/90</td>
<td>449.487</td>
</tr>
<tr>
<td>1990/91</td>
<td>280.573</td>
</tr>
<tr>
<td>1991/92</td>
<td>5.893</td>
</tr>
<tr>
<td>1992/93</td>
<td>103.785</td>
</tr>
<tr>
<td>1993/94</td>
<td>377.184</td>
</tr>
<tr>
<td>1994/95</td>
<td>1352.3</td>
</tr>
<tr>
<td>1995/96</td>
<td>668.166</td>
</tr>
<tr>
<td>1996/97</td>
<td>2814.25</td>
</tr>
<tr>
<td>1997/98</td>
<td>1012.92</td>
</tr>
<tr>
<td>1998/99</td>
<td>54.396</td>
</tr>
<tr>
<td>1999/2000</td>
<td>58.15</td>
</tr>
<tr>
<td>2000/01</td>
<td>217.688</td>
</tr>
<tr>
<td>2001/02</td>
<td>19.002</td>
</tr>
<tr>
<td>2002/03</td>
<td>86.948</td>
</tr>
<tr>
<td>2003/04</td>
<td>91.17</td>
</tr>
<tr>
<td>2004/05</td>
<td>138.283</td>
</tr>
<tr>
<td>2005/06</td>
<td>6065.68</td>
</tr>
<tr>
<td>2006/07</td>
<td>752.7</td>
</tr>
<tr>
<td>2007/08</td>
<td>205.72</td>
</tr>
<tr>
<td>2008/09</td>
<td>984.77</td>
</tr>
<tr>
<td>2009/2010</td>
<td>329.58</td>
</tr>
<tr>
<td>2010/11</td>
<td>19999.12</td>
</tr>
<tr>
<td>2011/12</td>
<td>4644.484</td>
</tr>
<tr>
<td>2012/13</td>
<td>1419.45</td>
</tr>
<tr>
<td>2013/14</td>
<td>4106.86</td>
</tr>
<tr>
<td>2014/15</td>
<td>8009.799</td>
</tr>
<tr>
<td>2015/16</td>
<td>9495.55</td>
</tr>
<tr>
<td>2016/17</td>
<td>6650.08</td>
</tr>
</tbody>
</table>

Source: Ministry of Planning and Finance

In order to see easily the increasing and decreasing inflows of FDI into the country, the pattern of the changes of the influx of foreign direct investment into Myanmar during the research time span is illustrated in Figure 1. As can be seen in Figure 1, the situation of the influx of foreign direct investment into Myanmar was fluctuating. The volume of FDI inflow into Myanmar has dropped significantly after 1997, except a little increase in 2000/01. Myat Thein (2004) commented that the partly reason why the inflow of FDI is declining is the onset of the Asian economic crisis in July 1997. In 1998/99 and 1999/2000, the approved amount of FDI declined by US$ 54.396 and 58.15 million respectively compared to US$ 2814.245 in 1996/97. A large part of FDI inflows were provided by 4 ASEAN countries (Singapore, Thailand, Malaysia, and Indonesia). Thus the noticeable and surprising change in FDI inflows because of the Asian financial crises seemingly shows this circumstance.

In addition, he mentioned that at the beginning of the inflows of FDI to Myanmar, a huge part started with large oil companies, however more investment have been filled up and they are operating now. So this factor could also be a contributory factor. Then again, some of FDI could flow into the country under the Myanmar Citizens Investment Law (MCI) because taxes according to MCI could be paid in local currency. Although FDI inflows declined greatly, the foreign exchange component of investment under the MCI increased in a large size.
Moreover, a large number of foreign companies decided to pull out of Myanmar or not to begin doing business here because U.S. federal sanctions enacted in May 1997 forbid new investment in Myanmar by American companies. Apart from the above, the formation of joint ventures is lack in a level of playing field. Regarding the permission to conduct business in Myanmar, according to Myat Thein's (2004) study, the government openly declared the policy which does not give monopoly power to any group or class of people. However, in fact, military occupying companies such as Myanmar Economic Corporation (MEC) and Myanmar Economic Holdings Ltd. (MEHL) are favored compared to private enterprises. This factor could also be an important factor for the instability of FDI inflows.

