Study on the Growth-Enterprise Development in Myanmar Final Report

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Introduction

This Study on the Growth-Enterprise Development in Myanmar examines the current status and issues of Myanmar's financial and capital markets, on the premise that the Growth-Enterprise Development Fund is established for promoting growth companies that should play a central role in the economic growth of Myanmar, and clarifies the issues among rules and regulations related to investments by summarizing legal frameworks for establishing such a fund. The Study also aims to formulate a scheme for fostering investee companies by providing financial support, business management improvement guidance, and other technical assistance through such a fund. This Study, which will drive growth of potential companies that will be listed in the future through investments, loans, and technical assistance, and eventually lead to the development of the securities markets, is designed to increase the international competitiveness of Myanmar companies and contribute to the industrialization and modernization of Myanmar.

With regard to the current status of financial and capital markets in Myanmar, not only are the capital markets under-developed, but indirect financing is also not functioning adequately. Therefore, Myanmar companies currently rely solely on their own capital or the assets of the owner's family.

Moreover, a major source of revenues for banks is based on profit margins between deposits and loans, and government bond trading, and very little income derives from trading profits, unrealized gains, and so on, due to lack of securities market. Deposits, as a general rule, only have terms of up to 1 year, and banks practically provide medium-term loans by rolling over the loans every year. Therefore, as advances in IT have lagged, administrative procedures have become complicated for both financial institutions and borrowers. In addition, financial institutions are not able to raise medium to long-term funds, and are constantly having problems with cash flows due to the duration mismatch that results from effectively providing medium-term loans with funds raised from short-term funding. Private sector companies are also in a difficult situation with respect to raising sufficient funds. Although development of banks and establishment and development of a securities market are underway, they will not be able to function immediately. Under such circumstances, instead of those measures, a provider of equity and debt capital is required.

When establishing an investment fund, it is important to consider the fund's structure from a practical perspective, such as the legal and taxation aspects.

From this Study it can be deemed that: 1) strong government support is required; 2) in cases where status equivalent to that of domestic companies can be attained by becoming a "Special Company," major advantages can be obtained in the execution and sale of investments by forming a joint venture with state-owned companies; and, 3) when considering the use of loan assistance from JICA, premised on a two-step loan through state-owned financial institutions, in order to make loans that are aligned with fund investments, it is optimal that the fund is established and operated by a joint venture between a Japanese investment management company and a Myanmar government agency, in particular, a state-owned financial institution, because it is desirable that the same financial institution be involved in both investment and loan.

On the other hand, in Myanmar there is no law that has direct jurisdiction over the establishment and operation of private equity funds, and legal practices are not always carried out pursuant to statutory law. Under such circumstances, at the present time it is extremely difficult to build a structure that is conclusively free of problem areas. Accordingly, it is true that there are a number of preconditions that will have to be met by even the structure that is determined to be optimal by this study.

The Growth-Enterprise Development Fund aims to have public and private sectors work together to improve management, and strengthen the competitiveness of companies in Myanmar, hence boosting Myanmar's economy, through private investment funds and management improvement support, as well as provision of funding through JICA's overseas investment finance and two-step loans, and further, through technical assistance and support from the Japan Center. With JICA providing assistance, although proactive involvement of the recipient country's government is assumed, because a great impact can be expected by supporting development of domestic companies in Myanmar, it is possible that the active involvement of Myanmar government, which regards the transition to a market economy to be an important issue, can be obtained. In addition, to ensure the understanding and cooperation of Myanmar government, we are proposing and engaging in discussions on such measures as jointly establishing an investment management company with state-owned financial institutions. In addition, the fund is considered to conform to basic concept regarding JICA overseas investment finance "that funds are provided to 'development projects' carried out as 'loan assistance' from JICA, a development assistance agency; and, funding is used for high-impact development projects that cannot be financed by existing financial institutions."

The Growth-Enterprise Development Fund is established with capital from Japan's private sector, and by combining JICA's support tools, and providing support as a series of packages, it can be expected that effects towards the development of Myanmar's capital markets and the transition to a market economy can be maximized. The flow-on effects from the development of growth companies through the provision of investment and management support, the development of capital markets through the listing of investee companies, as well as the accumulation of financing and review expertise by domestic banks in Myanmar through two-step loans provided by JICA, should have widespread effects on financial and capital markets in Myanmar.

Contents

List of Charts

List of Tables

List of Abbreviations

DICA	Directorate of Investment and Company Administration
GP	General Partner
JETRO	Japan External Trade Organization
MIC	Myanmar Investment Commission
MSEC	Myanmar Securities Exchange Centre

Chapter 1. Background and Objectives

1. Current Status and Issues of Myanmar’s Financial Markets

1-1 Current Status of Myanmar’s Financial Markets

The regulatory authority of the financial sector in Myanmar is the Ministry of Finance and Revenue, and the Central Bank of Myanmar supervises the financial sector including banks and insurance and securities companies.

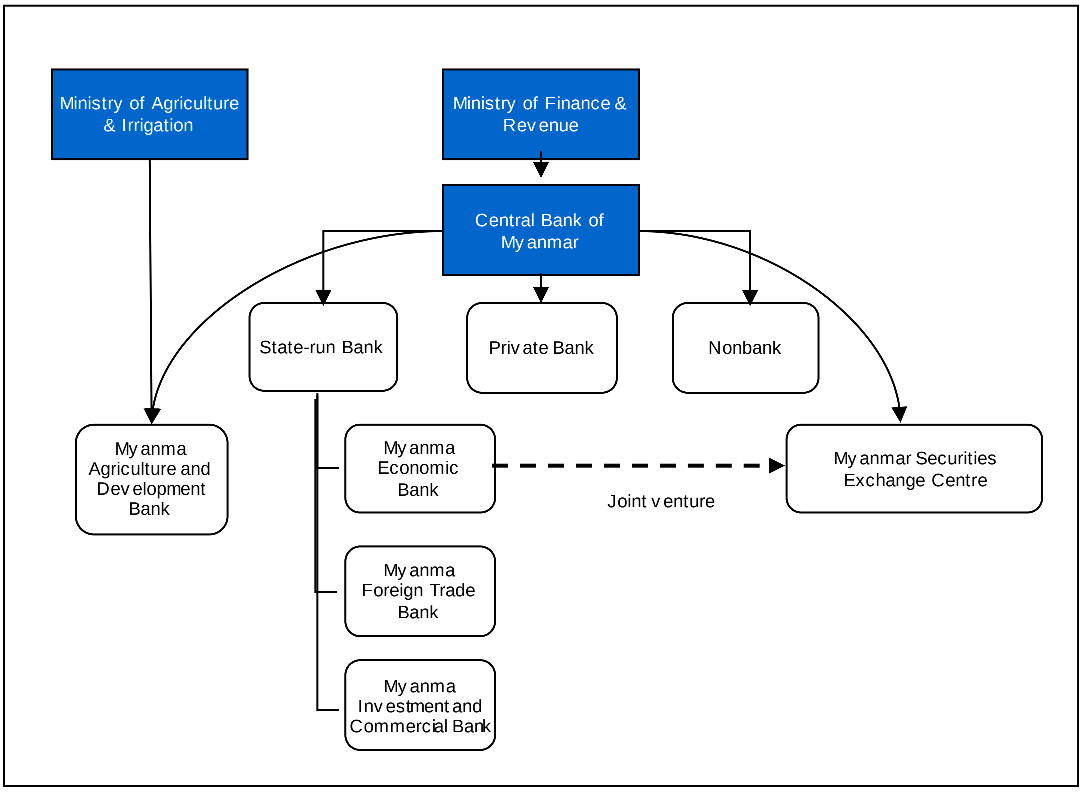

Chart 1 Outline of financial sector

(Source) Prepared by the Investigation Group based on “Changes in Transitional Economy in Myanmar, IDE-JETRO No. 546”

(1) Financial Market

Banks engaged in financial operations in Myanmar’s financial market comprise 4 state-owned banks and 19 private banks: a total of 23 banks. State-owned banks include 3 banks supervised by the Ministry of Finance and Revenue and the Myanma Agriculture and Development Bank supervised by the Ministry of Agriculture and Irrigation. All of these banks are controlled by the Central Bank. 9 private banks are joint ventures established by government agencies and private companies. Currently, foreign banks can only open representative offices, and they are not allowed to have a branch or a subsidiary in Myanmar, but it has been reported that central bank officials have said that the restrictions against establishing foreign-domestic joint ventures, wholly foreign owned banks, and the establishment of foreign bank branches will be lifted in stages.

Table 1 List of banks

	Name of bank	Location of head office	Incorporated
State-owned bank			
1	Myanma Economic Bank	Building 26/ Myatpanthazin Street, Near the Hotel Zone, Nay Pyi Taw	1976
2	Myanma Foreign Trade Bank	No 80/86 Maharbandoola Park Street, Yangon	1977
3	Myanma Investment and Commercial Bank	N0 170/176 Bo Aung Kyaw Street, Botadaung Township, Yangon	1978
4	Myanma Agriculture and Development Bank	No-26/42 Pansodan Road, Yangon	1979
Joint venture bank with government agency			
1	Myanmar Citizens Bank Ltd	No-383/Mahabandoola Road,Kyuktada Township, Yangon	1992
2	Yadanabon Bank Ltd	No-58(A) 26 Bayintnaung Street Between 84*85 Street, Aung Myay Tharzan Township, Mandalay	1992
3	Myawaddy Bank Ltd	Plot B-1 Near Thiriyadana Super Market, Hotel Zone, Naypyitaw	1993
4	Yangon City Bank Ltd	Coner of the Settyon Street & Banyerdala Street Mingalar Taung Nyunt Township,Yangon	1993
5	Small and Medium Industrial Development Bank	Plot No-2, Oktayathiri Quarter, Naypyitaw	1996
6	Treasury Bank of Myanmar	No-654/666 Merchant Road Pabedan Township, Yangon	1996
7	Rural Development Bank	Plot-2, Compound of Thiriyadanar Super Market, Naypyitaw	1996
8	Co-operative Bank Ltd	No-334/336 Corner of Strand Road and 23rd street, Latha Township, Yangon	1992
9	Innwa Bank Ltd	No-554/556 Corner of Merchant Road and 35th Street Kyuktada Township, Yangon	1997
Private bank			
1	First Private Bank Ltd	No-619/621 Merchant Road , Pabedan Township,Yangon	1992
2	Yoma Bank Ltd	No-1, Kungyan street Mingalar Taung Nyunt Township,Yangon	1993
3	Myanmar Oriental Bank Ltd	No-166/168 Pansodan Road Kyauktada Township, Yangon	1993
4	Asia Yangon Bank Ltd	No-319/321 Mahabandoola Road Botadaung Township Yangon	1994
5	Tun Foundation Bank Ltd	No-165/167 Bo Aung Kyaw Road(Middle), Kyauktada Township Yangon	1994
6	Kanbawza Bank Ltd	Plot No-1, Oktayathiri Quarter, Naypyitaw	1994
7	Asia Green Development Bank Ltd	No-168, Thiri Yatanar Shopping Complex, Zabu Thiri Township, Nay Pyi Taw	2010
8	Ayeyarwaddy Bank Ltd	Block (111, 112), Asint Myint Zay, Zabu Thiri Township, Nay Pyi Taw	2010
9	United Amara Bank Ltd	Block (2), Asint Myint Zay, Yaza Thingaha Road, Oattara Thiri Township, Nay Pyi Taw	2010
10	Myanma Apex Bank Ltd	Block (10), Asint Myint Zay, Yaza Thingaha Road, Oattara Thiri Township, Nay Pyi Taw	2010

(Source) Central Bank of Myanmar

Additionally, Myanmar private banks and foreign banks are moving ahead on collaborative efforts. When it comes to Japanese banks, Sumitomo Mitsui Banking signed a technical assistance memorandum of understanding with Kanbawza Bank in May 2012. In November 2012 Juroku Bank signed a business alliance agreement with Ayeyarwady Bank and in December 2012 Bank of Tokyo-Mitsubishi UFJ signed a business alliance agreement with CB (formerly Co-operative) Bank to provide technical assistance in foreign exchange operations.

