Myanmar's Banking Sector Liberalisation: A Win-win for All

On October 1, the Central Bank of Myanmar (CBM) granted nine foreign banks their first operating licences – issued as part of a move to liberalise Myanmar's banking sector. These licenses will allow the banks to participate in services which were previously restricted in this rapidly awakening country, described by some as the last frontier of Southeast Asia.

These nine banks include Australia's ANZ, Thailand's Bangkok Bank, Japan's Sumitomo Mitsui Banking Corporation, Bank of Tokyo-Mitsubishi UFJ and Mizuho Bank, Singapore's UOB and OCBC, Malaysia's Maybank and China's ICBC. The scope of these licenses will allow the foreign banks to provide credit to foreign companies and local banking institutions, but prohibit them from engaging in retail banking and direct lending in local currency. The strict licence terms also restrict operations to just one branch per bank.

These banks now have 12 months to fulfil the commitments highlighted in their initial proposals; to ensure functional banking operations from day one of business and to comply with requirements laid down by the Central Bank of Myanmar. This is a defining moment for a country that is slowly but surely opening up to foreign investment after 50 years of military rule, albeit slower than expected since the elections in November 2010.

One of the most "Under-banked" countries in the world

With a population of 51 million, Myanmar is regarded as one of the world's most "under-banked" countries, where bank loans comprise a mere 19% of GDP - a far cry from the numbers of some of the other emerging economies such as Vietnam (36%) and Cambodia (108%). This is a reflection of the shallow financial system in Myanmar, a consequence of foreign banks not being allowed to operate in the country for more than half a century.

Opportunities for foreign banks

Against the backdrop of this budding potential and a projected growth forecast of 8 to 9% annually over the next few years (based on IMF projections), these nine banks must surely view the awarding of these licenses as a significant milestone in their partnership with Myanmar. At the same time, it is also an opportunity to leverage their licences and build relationships with the country's local banks and corporate sectors. Foreign banks can commence booking onshore loans to foreign companies, facilitate greater cross-border trade between Myanmar and countries in the region, and serve customers seamlessly throughout the ASEAN region.

These foreign banks can also work with local banks to help them grow in trade finance and project finance businesses, whilst waiting for more financial reforms. Currently, most financing for projects undertaken by local companies are structured as cross-border offshore financing. It is expected that the biggest beneficiaries for these foreign banks' operations are the power, real estate and infrastructure sectors. Undoubtedly, this will improve access to capital and liquidity, as Myanmar boosts to finance its imports and lower its current account deficit.

Uncertainty clouds the road ahead

However, all this is not without risk as these banks start to do business in a frontier economy like Myanmar. The country's financial system is still very much cash-based and "shadow" banking – unregulated borrowing and lending occurring outside of the banking sector - is prevalent. There are still numerous challenges surrounding supervisory, legal and regulatory reforms. While the country has made significant efforts in welcoming foreign and private investment by revisiting several laws, particularly the Foreign Investment Law and the Central Bank Law, the banking sector needs to be aligned to international standards. There is also a clear need for a stronger legal framework and the implementation of bankruptcy laws for the financial sector.

Furthermore, enforcement of the laws surrounding recognition of security or collateral is lacking. According to a 2014 World Bank study, resolving insolvency in Myanmar can take up to five years. The recovery rate for a loan is 14 cents in a dollar, a very low rate compared to the rest of Asian and OECD countries. Until these safeguards are implemented and a full roadmap laid out on clear reforms to the financial services sector, transformation to the market system in Myanmar will continue to be fraught with uncertainty, potentially accompanied by financial crises.

A win-win for all

Clearly, Myanmar is keen to catch up with its neighbours and become one of the economic giants in the ASEAN region, as it once was in the 1960s. The issuance of foreign banking licences to these nine banks is a step in the right direction. The move will improve overall institutional strength, spur investment inflows, add an element of competition to the banking system, facilitate knowledge and technology transfer, and kick start the training and hiring of local staff. This is a crucial turning point towards transforming the financial system - a bumpy long-term journey but definitely a win-win for both the banks and the country to propel the growth and development of Myanmar.

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