As shown in figure, it can be said that the situation of the influx of foreign direct investment into Myanmar was fluctuating. The volume of FDI inflow into Myanmar sharply increased in 2005/06. After that, it has dropped significantly from 2005/06 to 2009/10. However, the volume of FDI into Myanmar enormously increased in 2010/11; the reason may be the removal of economic sanctions at that time. Then, the amount of FDI into the country decline again. After special economic zone law in 2014, the volume of FDI inflow into Myanmar increase significantly again in 2015/16. Therefore, it can be said that the influx of FDI depends considerably on investment policy, law, rules and regulations. Looking at the volume of foreign direct investment by sector during the research time span, the oil and gas sector was the main recipient of FDI, and the power sector took the third place in the influx of foreign direct investment into the country. The pattern of the influx of foreign direct investment by sector shows at Table 2 as follows.
As shown in Table 2, the oil and gas sector has been the main recipient of FDI from 1989/90 to 1994/95, except the hotel and tourism sector in 1990/91 and 1993/94. After that, the manufacturing sector mainly received from the world during the period of 1996/97 and 2001/02. The oil and gas sector became important again from 2002/03 to 2007/08, except the power sector in 2005/06. The mining sector mainly received FDI from the world only in 2008/09. The power sector mainly received FDI from the world only in 2011/12. In 2016/17, the transportation and communication sector become the leading recipient of FDI. Overall, it is clearly seen that the only one sector is not the main recipient of FDI all over the period.

V. Concluding Remarks

This paper emphasizes the situation of the influx of foreign direct investment into the country. According to this study, it is found that the situation of the inflows of direct investment into Myanmar was fluctuating. Looking at the pattern of the inflows of FDI into the country, it can be seen that the oil and gas has been the main receiving sector of FDI during the research time span. It is assumed, therefore, the volume of FDI inflows depend on the amount of oil and gas yields.

In addition, there can have many reasons for the fluctuations of the inflows of FDI. Myat Thein (2004) explained that Myanmar’s uncertain investment environment along with cumbersome administrative procedures prevented a sizeable inflow of FDI. Regarding the inflow of FDI, he expressed in his book that, the factors inhibiting the influx of direct foreign investment into Myanmar were "lack of infrastructure (particularly poor electric power condition), weak telecommunication services and expensive charges, unstable macroeconomic environment, frequent changes of rules and regulations and lack of transparency in its administration ", according to the analysis of the Japan Federation of Economic Organizations in 1995. Regarding unstable macroeconomic environment, the lack of macroeconomic stability hinders a sizeable inflow of foreign capital and investment to increase, this in turn, adversely affect growth prospect and cause future reform efforts more and more unattractive.
Regarding frequent changes of rules and regulations, Myat Hein (2004, p.166) stated that, for instance, July 1997 regulation by the Central Bank which limits foreign remittances of foreign exchange certificate (FECs) purchased by the kyat to US$ 50,000 per month;
- Further regulations by the Central Bank, which further limits foreign remittances of FECs purchased by the kyat to US$ 30,000 per month and then to US$ 20,000 per month;
- November 2000 regulation by the Central Bank, which limits foreign remittances of FECs purchased by the kyat to US$ 10,000 per month.

Apart from that, lack of transparency encourages corruption, and also gives rise to rumors which can be destabilizing. In short, during the period of 1989/90 and 2016/17, the factors such as Asian economic crisis, US federal sanctions, lack of infrastructure (particularly poor electric power condition), weak telecommunication services and expensive charges, unstable macroeconomic environment, frequent changes of rules and regulations and lack of transparency in its administration may be the reasons for the fluctuation of FDI inflows into the country. The existence of such factors may be difficult to encourage the willingness of foreign entrepreneurs to invest. If these factors fade, therefore, the inflows of direct foreign investment into Myanmar are likely to improve. The volume of FDI into Myanmar enormously increased in 2010/11; the reason may be the removal of economic sanctions at that time. In addition, if the authorities can strive to sign a large number of bilateral investment treaties (BITs), the volume of FDI inflow into the country is likely to increase. This suggestion comes from the analysis of many scholars. According to their studies, BITs has been believed by most Asian nations, especially developing economies to play an important role in helping them make their investment climate more attractive to foreign entrepreneurs. Banga (2003) and Neumayer and Spess (2005) concluded that the more BITs a country has ratified, the higher foreign investment flows into it.

In pursuing FDI-enabling policies, moreover, the country should consider giving more priority to cooperative frameworks, encourage inter-regional trade and investment linkages instead of attracting FDI individually, competitively and cooperatively arrange favorable organizations regarding the promotion of direct foreign investment. Accordingly, it can obtain more opportunities in attempting to promote the influx of direct foreign investment, and expect more favorable advantages.

Acknowledgements

I would like to extend my gratitude to Dr. Soe Win (Rector, Monywa University of Economics) and Professor Dr. Ni Ni Aung who always encourage me to write the research paper. My sincere thanks would also be extended to the authorities from respective departments who facilitated my study with indispensable facts and figures. Last but not least, I have not forgotten my entire family who are always ready to encourage and support me with all their love, kindness and goodwill at any time.

References

[7]. Directorate of Investment and Company Administration, (2017), Special Economic Zones, The Republic of the Union of Myanmar.

DOI: 10.9790/5933-0901010108 www.iosrjournals.org
Influx of Foreign Direct Investment into Myanmar