Chart 2 Trend of saving deposit balance and deposit/lending interest rates shows the trend of saving deposit balances and interest rates on deposit and loans. Until mid-2010, the saving deposit balance of state-owned banks exceeded the balance of private banks, but the private banks rebounded in September, 2010, and since then the difference between state-owned banks and private banks has expanded. As of September, 2010, saving deposit balances of state-owned banks and private banks were 1.45 trillion kyat and 1.46 trillion kyat, respectively. As of March 2012, however, the balance of state-owned banks was 1.93 trillion kyat, while that of private banks was 3.62 trillion kyat, representing approximately twice the state bank balance.

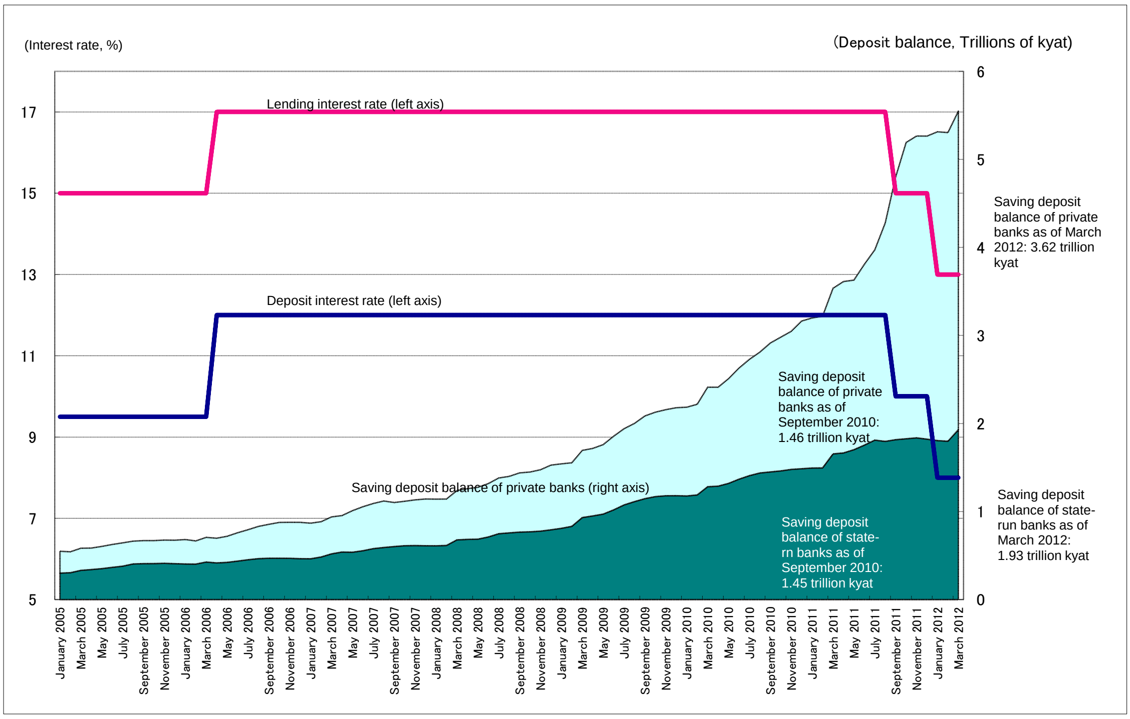

Chart 2 Trend of saving deposit balance and deposit/lending interest rates

(Source) Prepared by the Investigation Group based on Central Statistical Organization, IMF data

A factor pointed out behind the remarkable increase in the deposit balance of private banks in recent years is that the phased-in easing of regulations on total deposits accepted enabled private banks to accept more deposits. In addition, private banks, compared to their competing state-owned banks, have promoted more systemized operations to increase business efficiency, and also have more rapidly enhanced convenience for users through the introduction of an ATM network.

The lending balance seemed to increase in line with an increase in the deposit balance, although lending data have not been released by the Central Statistical Organization recently. According to 11 private banks interviewed during the first on-site feasibility study, the loan-to-deposit ratio was approximately 60% to 70%. Under regulations of the Central Bank, loans are extended on the basis of real estate collateral in principle, and the loan-to-value ratio is expected to be around 30% to 50%. Borrower screenings consist mainly of real estate appraisals, and screenings rarely look at a company's past performance or future business plans. Although most loans are taken out under an individual's name, the proceeds may be used only for business purposes. This is probably because in many cases companies fear that they could be taken over by the government, and therefore they register real estate in the name of an individual. However, if the loan is in an individual's name, it must be guaranteed by the board of directors of the company that is conducting the business that is being financed. Additionally, loans are granted only to existing companies, and loans to startup a new company are not permitted (however, it is possible for an existing company to obtain financing for a new business).

According to interviews with the Republic of the Union of Myanmar Federation of Chamber of Commerce and Industry (UMFCCI), company owners, and financial institutions, it appears that the funding needed for business comes mainly from internal sources or other business owners, and bank financing mechanism is not functioning very well.

Bank funding comes from deposits, but only short-term deposits are accepted and term deposits with a maturity of more than one year are not permitted (the term is up to one year). In principle, loans are also for a maximum of one year, but the banks effectively engage in medium-term lending through rollovers. Many banks are rolling over loans for 3-5 years for companies with appropriate collateral on real estate or companies that they have judged to be good borrowers in the past. They are using short-term funding to extend medium-term loans, and this gives rise to a duration mismatch.

Next, we will examine business access to the funds they need. The table below shows, for each country, the ratio of business loans outstanding to broadly defined liquidity. This ratio shows how much of overall capital, in a broad sense, is devoted to business lending, and serves as a measure of private enterprise access to capital. Here we have used the IMF criteria for broad liquidity, and we have used the "claims on private sector" pulled from each country's Monetary Survey data as business loans outstanding. Private-sector loans outstanding include not only loans to businesses, but also the loans outstanding to individuals, such as housing loans. In Myanmar, almost of this consists of business loans, so we have treated the entire amount as business loans. For other countries, we used the ratio after excluding the share of the loans to individuals within commercial bank loans outstanding as a rough gauge.

Table 2　Private enterprise access to bank lending

	Myanmar	Indonesia	Thailand	Japan (reference)
Business loans outstanding/broad defined liquidity	25%	40%	82%	342%

(Source) Prepared by the Investigation Group based on IMF, World Bank data

While an amount of capital equivalent to about 40% and 80% of broad defined liquidity is going to private sector in Indonesia and Thailand, respectively, the figure for Myanmar is just 25%. This shows that the reallocation of capital via banks is not yet functioning well.

(2) Capital Market

Myanmar Securities Exchange Centre (“MSEC”), which was established by the Myanma Economic Bank and Japan’s Daiwa Institute of Research Holdings, Ltd. (“DIR”) in 1996, is the sole foreign-capitalized financial institution, and it is an active player in the capital market. MSEC trades 2 issues through an over-the-counter market: Forest Product Joint Venture Company Limited and Myanmar Citizens Bank Ltd, both of which are a joint venture of the government and private sector, but transaction volume is small. From January 2010, under the designation of the Central Bank of Myanmar, MSEC has tendered and underwritten government bonds (two-year, three-year, and five-year bonds) together with the Myanma Economic Bank.

Chart 3　Trend of outstanding balance of government bonds presents the trend of balances of two-year, three-year, and five-year government bonds held by private and public sectors. It appears in reality that all types of bond are largely held by the private sector, especially private banks. There is no secondary market for government bonds in Myanmar, and investors generally keep bonds until maturity.

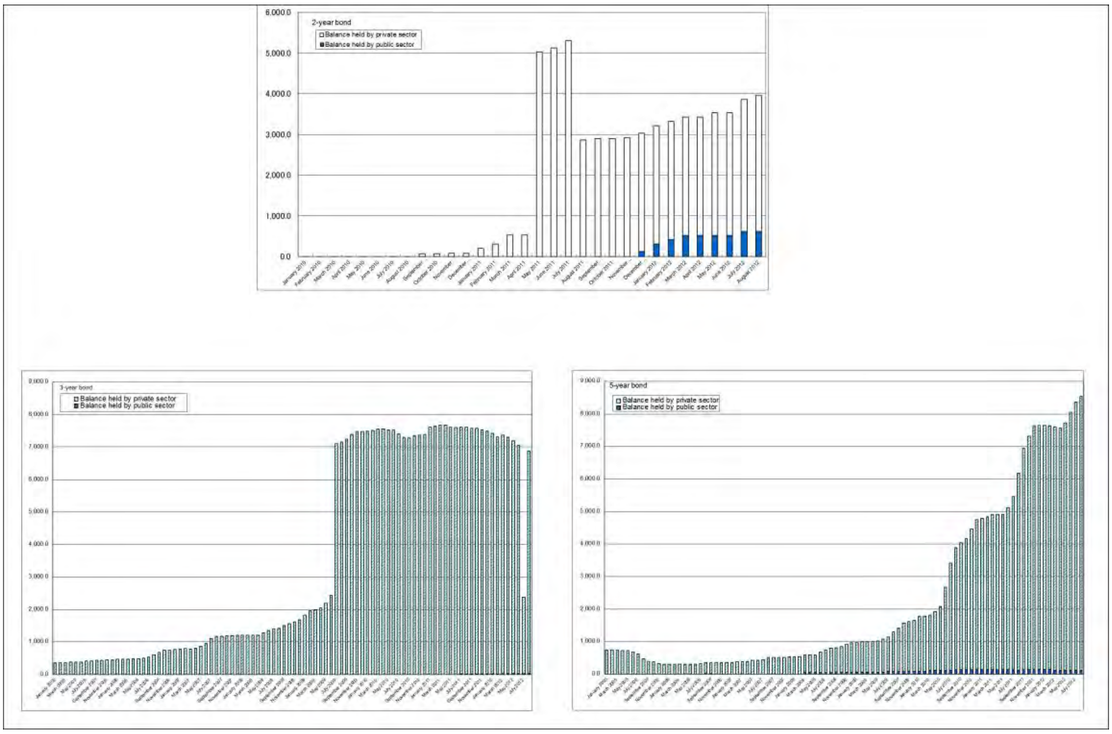

Chart 3　Trend of outstanding balance of government bonds

(Source) Prepared by the Investigation Group based on Central Statistical Organization data

With the aim of opening a stock exchange in 2015, the Myanmar government has been working on legislating the Securities Exchange Law. In this regard, the three parties of the Central Bank of Myanmar, the Tokyo Stock Exchange, and DIR entered into a Memorandum of Understanding on developing Myanmar's capital markets in May 2012. The memorandum commits the Tokyo Stock Exchange and DIR to providing support in the following five areas:

- Advice on designing the structure of the stock exchange,
- Advice on designing the system of the stock exchange,
- Support for the development of human resources,
- Implementation of seminars on securities and finance, and
- Support for the operations of the stock exchange

To establish the stock exchange in 2015, it is necessary to address a wide range of issues including the organization and scope of operations of the stock exchange, the structure of securities companies to become member firms of the stock exchange (composition, system, capital, and requirements for licensing), a monitoring agency to identify fraudulent transactions, listing requirements, finding and fostering companies to be listed, developing investors, and so forth, in addition to establishing relevant laws and regulations. It is also essential to develop IT systems including the stock exchange system and trading system connecting the stock exchange and securities companies, as well as front, middle, and back functions within securities companies. Furthermore, in Myanmar, there are few human resources with working experience at a stock exchange, monitoring agency, or securities company, so it will take time to develop necessary human resources.

