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McKinsey warns of risks for Myanmar investors

A new report from global consulting firm McKinsey & Co. warns of "major risk of disappointment" for companies entering Myanmar despite the country's recent reforms, particularly if the government fails to solve sectarian strife that again erupted in mob violence this week.

"The first thing the government is going to have to do is ensure a stable political situation," said Heang Chhor, senior partner at McKinsey and one of the principal authors of the report, one of the first comprehensive looks at Myanmar's economic potential, compiling half a year of independent research and interviews from the Southeast Asian country where data are notoriously hard to come by and often unreliable.

According to the McKinsey data, Myanmar could more than quadruple the size of its economy to more than \$200 billion by 2030, but only if it builds up basic infrastructure and diversifies its economy. The emerging market remains one in which there is "everything to play for," says the report, penned by McKinsey Global Institute, the firm's research unit.

"Quadrupling the economy in the next few decades is not an absurd number to have in mind, but it is not going to happen with just agriculture, energy and mining," said Mr. Heang Chhor, listing Myanmar's biggest sectors.

It will be an expensive process, he said. In infrastructure alone, Myanmar would need \$320 billion in investment over the next two decades to achieve annual growth rates of 8% and billions of dollars will also be needed to overhaul its crumbling education infrastructure and put in adequate training schemes to equip small businesses and rural dwellers with necessary skills. The investment needs are in line with other estimates.

Despite Myanmar's economic promise and hype since decades of military dictatorship gave way to a nominally civilian government under President Thein Sein in 2011, many Western companies have taken only cautious, tentative steps into the market, making exploratory trips but remaining hesitant to park big investments such as manufacturing plants.

"Investors are actively considering Myanmar, but many want reassurance that the government can resolve ethnic and communal violence," the report said.

Increasingly frequent eruptions of violence between majority Buddhists and minority Muslims are emerging as Mr. Thein Sein's biggest challenge. The bloodshed, some of it fanned by Buddhist extremists, has left hundreds dead and displaced more than 100,000 people, mostly Muslims, over the past year.

On Tuesday and Wednesday, the violence spread for the first time to northeastern Myanmar as mobs ravaged Muslim areas in the town of Lashio. According to a post on the official Facebook page of Myanmar's Ministry of Home Affairs, one person was killed Wednesday, the first report of a death in the Lashio clashes, with four others injured. Authorities said dozens of homes, Muslim shops, vehicles and all three religious schools there were destroyed, but that the situation was under control.

A curfew was imposed Tuesday night, but gangs on motorbikes wielding sticks and iron rods circled Muslim areas and launched fresh attacks Wednesday, some residents said. They said police and soldiers weren't intervening to stop the violence. Central government authorities have acknowledged the burnings but have otherwise commented little. Police have been mostly unreachable.

"Muslim people who live near the burned buildings and shops are moving to other places," said San Zar Ni Aung, a Muslim resident of Lashio, by telephone. "They don't dare live in these areas anymore."

The Lashio clashes are the first time the violence has crept so close to Myanmar's border with China, an area where many big infrastructure projects are based. Lashio is approximately 100 miles, or 160 kilometers, from the Chinese border town of Ruili, and about 40 miles, 65 kilometers, east of a \$2.5 billion oil-and-gas pipeline from the Bay of Bengal that will soon carry crucial energy supplies to Myanmar's northern neighbor. Activists in the area said there had been no word of an attack on the pipeline.

According to McKinsey, businesses are worried that the country may start to lose its momentum toward political and economic reform, with so many changes implemented in just over a year—everything from a new investment law to new media laws and a reworked legal infrastructure.

"It is very difficult to do this in a short time frame," Mr. Heang Chhor said, comparing it to the experience of other Southeast Asian countries like Indonesia and Vietnam in recent decades, where reforms came in spurts and sometimes stalled. But he added that the task of maintaining political and social stability was key for momentum to continue, and that failing to address current tensions would be the biggest risk to further economic development and foreign investment.

McKinsey said that well-executed economic reforms coupled with training and investments in targeted sectors—including tourism, which has already seen a huge lift since the country started to open up—could move 18 million people in the country of 60 million out of extreme poverty, and earning above \$1.25 a day by 2030. Though the report said three-quarters of Myanmar's population is still likely to be earning less than \$10 a day in 2030.

Experts there say these targets aren't impossible to meet with private-sector investment, particularly considering the experience of Myanmar's neighbors, including Thailand and Indonesia, which quadrupled their per capita gross domestic product from levels comparable with Myanmar's today in just 13 and 14 years respectively.

The country will host the East Asia meetings of the World Economic Forum next week, seen as a symbol of government and private-sector players rewarding the country for its economic and political changes. Executives from dozens of companies and high-level government officials from the region are expected to attend, including from PepsiCo, General Electric, Chevron and AirAsia.

The meetings will be seen as a test of investor appetite, particularly for Western companies, more than a year after sanctions against the once-isolated country began to be lifted.

"If [Myanmar] fails to build a compelling growth plan and implement it effectively, today's goodwill and cautious optimism could evaporate all too rapidly," the McKinsey report said.

—Myo Myo in Yangon, Celine Fernandez in Kuala Lumpur and Jacob Gronholt-Pedersen in Singapore contributed to this article.

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