1-2 Issues on Myanmar's Financial Market

As discussed in 1-1.Current Status of Myanmar's Financial Market, sufficient corporate loans are not provided by banks in Myanmar. With respect to bank interest rates, the central bank set up a minimum interest rate for deposits (8% as of May 2013) and a maximum interest rate for loans (13% as of May 2013). Each bank can set its own interest rates, but their interest rates are currently stuck at the respective minimum and maximum, so there is no difference in interest rates between banks. Going forward, in order to foster the development of Myanmar's banks it will be essential to liberalize interest rates, thereby promoting stronger competition among banks. Furthermore, at present loans are secured by real estate in principle, and therefore the main subject of loan reviews is the appraisal of the collateral on property. Through our interviews we learned that although (potential) borrowers submit financial statements, reviews are very rarely based on a company's business plan. In our view, as banking deregulation proceeds, leading to competition among banks and expanded lending, it will be necessary to strengthen the banks' loan review capabilities. There are a number of other matters that must be addressed to facilitate the development of banks in Myanmar, such as the creation of an interbank market as a mechanism for adjusting short-term funding surpluses and deficits among banks. These are not issues that can be addressed in a day, so it will take some time to have a well-functioning system.

The stock exchange is now just in the preparatory stage, so the amount of capital being supplied to companies is completely insufficient.

On the other hand, U Thein Sein, the President of Myanmar, has announced raising the ratio of the manufacturing sector to GDP (by relatively reducing the ratio of the agricultural sector), expanding employment, and increasing GDP per capita. To achieve these goals, the financial sector should play a major role. To effectively provide flows of funds to companies, it is ideal to have indirect financing—with deposits collected from the public lent to companies, and direct financing, with funds flowing from investors to companies through a stock exchange—develop in a balanced and mutually supplementing way. However, as discussed above, considering the current status of Myanmar, it seems difficult to foster the banking function and open and develop the securities market immediately. Therefore, it is necessary to create a fund supplier who can provide investments and loans in near term on behalf of suppliers of indirect and direct financing.

The expectation is that the Growth-Enterprise Development Fund will invest in about 10 companies, and the desire to eventually go public is one of the criteria that will be used in screening portfolio companies. Accordingly, it will perform the function of supporting public offerings by identifying and fostering portfolio companies as candidates for public listing. Therefore, its existence will be significant in a Myanmar that is in the initial stages of developing its capital markets, as it works closely with the Myanmar government, the Tokyo Stock Exchange, and Daiwa Institute of Research in their efforts to establish and foster a securities exchange, including the effort to establish a securities and exchange law.

Regarding the stock exchange in its preparatory stages, looking at cases in neighboring countries, to ensure smooth operation of a stock exchange after its establishment, it is important to secure listing companies. Currently, there are 2 types of companies in Myanmar under the Myanmar Companies Act of 1913 ("Companies Act"); a "Private Company," which is restricted from transferring shares and a limited maximum number of shareholders, and a "Public Company," which is not subject to such restrictions, but is required to disclose certain information.

When it became possible to establish private sector companies thanks to open-door policies starting in 1988 and the passage of the Private Industrial Enterprises Law in 1990, public companies, which can raise capital from a wider base, were also allowed. These public companies were established against the backdrop of economic reforms, albeit in fewer numbers that private companies. However, the government took a somewhat passive stance towards the establishment of public companies after the collapse of a number of finance companies which had raised capital from a broad base that had been organized as public companies. Later, with it taking concrete steps towards the establishment of the Myanmar securities exchange in 2015, increasing the number of public companies as candidates for listing on this exchange came to be seen as an important issue for the government. Now, with the government's encouragement, public companies are being established mainly as companies with a need for substantial amounts of capital, such as companies established to bring together a number of companies in the same industry in order to improve the industry's business environment (for example a commodities exchange) or infrastructure-related companies. As a result, the number of such companies is trending upwards, but there are still only around 50 public companies as of February 2013. Many corporate owners tend to strongly dislike the increases in tax burden and administrative costs associated with the information disclosure, and are apt to hesitate to reorganize their companies from private to public companies.

To increase the number of public companies, thus expanding the number of listing companies, it is necessary to disseminate an understanding of the advantages of a stock listing, as well as to take some measures to provide tax benefits. In Myanmar, keeping multiple books of account is common, and most private companies do not pay the tax amount due. Regardless of whether this is true or false, to reduce burdens inherent to reorganizing a private company into a public company and listing its shares and create incentives to for such listing, we believe it is necessary to examine giving listed companies tax incentives.

Once the ASEAN Economic Community is established at the end of 2015, cross-border movements of people, goods, and capital within ASEAN territories will be free, in principle. As a result, Myanmar companies will face fierce competition within ASEAN territories, including inside the country. If a developing Myanmar economy participates in such competition, it may have a significantly large impact on companies and the business community in Myanmar. To limit such impacts as much as possible, there is an urgent need to foster Myanmar companies prior to the establishment of the ASEAN Economic Community. In so doing, it is necessary to provide support for enhancing the management of companies, in addition to investment, thus assisting unified growth in line with a company’s growth strategy.

Chapter 2. Considerations on the Structure of the Growth-Enterprise Development Fund (GEDF)

1. Legal considerations

In Myanmar, not only may legal practices be somewhat out of sync with the legislation on which they are based, but laws such as the Foreign Investment Law have also been subject to frequent revision of late in line with the processes of market liberalization.

With this in mind, we inquired into current legal practice insofar as it may relate to the structure of the Growth-Enterprise Development Fund (GEDF) by making written inquiries to a number of local law firms in Myanmar. As a part of this research, we also visited Myanmar for direct discussions with local law firms to clarify such matters as remained unclear based purely on the written survey . We also took the opportunity while in the country to meet with representatives of the Directorate of Investment and Company Administration (DICA) and of the Central Bank of Myanmar to discuss the law as it might pertain to the establishment the GEDF and of a company to manage its investments.

There are two main ways in which the fund might be structured. In short, the investment vehicle might take the form of a Special Company (see Chapter 2 1-2. (1) “Share acquisition vehicle”) or Foreign Company (see Chapter 2 1-1. (1) (a) “Limitations placed on Private Companies”), either of which would invest funds raised by an overseas partnership or company in a Myanmar company, which would buy shares in such other Myanmar companies as constituted investment targets

(1) GEDF to be established as the subsidiary of a joint venture between an investment management company and a Myanmar government institution (see Chart 5: Structure 1). Funds to be raised for investment in the GEDF by a partnership or company established for the purpose overseas.

(2) GEDF to be established in association with a Myanmar government institution in the form of a joint venture which would also manage the investment of funds raised (See Chart 6: Structure 2). Funds to be raised for investment in the GEDF by a partnership or company established for the purpose overseas.

(1) Structure under which an investment management company could be established as a joint venture with a Myanmar government institution, with the GEDF as its subsidiary

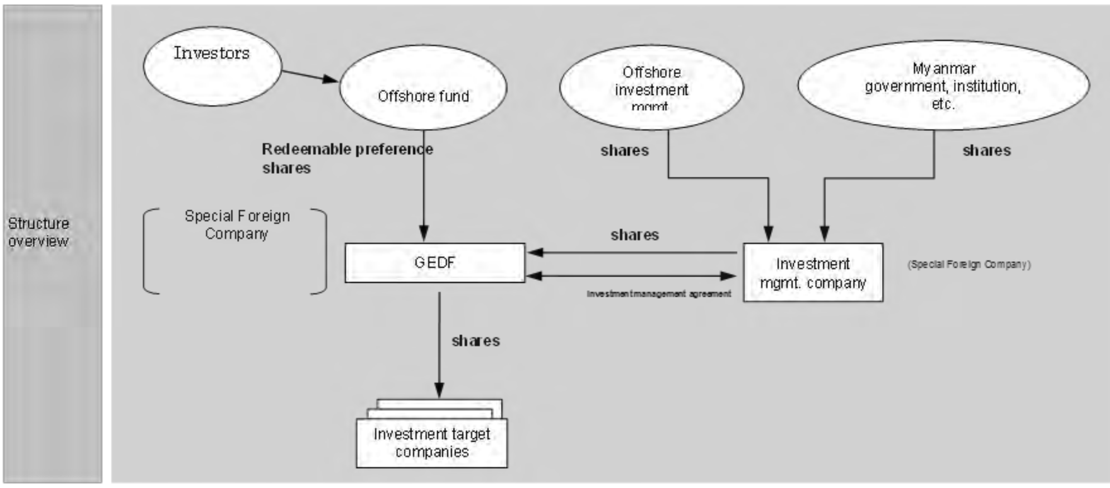

Chart 4 Structure 1

(2) Structure under which the GEDF and investment management company are established independently of the Myanmar government (no joint venture)

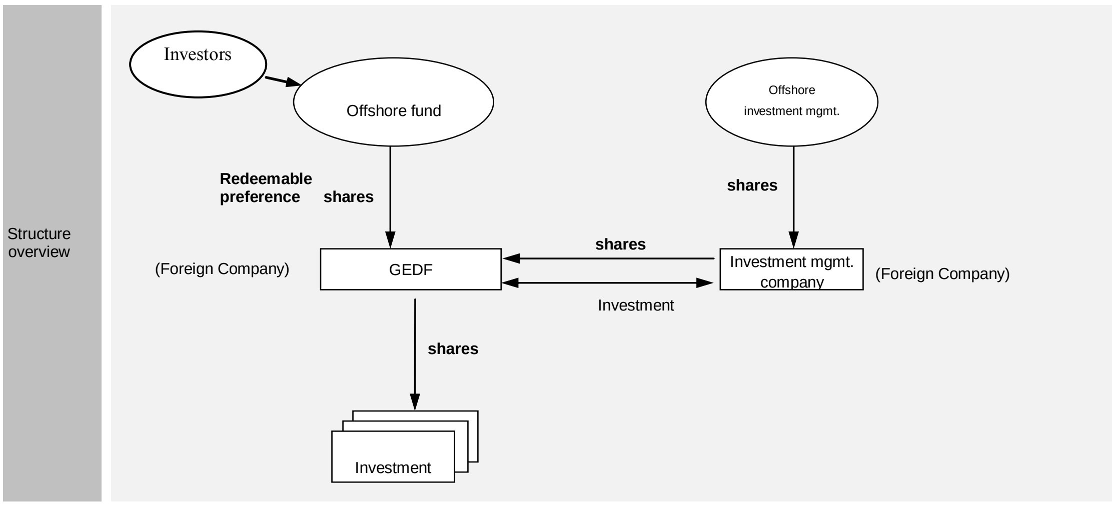

Chart 5 Structure 2

However, given the problems outlined below, should structures 1 or 2 be adopted, the common practice of treating a joint venture with a Myanmar government institution as a Special Foreign Company (see Chapter 2 1-2. (1) "Share acquisition vehicle") would need to be reformed. Absent such reform and the adoption of any of structures 1 or 2 would necessitate the root and branch reform of current business practice whereby foreign companies are effectively prevented from acquiring shares in Myanmar companies (see Chapter 2 1-1. (1) (a) "Limitations placed on Private Companies").

1-1 Problems of investing in Myanmar

Those we currently envisage subscribing to the GEDF would be Japanese institutional investors and, as such, foreign investors from the standpoint of any Myanmar company targeted for investment. When considering the structure of the fund, therefore, the question that inevitably arises is whether or not foreign investors, and the company that channels their funds, will be permitted to acquire shares in Myanmar companies.

Table 3 Classification of Myanmar corporations from standpoint of shareholder

Myanmar Company	A company whose equity capital is entirely held or controlled by Myanmar citizens at all times (Companies Act Article 2(I)(2A))
Foreign Company	A company other than a Myanmar Company or a Special Company established pursuant to the Special Company Act of 1950 (Companies Act Article 2(I)(2B)) (Note 2)
Special Company	A company established pursuant to the Special Company Act of 1950 (Companies Act Article 7(1)) (Note 1) (Note 2)

(Note 1) Although it is not expressly provided in laws and regulations, according to local law firms, a joint venture with a Myanmar government body is established as Special Company.

(Note 2) Although it is not expressly provided in laws and regulations, according to DICA, a Special Company that is joint venture between a foreign investor and a Myanmar government body is treated as a Special Foreign Company.

Table 4 Classification of Myanmar corporations from standpoint of liquidity

Private Company	A company that in its articles of incorporation (a) restricts the right to transfer its shares; (b) limits the number of shareholders to 50 persons, excluding individuals employed by the company; and (c) prohibits the offering of shares or bonds to the general public (Companies Act Article 2(I)13)
Public Company	A company that is not a Private Company (Companies Act Article 2(I)(13A) (Note)

(Note) Local law firm B indicated that a Public Company must have at least 7 shareholders.

(1) Practical restrictions on the transfer of shares

Under the terms of the Myanmar Companies Act, no restrictions are placed on the acquisition of shares in Myanmar companies (including new shares issued by such companies) by individual foreign investors or Foreign Companies[1]. However, given the distinction between a Private Company and a Public Company, as defined by the Myanmar Companies Act, share transfers of the sort outlined below are effectively prevented from taking place.

(a) Limitations placed on Private Companies

Under the terms of the Myanmar Companies Act, companies in Myanmar are divided into Myanmar Companies and Foreign Companies. Under Article 2 of the Act, a Myanmar Company is defined as "a company whose equity capital is at all times held and controlled by citizens of Myanmar" (Myanmar Companies Act, Article 2, Clause I, Item 2A), and a Foreign Company is defined as "a company other than a Myanmar Company, or a Special Company established under the terms of the Special Company Act 1950" (Myanmar Companies Act, Article 2, Clause I, Item 2B).

1 DICA and Local law firms A and B all agree on this point.

As noted above, therefore, there is nothing in the Myanmar Companies Act to prevent either a foreign investor or Foreign Company from buying shares in a Myanmar Company. In practice, however, as pointed out by Local law firm A, in the event that an investment target company was originally established as a Myanmar Company under the terms of the Myanmar Companies Act[2], the Company Registration Office (CRO) will not recognize a transfer of its shares (including new shares issued by the company) between members of the Myanmar public, in their capacity as shareholders in the Myanmar Company in question, and a foreign investor or Foreign Company. According to responses provided by Local law firm B, on the other hand, neither a foreign investor or Foreign Company can buy shares in a Public Company but they can buy shares in a Public Company. In answer to questions posed on this point during the course of our meetings, representatives of DICA and the CRO suggested that if the legal status of a Myanmar Company targeted for investment were to be changed to that of a Foreign Company, there would no longer be any obstacle to the acquisition of shares in the Myanmar Company by either a foreign investor or a Foreign Company. According to Local law firm A, however, there is no legal provision for such a change of legal status from a Myanmar Company to a Foreign Company and they cannot, in fact, find any precedent for such a change.

This difference of opinion between Local law firms A and B could well be due to their predicating their responses on different premises. In other words, while one may be based on comprehensive research into current practice including whether or not an investment target in the shape of a Myanmar Company can change its legal status to that of a Foreign Company, the other may be ignoring this question and providing a purely theoretical response based on whether or not a foreign investor or Foreign Company may be permitted to buy shares in an investment target company (both Myanmar Company and Private Company). One way or another, the primary prerequisite if the GEDF is to be permitted to buy shares in a Myanmar Company targeted for investment must be for the government of Myanmar to enact legislation to enable a Myanmar Company to change its legal status to that of a Foreign Company, thereby making it possible in practice for a foreign investor or Foreign Company to acquire shares in a Myanmar Company[3].

(b) Limitations placed on Public Companies

Under the terms of the Myanmar Companies Act, there is nothing to preclude a foreign investor or Foreign Company from buying shares in a Public Company or from establishing a Public Company. According to Local law firm B, however, it is not possible in practice for a foreign investor or Foreign Company either to establish a Public Company or to buy shares in a Public Company.

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2 As noted in Chapter 2 1-2. (3) (a) "Procedures and time required for the establishment of a Foreign Company" below, a company may be established in Myanmar under the terms either of the Myanmar Companies Act or of the Foreign Investment Law.

3 Local law firm A suggests that given the limitations currently place in practice on the acquisition of shares in a Myanmar Company by a foreign investor or Foreign Company, an alternative way of structuring the proposed fund would be (1) for the GEDF to establish a Foreign Company (under the terms of either the Foreign Investment Law or the Myanmar Companies Act) as a receptacle company, and (2) for the investment target company to transfer its assets to said receptacle company. It should be noted, however, that if this alternative approach were to be adopted, careful attention would need to be paid to the plethora of individual conditions attaching to the transfer of assets.

Therefore, we believe that it will be necessary for the Myanmar government to revise the restrictions currently imposed in practice on the acquisition of shares in a Public Company by the GEDF.

(2) Business restrictions

The Financial Institutions of Myanmar Law places no direct limitations on such business activities as would be carried out by the GEDF and its associated investment management company[4]. During our meeting with the Central Bank of Myanmar, however, we were advised that the Financial Institutions of Myanmar Law, currently under revision, and the proposed Myanmar Securities Exchange Law may include provisions relating to such business activities and that we should consequently keep a close eye on developments in this area.

1-2 Considerations on structure

(1) Share acquisition vehicle

As noted in Chapter 2 1. 1-1 (1) "Practical restrictions on the transfer of shares" above, a foreign investor or Foreign Company is prevented in practice from acquiring shares in a Myanmar Company. Therefore, the question is whether there is some form of entity that can be used to acquire shares in a Myanmar corporation (hereinafter referred to as the "acquisition vehicle")[5] that would not be subject to this practical restriction. Structure 1 shown in Chart 5 attempts to avoid the practical restriction against the acquisition of Myanmar Company shares by a Foreign Company by having a Special Company hold all of the voting rights in the share acquisition vehicle.

In addition to Myanmar Companies and Foreign Companies established under the terms of the Myanmar Companies Act, the laws of Myanmar also provide for the establishment of a Special Company under the terms of the Special Company Act. Local law firms A and B both note in their responses that while there is no express provision in the Special Company Act, joint ventures with a Myanmar government institution can be established in the form of Special Companies.

Under the terms of the Myanmar Companies Act, a Special Company is not defined as a Foreign Company (Myanmar Companies Act, Article 2 (I) (2b)). Thus, if a share acquisition vehicle in the form of a subsidiary of a Special Company were set up as a joint venture with a Myanmar government institution, there is in theory no reason why it should be subject to the restrictions imposed on the acquisition of shares in Myanmar Companies by a foreign investor or Foreign Company, as described in Chapter 2 1. 1-1 "Problems of investing in Myanmar" above.

According to Local law firm A, however, Special Companies are in practice set up to carry out a single specific business activity and would not normally be permitted to hold shares in another company. Such a vehicle might thus be precluded from acquiring shares in a Myanmar Company in the same way as a foreign investor or Foreign Company, albeit for a different

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4 It should be noted, however, that if the GEDF were to lend money to an investment target company, it would be deemed to be a finance company and would also fall as such within the ambit of the Financial Institutions of Myanmar Law, whereby it would be required to obtain prior permission for its activities from the Central Bank of Myanmar (Financial Institutions of Myanmar Law, Article 12).

5 This corresponds to the Growth-Enterprise Development Fund shown in the structure chart.

reason. For its part, on the other hand, DICA gave us to understand that if the articles of incorporation of a Special Company and its relevant joint venture agreement specified "investment" as its intended business activity, then it would be permitted to hold shares in other companies.

In its responses, DICA also suggested, however, that a joint venture between a Foreign Company and Myanmar government institution would also be treated as a Special Foreign Company. In light of the above, the subsidiary of a Special Company incorporated as a share acquisition vehicle by joint venture with a Myanmar government institution would be prohibited from buying shares in Myanmar Companies in the same way as a Foreign Company, as described in Chapter 2 1. 1-1 (1) "Practical restrictions on the transfer of shares" above,

To judge from the above, if the GEDF is to realize its objective of investing in Myanmar Companies in spite of the limitations currently placed on share transfers as described in Chapter 2 1. 1-1 (1) "Practical restrictions on the transfer of shares" above, Myanmar's government will need to take steps to reform the current treatment of joint ventures and the subsidiaries of joint ventures between foreign investment companies and government institutions as Special Foreign Companies.

(2) Fund raising vehicle

Even were the Myanmar government to reform the way in which joint ventures between Myanmar government institutions and foreign investors are treated, as described above, and use a Special Company established under Myanmar laws and regulations, it is our considered opinion that a partnership or company established overseas should be used as the entity for raising funds from investors (hereinafter referred to as the "fund raising vehicle")[6]. Our view is based on the assumption that if individual investors were to invest directly in a Myanmar Company, each would be variously subject to the procedures required by the Foreign Investment Law and/or the Myanmar Securities Exchange Law, thereby unnecessarily complicating the flow of funds between foreign investors and the GEDF[7].

(3) Other points from the survey

Following is a summary of other points that arose during the course of our survey concerning the structure of the proposed fund.

(a) Procedures and time required for the establishment of a Foreign Company

There look to be two main ways in which a Foreign Company can be established, namely (1) by obtaining an investment permit from the Myanmar Foreign Investment Committee

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6 This corresponds to the offshore fund shown in the structure chart.

7 If the GEDF itself were to be set up as a Special Company in joint venture with a Myanmar government institution, each individual investor would have to be made party to the joint venture agreement, thereby rendering it impractical as a scheme for the raising of funds from multiple investors.

(MIC), as provided for under the terms of the Foreign Investment Law[8], and (2) as a services company under the terms of the Myanmar Companies Act.

Procedure for the establishment of a Foreign Company as per (1) above is outlined below[9].

- Promoter or investor forwards proposal documentation to MIC.
- MIC carries out initial appraisal of proposal document, after which government issues business permit (including such conditions as may apply to the type of business activities envisaged for the proposed company).
- Request to registrar of companies to obtain establishment permit from Ministry of National Planning and Economic Development when company established.
- Register establishment of company.

Under the terms of the new Foreign Investment Law, submission of the proposal documentation to MIC and the request to the Ministry of National Planning and Economic Development to issue an establishment permit must take place simultaneously, as also must the granting of permission by MIC, issuance of the establishment permit by the Ministry of National Planning and Economic Development, and registration of the newly established company. If so requested, however, the Ministry of National Planning and Economic Development may also issue a provisional establishment permit and provisional registration.

Procedure for the establishment of a Foreign Company as per (2) above is outlined below.

- Request to registrar of companies to obtain establishment permit from Ministry of National Planning and Economic Development when company established.
- Register establishment of company.

According to Local law firm B, once it has obtained its establishment permit and registered its establishment, as required by Article 27A of the Myanmar Companies Act, the GEDF and its investment management company must also apply for a Business License.

8 Notification No.1/2013, a subordinate law to the Foreign Investment Law, lists (1) businesses in which investment by foreign investors is prohibited, (2) businesses permitted only in joint venture with the people of Myanmar, and (3) businesses permitted only under specified conditions. The proposed business activities of the GEDF and investment management company themselves are not listed and it seems likely that, based 100% on foreign capital, they would be permitted but if an investment target company's business is listed among the prohibited or restricted business types above, any investment of funds in the investment target company is likely to be either prohibited or restricted in some way.

9 Under the terms of the new Foreign Investment Law, Article 20(b), MIC must approve or reject a proposal within 90 days of receiving submission of proposal documentation. However, as described in Chapter 2. 1-5 below, since the new Foreign Investment Law Enforcement Ordinance has only recently been promulgated, it is still too early to see how procedures will actually be handled in practice under the new law .

We were also advised by both Local law firm B and DICA that when a new company is established, the specific business area in which it intends to operate must also be specified as one or other of (a) Trading, (b) Services, (c) Industry and manufacturing, (d) Hotel Business, (e) Tourism, (f) Gemstones Enterprise, (g) Construction, and (h) Banking[10], but according to DICA, as the area in which the proposed GEDF and investment management company would operate is new to Myanmar, it is not as yet clear whether it should be incorporated under (b) Services or not. It is conceivable, therefore, that establishment of the company would not in practice be permitted under approach (2).

(b) Number of directors and qualifications

While the Myanmar Companies Act stipulates the number of directors of a Public Company as three or more (Myanmar Companies Act, Article 83(A), Clause 1), there are no legal requirements concerning the numbers of directors of a Private Company.

However, the answers provided by local law firms A and B state that CRO usually requires registration of at least two directors. In addition, while it is not a statutory requirement under the Myanmar Companies Act to establish a board of directors, CRO usually requires it according to Local law firms A and B.

Under the Myanmar Companies Act, qualifications of directors do not require them, unless otherwise provided for in the articles of association of the company, to hold the company's shares (Myanmar Companies Act, Article 85, Clause 1[11]). In addition, the Local law firm A states that there are no requirements concerning a director's nationality or residence.

(c) Preferred shares and related matters

Under the Myanmar Companies Act, a company is allowed to issue redeemable preference shares if it is provided for in the articles of association (Myanmar Companies Act, Article 105B). Preference shares can be non-voting shares. No restriction is imposed on the issue amount and number of redeemable preference shares according to the answers of Local law firm A. However, the Myanmar Companies Act allows the redemption of redeemable preference shares only when the company records profits and has paid the full amount to be paid in for the preference shares in question (Myanmar Companies Act, Article 105B).

Although shares issued by a Myanmar Company have a par value, there is no provision in the Myanmar Companies Act that restricts a premium issue (issuance of shares of which the issue price is greater than the par value). However, the issue price of new shares must in practice be equal to par value because CRO does not approve premium issues according to Local law firm A.

According to answers from Local law firms A and B, there is currently neither provision concerning share options in the Myanmar Companies Act nor are they issued in practice.

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10 By means of Notification No.1/2013, DICA announced that from February 22, 2013, instead of selecting the intended business area from eight business categories during company registration, the intended business area will be copied unchanged from the articles of incorporation. However, according to answers from Local law firm A, an intended business are that matches one of the eight categories is demanded during the company registration process.

11 According to Local law firms A and B, a promoter is not required to hold shares in the company he is promoting.

(d) Capital and related matters

The Myanmar Companies Act makes no provision concerning a company's minimum capital.

On the other hand, DICA's website indicates a minimum capital requirement for Foreign Companies operating in the following business areas.

Table 5 Foreign Companies' minimum capital requirement by business type

Business type	Minimum capital
Industrial, Hotel, and Construction	USD 150,000
Services, Travels and Tours company, Bank Representative office, Insurance Representative office	USD 50,000

According to Local law firm A, the minimum capital must be paid in full at the time of incorporation. Providing the minimum capital requirement is met, directors of the company may decide any capital amount to be paid at incorporation that is 5% or more of the par value of shares and more than the minimum capital requirement (Myanmar Companies Act, Article 101, Clauses 2 and 3). The shareholders are not obligated to pay in the capital not paid at incorporation until the company makes the call (however, neither are the shareholders prevented from making voluntary payments) (Myanmar Companies Act, Article 49, Clause 2). However, Local law firm A stated that MIC may impose other requirements on companies established under the Foreign Investment Law.

According to the answer from Local law firm A, payment status is recorded in the shareholders' register, and on stock certificates and Form VI to be submitted to CRO.

The Myanmar Companies Act requires existing shareholders to be offered an opportunity to subscribe for their pro rata share of the new shares when a company increases its capital (Myanmar Companies Act, Article 105C). If a shareholder rejects the offer, the company may offer the right to other existing shareholders and third parties (Myanmar Companies Act, Article 105C). However, MIC's approval must be obtained before a capital increase in the case of a company established pursuant to the Foreign Investment Law, according to Local law firm A.

Under the terms of the Myanmar Companies Act (Article 54A, Clause 1), share buybacks are permitted only as part of a capital reduction. However, according to Local law firm A, in the case of a company established under the Foreign Investment Law, the approval of both MIC and CRO is necessary before a capital reduction and share buyback can go ahead. On the other hand, in the case of a company established pursuant to the Myanmar Companies Act, only CRO's approval is necessary. Local law firm B states that CRO deems capital reductions to be undesirable with the result that it does not approve them in practice.

(e) Debentures

Although provisions for debentures exist in the Myanmar Companies Act (clauses after Article 126), issuance of debentures is not currently practiced in Myanmar according to Local law firms A and B. The Myanmar Companies Act does not have provisions for equity-linked debt such as convertible bonds.

(f) Dividends

Under the Myanmar Companies Act, a company may, with a resolution of the general meeting of shareholders, pay a dividend from the company's current fiscal year profit, provided it remains within the limit recommended by the directors of the company (Articles 95 and 97 of Table A, which are deemed to be included in the articles of association of the company in accordance with the Myanmar Companies Act, Article 17, Clause 2). The Foreign Investment Law also recognizes the right of foreign investors to remit net income after the deduction of tax payable abroad (Foreign Investment Law, Article 39, Clause c).

According to the answers of Local law firms A and B, a company established under the Foreign Investment Law needs prior approval from MIC for the payment of a dividend. On receipt of said approval, the company may pay a dividend within the limit recommended by the company's board of directors and approved by a resolution of a general meeting of shareholders.

1-3 Fund Structures

The advantages and disadvantages of each structure that were presented at the beginning of this chapter are summarized in the following table. However, if, as described in Section 1-2(1) "Share acquisition vehicle", we assume that a joint venture between a foreign investor and a Myanmar government institution is treated for practical purposes as a Special Foreign Company, there might not be a significant difference between the two from a legal standpoint.

Table 6 Advantages and disadvantages of each structure

Structure	Advantages	Disadvantages
(1) Establish an investment management company as a joint venture with the Myanmar government (Special Company), with the GEDF as its subsidiary. Establish partnership or company overseas to raise funds for investment in the GEDF.	− In theory, a Special Company is not a Foreign Company but is, under the terms of the Myanmar Companies Act, a Myanmar company with the result that there is in theory only a fairly low risk that CRO may refuse to register shares acquired by the Special Company in other Myanmar Companies. According to DICA, however, since any joint venture formed between a foreign investor and a Myanmar government institution is likely to be treated as a Special Foreign Company, along with any of its subsidiaries, registration by the CRO of such shares as may be transferred to the company is not a foregone conclusion. − A Special Company is not required to obtain a permit from the President of Union, which is usually required under the Myanmar Companies Act.	− Advice from DICA is that as a subsidiary of a Special Foreign Company, the GEDF will also be treated as a Special Foreign Company, with the result that CRO may not in practice agree to register transfers of shares in other Myanmar companies (including new shares issued by investment target companies). − In practice, Special Companies are not normally allowed to hold shares of other companies with the result that the investment management company may not be allowed to hold shares in the GEDF[12]. −
(2) Establish GEDF and investment management company as Foreign Companies. A partnership or corporation established overseas raises capital, which it then invests in the GEDF.	There is no need for negotiations to establish a joint venture with a Myanmar government institution or for an investment from a Myanmar government institution. There is no need to share returns on investment with a Myanmar government institution or other party. − There are many precedents for the establishment of a Foreign Company, so the procedures have a high level of predictability.	− The CRO may not in practice agree to register transfers of shares in other Myanmar companies (including new shares issued by investment target companies). − Because it would not be a Special Company, it would be necessary to obtain a permit from the President of the Union as required in the Companies Act.

1-4 Target companies by type

Based on key points to emerge from our research to date, as detailed in Sections 1-1 "Problems of investing in Myanmar" and 1-2 “Consideration on structure” above, in the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), its ability to acquire shares in investment target companies will likely depend on the type of company targeted, as summarized below[13].

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12 According to DICA, as long as the Special Company's proposed business activity is shown as "investment" in both its articles of incorporation and the joint venture agreement, it should have no problem acquiring shareholdings in other companies.

13 According to Local law firm B, foreign investors are not permitted to become shareholders in state-owned companies. Moreover, (1) permission to invest in a Special Company following its establishment, and (2) permission to invest in a joint venture between a Myanmar Company and a state-owned company are decided on a case-by-case basis.

Table 7 Acquisition of shares in target companies

Investment target company type	Foreign Company (100% foreign capital)	Myanmar Company	Joint venture between Myanmar Company and Foreign Company
Private Company with MIC investment permit	- As the investment target company is a Foreign Company, share acquisition should be possible under both the Myanmar Companies Act and the Foreign Investment Law, and also in practice	* It is theoretically impossible for a company of this type to exist	- As the investment target company is a Foreign Company, share acquisition should be possible under the Myanmar Companies Act (according to Local law firm A, a fresh investment permit will need to be obtained from MIC). - For shares acquired from a shareholder that is a Myanmar Company, the holding ratio may be limited if the investment target company's business activities are subject to restriction under the Foreign Investment Law.
Private Company without MIC investment permit	- As the investment target company is a Foreign Company, share acquisition should be possible both under the Myanmar Companies Act and in practice.	- As the investment target company is a Myanmar Company, acquisition of its shares may not in practice be permitted. - Even if acquisition of its shares were permitted, if the investment target company's business activities are prohibited under the Foreign Investment Law, share acquisition will not in practice be permitted, and if its business activities are subject to restriction under said law, the holding ratio may be limited.	- As the investment target company is a Foreign Company, share acquisition should be possible both under the Myanmar Companies Act and in practice. - For shares acquired from a shareholder that is a Myanmar Company, the holding ratio may be limited if the investment target company's business activities are subject to restriction under the Foreign Investment Law.

(Table 7 continued)

Investment target company type	Foreign Company (100% foreign capital)	Myanmar Company	Joint venture between Myanmar Company and Foreign Company
Public Company with MIC investment permit	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be able to buy shares in a Public Company. - It appears that shares may be acquired under the terms both of the Myanmar Companies Act and of the Foreign Investment Law. * According to Local law firm A, since a foreign investor or Foreign Company may neither set up a Public Company nor buy shares in a Public Company, companies of this type may not in practice exist.	* It is theoretically impossible for a company of this type to exist	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be able to buy shares in a Public Company. - It appears that shares may be acquired under the terms of the Myanmar Companies Act (according to Local law firm A, a fresh investment permit will need to be obtained from MIC). - For shares acquired from a shareholder that is a Myanmar Company, the holding ratio may be limited if the investment target company's business activities are subject to restriction under the Foreign Investment Law. * According to Local law firm A, since a foreign investor or Foreign Company may neither set up a Public Company nor buy shares in a Public Company, companies of this type may not in practice exist.

(Table 7 continued)

Investment target company type	Foreign Company (100% foreign capital)	Myanmar Company	Joint venture between Myanmar Company and Foreign Company
Public Company without MIC investment permit	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be able to buy shares in a Public Company. - It appears that shares in a Public Company may not be acquired by a Foreign Company under the terms of the Myanmar Companies Act. * According to Local law firm A, since a foreign investor or Foreign Company can neither set up a Public Company nor buy shares in a Public Company, companies of this type may not in practice exist.	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be able to buy shares in a Public Company. - Even if acquisition of its shares were permitted, if the investment target company's business activities are prohibited under the Foreign Investment Law, share acquisition will not in practice be permitted, and if its business activities are subject to restriction under said law, the holding ratio may be limited.	- In the event the GEDF is deemed to be a Foreign Company, it may not in practice be able to buy shares in a Public Company. - It appears that shares may be acquired under the terms of the Myanmar Companies Act. - For shares acquired from a shareholder that is a Myanmar Company, the holding ratio may be limited if the investment target company's business activities are subject to restriction under the Foreign Investment Law. * According to Local law firm A, since a foreign investor or Foreign Company can neither set up a Public Company nor buy shares in a Public Company, companies of this type may not in practice exist.

Table 8 Establishment of new joint venture

Joint venture type	Foreign Company (100% foreign capital)	Joint venture between Myanmar Company and Foreign Company	Special Company
Private Company with MIC investment permit	- Providing the company's business is neither prohibited nor subject to restrictions under the Foreign Investment Law, there does not appear to be anything either in said law or in practice that would preclude the establishment of a joint venture financed 100% by foreign capital.	- In the event the company's business activities are subject to restrictions under the Foreign Investment Law, investors' capital interest will be confined to a maximum of 80% (Foreign Investment Law, Article 10 (a) (iv), Foreign Investment Law Enforcement Ordinance, Article 20).	- The situation must be discussed with a government institution.
Private Company without MIC investment permit	- Providing the company's business is neither prohibited nor subject to restrictions under the Foreign Investment Law, there does not appear to be anything either in said law or in practice that would preclude the establishment of a joint venture financed 100% by foreign capital.	- In the event the company's business activities are subject to restrictions under the Foreign Investment Law, investors' capital interest will be confined to a maximum of 80%.	

(Table 8 continued)

Joint venture type	Foreign Company (100% foreign capital)	Joint venture between Myanmar Company and Foreign Company	Special Company
Public Company with MIC investment permit	- Since a Foreign Company is numbered among the shareholders, it may not be possible in practice to establish a Public Company.	- Since a Foreign Company is numbered among the shareholders, it may not be possible to establish a Public Company. - In the event the company's business activities are subject to restrictions, investors' capital interest will be confined to a maximum of 80% (Foreign Investment Law, Article 10 (a) (iv), Foreign Investment Law Enforcement Ordinance, Article 20).	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be possible to establish a Public Company. - The situation must be discussed with a government institution.
Public Company without MIC investment permit	- Since a Foreign Company is numbered among the shareholders, it may not be possible in practice to establish a Public Company.	- Since a Foreign Company is numbered among the shareholders, it may not be possible to establish a Public Company. - In the event the company's business activities are subject to restrictions under the Foreign Investment Law, investors' capital interest will be confined to a maximum of 80%.	- In the event the GEDF is deemed to be a Foreign Company (including Special Foreign Company), it may not in practice be possible to establish a Public Company. - The situation must be discussed with a government institution.

1-5 Progress to date on related laws and ordinances

According to Local law firm D and reports in local media, the situation to date with respect to laws and ordinances potentially relevant to the way in which the proposed fund is structured is as follows.

Table 9 Progress to date on related laws and ordinances

	Law / Ordinance	Progress to date
1.	Foreign Investment Law	New Foreign Investment Law implemented with effect from 2/11/2012
2.	Foreign Investment Law Enforcement Ordinance	Promulgated on 31/1/2013 by the Ministry of National Planning and Economic Development. List of businesses for which foreign investment approved published on same date.
3.	Foreign Exchange Management Law	Former Foreign Exchange Law revised and replaced as of August 2012 by the Foreign Exchange Management Law.
4.	Financial Institutions of Myanmar Law	New Financial Institutions of Myanmar Law in process of being drafted.
5.	Myanmar Citizen Investment Law	New Myanmar Citizen Investment Law bill approved by parliament. Enactment expected in very near future.
6.	Myanmar Securities Exchange Law	Myanmar Securities Exchange Law bill approved by parliament. Enactment expected in very near future.
7.	Central Bank of Myanmar Law	New Central Bank of Myanmar Law bill approved by parliament. Enactment expected in very near future.
8.	Myanmar Companies Act	No revisions in immediate prospect but the act is currently under review by the Drafting Committee

1-6 Conclusions

Following is a summary of our research and of our deliberations based on said research.

Given that foreign investors and Foreign Companies are currently and for all practical purposes prohibited from buying shares in a Myanmar Company, the biggest obstacle to the structuring of our proposed fund is the fact that a joint venture with a Myanmar government institution (including its subsidiaries) is treated as a Special Foreign Company. If this way of treating Foreign Companies were to be revised, however, our fund might well be structured as shown in (1) of Chapter 3 1. above.

On the other hand, if it proves impossible to revise the current practice of treating a joint venture with a Myanmar government institution as a Special Foreign Company, an alternative would be root and branch reform of the current situation whereby foreign investors and Foreign Companies are effectively prevented from acquiring shares in Myanmar Companies. This could open the way for the GEDF not only to acquire shares in its investment target companies[14] but also, and more particularly, looking further ahead, to list such companies and (having changed their status to Public Companies) to offer their shares for sale in the secondary market.

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14 Even in the current business environment, share acquisition should be possible based on the alternative strategy outlined in Note 3.

One further obstacle to progress on this front is DICA and the Central Bank of Myanmar's reluctance to say clearly whether the proposed fund structure would be viable under the law as it stands today. This reluctance they attribute this to the fact that the drafting of relevant legislation is as yet incomplete. If we are to eliminate these impediments and implement the proposed fund structure at an early date, we need to negotiate directly with the relevant public institutions.

1-7 Supplementary considerations: Limitations placed on fund raising vehicles (off-shore funds) by Japanese law

(1) Fund raising vehicle as partnership

If the fund raising vehicle were to be set up as a partnership, such limitations as may be imposed under Japanese law on said vehicle and its investment management company are summarized below.

First, under the terms of the Financial Instruments and Exchange Law (FIEL), if the proposed business activity of the partnership is to establish a fund (collective investment scheme), to invite Japanese investors to acquire shares in it (self-offering: FIEL Article 2, Clause 8, Item 7), and to invest the fund's assets primarily in securities (self-management: FIEL Article 2, Clause 8, Item 15), it will fall within the definition of a "financial instruments business" and the partnership will in principle be required to register as a financial instruments business operator (FIEL Article 29).

Much will depend of course on specifics such as the particular characteristics of the adopted scheme and the various interested parties but as far as the requirement to register the self-offering of shares in the fund is concerned, the likelihood is that (1) the fund, in the shape of a general partnership (GP) formed by parties registered as financial instruments business operators (financial instruments business type 2), will opt for self-offering, (2) (in the event the requirements of a designated fund for professionals are met) the GP will undertake self-offering based on the filing of notifications of specially permitted business in respect of qualified institutional investors (FIEL, Article 63, Clause 1, Item 1), or (3) the GP will entrust all self-offering related external activity to a financial instruments business operator. As for registration of the fund with respect to self-management, the likelihood is that (1) operators registered as financial instruments business (investment management business) operators will form the GP and carry out self-management, (2) (in the event the requirements of a designated fund for professionals are met) the GP will undertake self-management based on the filing of notifications of specially permitted business in respect of qualified institutional investors (FIEL, Article 63, Clause 1, Item 2), or (3) the GP will conclude a discretionary investment contract with a registered investment manager to whom all rights to self-management will then be entrusted (FIEL Enforcement Ordinance, Article 16, Clause 1, Item 10).

Funds for investment exclusively in securities will fall to be dealt with on the basis of "securities investment business rights" (see FIEL, Article 3, Item 3) and will be subject as such to disclosure regulations. If, under these circumstances, the fund has upwards of 500 shareholders, the solicitation to acquire shares will be treated as a "securities offering" and will as such require disclosure in the shape, for example, of the submission of a securities registration statement.

Next, as far as the Foreign Exchange and Foreign Trade Act (hereafter, "Foreign Exchange Act") is concerned, shares in an unincorporated foreign partnership are not deemed to fall within the meaning of "securities" as defined in the Act (Foreign Exchange Act, Article 6, Clause 1, Item 11) with the result that the acquisition of a share of this sort does not entail processing as an outward direct investment or capital transaction. However, payments with respect to the acquisition of such a share must be reported separately (Foreign Exchange Act, Article 55, Clause 1).

(2) Fund raising vehicle as company

If the fund raising vehicle is structured in the form of a company, unlike a partnership it will not be subject to regulation under the terms of the Financial Instruments and Exchange Law with respect to self-offering and self-management. Such parties as may enter into an investment advisory contract (FIEL, Article 2, Clause 8, Item 11) or discretionary management contract (FIEL, Article 2, Clause 8, Item 12) with the fund raising vehicle for management of the fund's investments may be subject to regulation under the terms of FIEL. Since management activity of this sort does not require special permission to engage in specially permitted business as a qualified institutional investor, the involvement of operators registered for financial instruments business may be possible (depending on the circumstances of individual cases, since the investment activity in question takes place outside Japan, it may be exempt from regulation under the terms of Japan's FIEL in the same way as the investment management company of the GEDF in Chart 2 below). The application of disclosure regulation under the terms of FIEL may also be a subject for debate depending on whether investment in the domestic investment vehicle takes the form of investment in shares (investment certificates) or an investment agreement.

Under the terms of the Foreign Exchange Act, outward direct investment procedures must be undertaken in addition to a payment-related report. The vehicle may also fall within the definition of a foreign investment company, in which case legal requirements pertaining, for example, to the filing of notifications as in the case of investment trusts and investment companies will need to be met.

(3) Regulation of the GEDF's investment management company

Much will of course depend on the precise characteristics of the scheme and interested parties and on the nature of the business activities undertaken but providing the GEDF's investment management company is established in Myanmar, or indeed anywhere other than Japan, and confines itself exclusively to management of the fund's investments (in this case, investment of funds, raised through an offshore fund, in Myanmar Companies within Myanmar itself), it should not be subject to regulation under Japanese laws such as the Financial Instruments and Exchange Law.

2. Considerations on Taxation

To consider the tax implications, we used interviews with a global tax advisory firm and a large local accounting firm as the basis for investigating and examining under which structure the projected GEDF would have the best tax effects, and what tax relations would affect an investment management company to be established in Myanmar. We started by envisaging a number of basic patterns. The premises, issues, and results of these investigations are set out below.

2-1 Assumptions and Estimated Patterns

(1) Assumptions

Considering the survey and discussion results in other items, we set the following assumptions:

(a) Each investor of the fund is a Japanese resident for tax purposes.

(b) The fund invests in stock of companies.

(c) Each investee is a Myanmar resident for tax purposes.

(d) The fund's ownership ratio in each investee is less than 50%.

(e) Effective corporate income tax rate in Japan is 38%.[15]

(2) Estimated Patterns

Based on the above assumptions, we estimate and discuss the following four patterns of the fund's location and investment structure:

(a) Direct investment from Japan;

(b) Investment through a fund established in Myanmar;

(c) Investment through a fund established in a low tax jurisdiction; and

(d) Investment through a fund established in a country that has a tax treaty with Myanmar.

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15 In response to the revision of the corporate income taxation system following the "Act on Partial Revision for the Income Tax Act, etc., for the Purpose of Creating Taxation Systems Responding to Changes in Economic and Social Structures" passed and enacted on November 30, 2011 and promulgated on December 2, 2011, the corporate income tax rate was lowered from 30% to 25.5%. Along with this, the effective corporate income tax rate was also lowered from 40.69% to 35.64%. Then, however, it was decided that a special reconstruction tax calculated by multiplying the base corporate tax amount of each taxable financial year by a 10% tax rate would be imposed for the financial years starting from April 1, 2012 to March 31, 2015. As a result, for the special reconstruction corporate tax applicable fiscal year, the corporate tax rate has been set at 28.05% (25.5% * (1 + 10%)), even though it was lowered from 30% to 25.5% along with the afore-mentioned revision in December 2011 and the effective corporate tax that was supposed to be lowered to 35.64% is now 38% as shown in the formula below.

[Corporate income tax rate 25.5% * {1 * (1 + 10%) + Resident tax 20.7%} + (Business tax excessive tax rate 3.26% + Business tax standard tax rate 2.9% * Special local corporation tax 148%)]/(1 + Business tax excessive tax 3.26% + Business tax standard tax rate 2.9% * 148%) = 38.009% ≒ 38%.

2-2 Major Issues

Investors of the fund acquire stock of companies in Myanmar through the fund. When the fund sells stock of the Myanmar companies and distributes the sales proceeds to the Japanese investors or when the fund temporarily keeps the sales proceeds of stock as an asset of the investors, because the Japanese income tax law levies tax based on the worldwide income of a Japanese resident, we consider the following Japanese tax legislation stipulating tax relations on foreign income earned by a Japanese resident will become a major issue in this examination.

(1) Anti-tax haven taxation (Controlled foreign company taxation)[16]

Anti-tax haven rules have been introduced to combine the income of a company established in a tax haven country (specified foreign subsidiary) with the income of a taxpayer in Japan, and impose taxes on such combined income to the taxpayer in Japan for the purpose of preventing the Japanese taxpayer from illegally reducing tax burdens by means of pursuing business through a paper company or alike, established in the tax haven country.

When a Japanese individual or corporate owns more than 10% of the stock of a specified foreign subsidiary at the end of the fiscal year of the said subsidiary, the said Japanese individual or corporate is required to file taxable income of the said specified foreign subsidiary corresponding to its share as taxable income in Japan. The income tax and other relevant taxes, however, paid by the specified foreign subsidiary in a tax haven country are adjusted by a deduction in Japan. When the specified foreign subsidiary provides after-tax dividends for shareholders in Japan, 95% of the dividends naturally become non-taxable, provided the foreign dividend exclusion mentioned below is applied to the dividends. When shareholders in Japan have a tax amount imposed by the anti-tax haven rules in the related fiscal year and for the last ten years (specified taxable amount), up until the specified taxable amount is fulfilled, 100% of dividends from the specified foreign subsidiary become nontaxable, instead of 95%, and the withholding tax on dividends is included in deductible expenses. Furthermore, even if the dividends from the specified foreign subsidiary are not subject to foreign dividend exclusion from the income of the specified foreign subsidiary, the related dividends are excluded from income within the range of the specified taxable amount.

A specified foreign subsidiary means a company of which more than 50% of shares outstanding or paid-in capital is, regardless of directly or indirectly, held by a corporate or individual who is a Japanese resident (or a non-resident individual who has a special relation with a Japanese corporate) and a company whose head office or main office is located in a country where no tax is levied on income or a country where the effective tax rate on income is less than 20%.

Because all investors of the GEDF are assumed to be Japanese residents, depending on the effective tax rate, the fund may be applicable as a specified foreign subsidiary for an investor.

Anti-tax haven rules have the exemption provisions (a) to (e) below. In case a specified foreign subsidiary mainly engaging in the wholesale trade, bank, trust banking, insurance, securities, water transportation, or air transportation business satisfies all the requirements of (a) to (d), or a specified foreign subsidiary engaging in any business other than the said businesses satisfies all the requirements of (a) to (c) and (e), such subsidiary is exempted from the related taxation.

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16 Act on Special Measures concerning Taxation

Based on the facts, however, that the GEDF's main business is to hold shares and accordingly the fund does not satisfy requirement (a), the exemption provisions of the tax haven rules do not apply to the fund.

(a) Business criteria: The principal business of a specified foreign subsidiary shall not correspond to any business of holding equities and bonds, providing patents, copyrights, or other licenses, or leasing of vessels or aircraft.

(b) Entity criteria: A specified foreign subsidiary shall have an office(s), store(s), plant(s), or other fixed business place(s) necessary for pursuing the business at the location of its head office.

(c) Management and control criteria: A specified foreign subsidiary shall itself conduct management, control, and operation at the location of its head office.

(d) Non-affiliated person criteria: The business of a specified foreign subsidiary shall be performed mainly with other than affiliated persons (holding 50% or more of its shares).

(e) Local country criteria: The business of a specified foreign subsidiary shall be conducted mainly at the location of its head office.

When an investment target company has shareholders of Japanese residents other than the GEDF and Japanese residents hold a total of more than 50% of the investment target company's shares, the said investment target company may be applicable under a specified foreign subsidiary and anti-tax haven rules may be applied to taxable income of the said investment target company. However, such a risk cannot be prevented by the structuring of the fund, so we do not discuss the issue in this report.

(2) Foreign dividend exclusion[17]

95% of dividends received from a foreign subsidiary are not subject to corporate income tax of a Japanese parent company. However, withholding tax on such dividends cannot be tax deductible nor included in deductible expenses.

A foreign subsidiary means a foreign company satisfying the following 2 conditions in principle:

- 25% test: Japanese corporate directly holds more than 25% of shares of such company.
- 6 months test: Japanese corporate directly holds more than 25% of shares of such company for at least 6 consecutive months from the declaration date of dividend payment.

On the other hand, all dividends received from a foreign company other than a foreign subsidiary (a company in which Japanese corporate owns less than 25% of shares) are subject to tax, while withholding tax on such dividend is subject to foreign tax credit.

(3) Foreign tax credit[18]

When foreign income earned by a Japanese corporate is levied in a foreign country, the tax

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[17] Corporation Tax Act

[18] Corporation Tax Act

amount paid in the foreign country is deductible from the tax amount due in Japan, within the range of the amount calculated based on the following formula:

Deductible maximum amount = Income tax amount in Japan × Foreign income ÷ Worldwide income

Along with the introduction of a provision for deemed income tax withheld in 2011 tax system revision, it has been clarified that income subject to a foreign corporate income tax in a tax convention member country shall be treated as foreign income used in the formula for calculating the afore-mentioned deductible maximum amount even if the tax convention does not include any provision for withholding deemed tax. On the other hand, it has not been clarified whether or not income subject to a foreign corporate income tax in a tax convention non-member country should be treated as foreign income. As a result, the possibility of applying a foreign tax credit to this case is not clear, and if it is not applied, double taxation occurs.

2-3 Other Issues

Beside the aforementioned issues, there are 3 common issues for several estimated patterns as follows:

(1) Taxes on capital gains and dividends in Myanmar

Regardless of its location, the business of the fund consists of acquiring and selling shares of Myanmar companies, which is common to all structures. Estimated income from such business constitutes capital gains and dividends. The corporate income tax rates imposed on them are shown in the table below:

Table 10 Corporate income tax rate in Myanmar[19]

Type of Income	Resident Corporation (Corporation established under Myanmar Companies Act and Foreign Investment Law)	Non-resident Corporation (Foreign corporation including its branches established in Myanmar)
General business revenue	25%	35%
Capital gain[20]	10%	40%
Dividend[21]	Non-taxable	Non-taxable

(2) Transaction tax in Myanmar

In the case of a sale of stock of a Myanmar company, stamp duty of 0.3% shall be imposed on sales proceeds[22]. This stamp duty is not exempted by a tax treaty or structuring of the fund, and may have an effect on all patterns estimated.

19 The Myanmar Income Tax Law (1974) and Notification 111/2012 (March 15, 2012)

20 The tax rate applied on capital gains from selling non-current assets (including shares) in the oil and gas business is 40% to 50%.

21 Tax withholding is not applied to payments

22 The Myanmar Stamp Act (1891)

(3) Legal structure of domestic fund in Myanmar

As discussed in the legal survey in the preceding chapter, in the case of establishing a fund in Myanmar, there are 2 types of legal structure: corporation and partnership. However, Myanmar legislation does not specify any pass-through entity and a partnership seems to be tax levied under the Myanmar Income Tax Law (1974)[23], thus, using a partnership may not produce any particular tax advantage. Accordingly, we will consider all of the types of fund structure examined in this report as a corporate-type fund.

3. Evaluations and proposals for JICA cooperation

3-1 Significance of JICA's cooperation for GEDF

In December 2011, during his visit to Myanmar, Minister for Foreign Affairs Koichiro Gemba (at that time) praised the Myanmar government for implementing speedy measures to promote democracy and national reconciliation. In addition, Minister for Foreign Affairs announced support in four areas: human exchanges, economic cooperation, economic, and cultural exchanges. Of these four areas of support, in the area of economic cooperation, Japan has expressed its support for the transition to a market economy, and in the area of economics, talks are scheduled to begin on preparing the investment environment and forming an investment treaty to promote investment from Japan. Moreover, at the Japan-Myanmar Summit Meeting, held in April 2012, the leaders of both countries confirmed a road map for the resumption of yen-denominated loans. Prime Minister Yoshihiko Noda (at that time) told President Thein Sein that Japan would fundamentally review its policy for economic cooperation with Myanmar. A policy for wide-ranging support was conveyed centering on 3 main pillars: (1) improve the daily lives of the nation's citizens, (2) improve human resource capabilities and put a system in place to support the economy and society, and (3) develop the infrastructure and systems necessary for sustainable economic growth. In accordance with this policy, at the November 2012 Japan-Myanmar Summit, Prime Minister Noda (at that time) announced priority issues that Japan would actively support. Furthermore, Deputy Prime Minister Taro Aso visited Myanmar at the start of January 2013 and additionally announced solutions for outstanding debt and a resumption of yen loans. Then, at the end of January, Japan canceled 326.3 billion yen in outstanding debt and provided bridge loans to clear the way for new yen loans. On March 25, the Japanese government announced yen loans totaling up to 51.052 billion yen for three projects: "Regional Development Project for Poverty Reduction Phase 1," "Urgent Rehabilitation and Upgrade Project Phase 1," and "Infrastructure Development Project in Thilawa Area Phase 1."

Of the economic cooperation policies discussed above, one example of the second pillar—improve human resource capabilities and put a system in place to support the economy and society—is the development of a securities market, in other words the creation of a capital market. We believe it has become increasingly important to examine concrete details of JICA's development aid program for developing a capital market in Myanmar. The GEDF, which is the basic premise of our survey, is a fund to be established using capital from Japan's private sector, which aims to nurture growth companies that are to be the nucleus of Myanmar's economic growth. Promoting this fund as a series of packages, coupled with JICA's development aid tools, is expected to optimize benefits from assistance given to develop capital markets and make the transition to a market economy. The deployment of the GEDF in synch with JICA's development aid tools falls in line with the policy

[23] Internal Revenue Department, Ministry of Finance and Revenue (http://www.myanmar.com/finance/dept_ird_02.html)

highlighted on April 18, 2008 for a public-private sector partnership to accelerate growth.

The following is our assessment and proposals for JICA's assistance policies, which should produce benefits when carried out in conjunction with the GEDF.

3-2 Financial cooperation related to GEDF

Financial cooperation provided by JICA is divided broadly into 2 categories: grant aid and ODA loans assistance. However, grant aid is considered to have little affinity with GEDF, which is aiming to nurture a capital market, thereby putting in place key infrastructure for a market economy. For this reason, we judge that provision of support through grant aid and linkage of such a program with GEDF is unrealistic. Consequently, we decided to limit our investigation to ODA loans and the technical cooperation program.

(1) ODA loans

ODA loans chiefly consist of 2 programs: yen loans and overseas investment and financing. There are expected to enhance the effectiveness of the GEDF. Below, first we examine and offer proposals on the use of overseas investment and financing, which is believed to be the most directly effective, and then we examine and provide proposals on the use of yen loans.

(a) Overseas investment and financing

The various businesses carried out by private-sector companies in developing nations spark economic activity and create employment in those markets. Consequently, this triggers expectations of economic benefits that will bring about improved living conditions for the people in these countries. However, the high-risk, low-return forecasts for businesses set up in developing nations obstruct opportunities to receive financing from private-sector financial institutions. JICA's overseas investment and financing program supports both the investment and financing needs of private-sector companies in this situation.

Under the Reorganization and Rationalization Plan for Special Public Institutions, overseas investment and financing was temporarily halted in 2001. However, discussions in the global community led to an increased recognition that promoting private-sector activity in developing nations would trigger economic growth and reduce poverty in these countries. Consequently, Japan looked at resuming this program. After carrying out a pilot project and field tests, a decision to fully resume the program was made in October 2012. Implementing overseas investment and financing in conjunction with the GEDF is not merely an example of a single business launched by a private-sector company, but will contribute to the development of infrastructure needed for Myanmar's transition to a market economy through the establishment of a capital market and modernization. We believe that this example is highly significant as a useful format for new overseas investments and financing based on an increasing, clearly defined need.

As overseas investment and financing implemented in tandem with the GEDF, we see the possibility of investing in the fund or the investment management company. The fund's capital would be directly increased without any impact on its financial health. Meanwhile, from the standpoint of increasing investment capacity, although there is a relatively high risk involved with providing capital to companies in Myanmar, which is undergoing a transition to a market economy, we expect a high level of development benefits because this risk is to be shouldered by those providing capital and through the participation of JICA's overseas investment and financing program, which is essentially capital from the Japanese government. As a result, the creditability of the GEDF will be enhanced, making it possible to attract sufficient investment capital. In other words, we anticipate a pump-priming effect; therefore, we believe this is a suitable method of investment.

i) Compatibility with rules for leveraging overseas investment and financing

As a result of discussions on resuming overseas investment and financing, it was decided that projects would be selected in accordance with JICA's project selection policies on overseas investment and financing (as of October 16, 2012, referred to as selection policies hereafter). Accordingly, with regard to the GEDF, when examining the use of overseas investment and financing, it will be necessary to confirm whether the fund complies with JICA's selection policies.

- Target areas

  The 3 target areas for overseas investment and financing are MDGs/poverty reduction, infrastructure/growth acceleration, and climate change strategies. The objective of the GEDF is to foster the advancement of those growth companies that are the core of Myanmar's economic growth.

- Target models based on business format

  In the selection policies, a prerequisite of investment is that proper advance notice is given to the host country's government about the project to be implemented and, in principle, that a response is obtained. Giving consideration to these points, it will be necessary to seek out projects with high development benefits, which cannot be handled by existing financial institutions.

  Myanmar's capital market (direct finance) and its financial markets (indirect finance) are both underdeveloped. Private-sector companies will face difficulties procuring sufficient capital. Both Myanmar's government and its domestic financial institutions lack the expertise and experience to foster corporate development. In light of this, establishment of the GEDF and the developmental aid the fund is likely to provide to companies in Myanmar are expected to bestow substantial development benefits. Moreover, the government of Myanmar has positioned creating a capital market and shifting to a market economy as key issues. Given this, we consider the government of Myanmar is likely to actively participate in establishment of this fund, because it is closely connected to the formation of a capital market. In addition, to secure the understanding and cooperation of the government of Myanmar, talks are underway concerning setting up the fund management company jointly with a state-owned financial institution.

  In light of the above, we believe the fund is in compliance with JICA's basic concept on overseas investment and financing because JICA, which is an ODA agency, provides ODA loans to supply capital for a company's development, and because the project has a high development benefits and cannot be handled by an existing financial institution.

ii) Factoring in evaluations of past overseas investment and financing

As part of the assessment for resuming overseas investment and financing, external organizations are evaluating projects JICA implemented in the past[24]. We assume that an ex-post evaluation will be carried out when screening the use of overseas investment and financing in the fund. We believe it would be beneficial to reflect the track record, accomplishments, advice, and other factors indicated in this report in the scheme design.

Of overseas investment and financing projects carried out in the past, JICA participated in the following 2 investment projects to assist corporate development.

24 Post facto overseas investment Package 1 & 2, JICA, October 2010

Table 11 Example of overseas investment and financing in investment funds prior to resumption (overview)

Project name	SME rehabilitation & growth fund in Thailand	Regional company growth fund
Partner country	Thailand	India
Objective	(1) investment, (2) growth and rehabilitation of SMEs and medium-sized companies through advisory services	Investment in SMEs and medium-sized companies through state funds set up in 10 regional states, trigger growth of SMEs and medium-sized companies, create employment, and expand exchanges between Japanese and Indian private-sector companies
Investment	SME rehabilitation and growth fund (investors: JICA, ADB, KfW, and overseas private-sector companies)	Regional company growth fund (investors: JICA, IFC, ADB, 6 Indian companies, and 1 Singaporean company)
Fund size (Total/initial investment)	Total USD 100 million/initial USD 50 million	1,100 million rupee
Fund manager	(1) fund management company (investors: ADB, overseas company A) (2) investment advisor (investors: management, overseas company A)	Local fund management
Capital	USD 3.3 million	-
Investment approval date/initial investment date	March 2001/July 2001	October 1994/April 1996
Approved investment amount/ratio	3,300 million yen (equivalent USD 25 million)/ 25.0% of the total investment	250 million rupee (equivalent to 1,000 million yen)/25.0% of the total investment
Investment years	2001-2004	1996-2001
Implemented investment	391 million yen (equivalent to USD 3 million)	250 million rupees (773 million yen)
No. of investments/amount	2 investments/USD 8.5 million	36 companies & 37 investments/1,800 million rupees (including reinvestment)
Tie-up with JICA and other organizations	N/A	N/A
Fund investment track record	Of the 2 companies receiving investment, one is a subsidiary of a Japanese company and is operating smoothly. The other company has experienced a sharp decline in enterprise value due to a business slump; the fund waived its investment and the fund is insolvent.	Of the 36 companies invested in, 16 are publicly listed and there are no bankruptcies
Profit margin/JICA ROI	- USD 3.3 million/74%	Internal Rate of Return marginally negative/ROI is slightly under 100% (*prior to termination of fund)

The 2 aforementioned investments in private-sector funds are lessons that confirm the abilities of fund managers, reasonable fund management costs, and exit strategy from the fund[25]. We believe these are crucial points that warrant attention when investing in the GEDF. That said, the 2 investment examples mentioned above were joint investment projects with the international organization. In contrast, investment in the fund set up by Japanese private-sector companies would make it possible for JICA to accurately monitor its investment through close ties with the fund management company.

We note that in the event that there were previous projects, implemented soon after resumption of overseas investment and financing, trends should be closely monitored.

iii) Plan (draft)

- Investment amount and timing

  JICA's investment limit is 25%.In the event of an additional subscription, the investment management company will consider making a request to JICA for additional capital after discussions between JICA and the investment management company.

- Monitoring and recovery

  From the standpoint of handling projects with a high development benefit, which existing financial institutions have difficulty in addressing, we believe it is difficult to anticipate a high level of profitability from overseas investments and financing. Given that the fund is mainly set up by private-sector Japanese companies, including investment from JICA, it will be managed and operated with the purpose of securing a certain degree of profitability. We believe it is essential that management and operation of the fund can be monitored, and that we make sufficient efforts so that investors in the fund are able to obtain a reasonable profit.

25 In addition, the selection criteria for sub-projects at the time of the investment in the private-sector fund and confirmation of fund buildup were also pointed out. This was noted for the project in India (regional company development fund), which is structured so that the main fund invests in sub-funds set up in the 10 regional states. We believe this has no direct impact on the fund we are setting up.

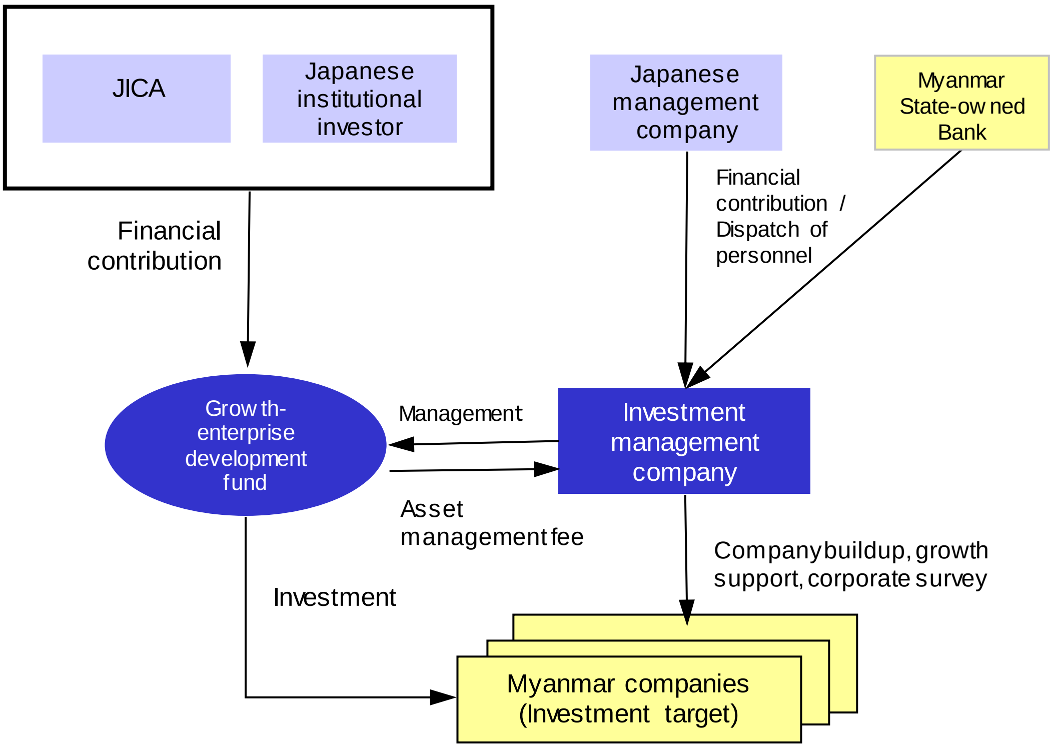

Chart 6 Tie-up between GEDF and JICA overseas investment and financing (image)

(b) Yen loans

Yen loan operations are for developing nations with inadequate economic and social infrastructures, including electric power and gas, transport, and communications systems. The loans are extended at low interest rates, for a long period, and under relaxed terms, for use as development capital to support development in emerging nations. In particular, development finance loans (two-step loans), which are project loans taking the form of yen loans, are based on the policy-oriented financial system of the borrowing nation, and funds are provided through a financial institution of the partner country, such as a development bank, to supply the necessary capital for implementing certain policies to promote specific sectors, such as small and medium-sized manufacturers and farmers, and to build a local infrastructure for the poor. This mechanism also promises to trigger benefits by supplying funds to a considerable number of end-beneficiaries in the private sector and it supports the strengthening of operational capabilities at local financial institutions that provide funds, while aiding development of the financial sector.

In Myanmar, in addition to underdeveloped direct financing functions (capital markets), indirect financing functions, such as bank financing, are still not sufficiently developed. At present, there are 4 state-owned banks and 19 private banks in Myanmar under the control of the Central Bank. The majority of the financial operations conducted by these banks are in principle loans collateralized by land. When companies seek to procure funds, in many cases the loans are extended in the private name of the president of the company. We believe that banks have not amassed sufficient expertise, such as on loan screening and credit management. Aid to growth companies via the fund is implemented as one step in the creation of a capital market. From the standpoint of developing financial and capital markets that are indispensable for the transition to a market economy, it is essential that measures be simultaneously carried out to strengthen indirect financing functions. In light of this, we believe it would be effective to use two-step loans to establish a mechanism for supplying capital to the private sector through Myanmar's domestic financial institutions. At the Japan-Myanmar Summit on November 19, 2012, Prime Minister Noda (at that time) announced Japan would consider support in the form of new yen loans, around 50 billion yen, in the 3 areas of emergency repairs for thermal power generators, regional development/poverty reduction, and development in Thilawa. In addition, by implementing management reforms at companies with growth potential, increasing competitive strength, and supplying indispensable capital, mainly for capital expenditures, it is possible to tie this into the development of a diverse range of companies that are potential candidates to become players in the market economy. Moreover, at the same time, by leveraging two-step loans, it is possible to enhance operating capabilities at financial institutions that conduct financing and support development of the financial sector. Due to this, we can expect a strengthening of operating capabilities and development of human resources through the provision of two-step loans at Myanmar banks, which are still developing their financing functions, such as insufficient expertise on loan screening and credit management, as discussed earlier. In Myanmar, financing provided to private individuals using real estate as collateral is a common practice at present. We believe it would be prudent to implement financing for companies based on assets and profit margins. We look to the incorporation of support measures to achieve this goal.

i) Working alongside the GEDF

The use of two-step loans in Myanmar is expected to bring greater benefits when working with the fund. This fund is considering establishment of an investment management company through a joint venture with Myanmar state-owned bank. Myanmar state-owned bank is to be positioned as one of the main financial institutions participating in the two-step loan program. This will make it possible to lend capital to the investment-target companies in this fund. Accordingly, in addition to receiving financing, the fund's investment-target companies are provided with a choice for financing capital procurement—borrowing through the bank. The benefit is that the fund does not have an excessive impact on rights facilitating stable management. For the fund, availability of other funding sources protects it from having to raise its investment ratio excessively and makes it possible to supply additional capital. We note that in the event that the fund's investment target companies receive the aforementioned loans, it will be vital from the standpoint of investors to verify if the debt-equity ratio is appropriate or not.

ii) Implementation structure

The outcome of due diligence, the process by which the fund selects a portfolio company, will be a valid factor in loan screening for investment target companies in the fund. In light of this, the investment management company provides Myanmar state-owned bank with the necessary information to facilitate a smooth screening process[26]. Regarding the investment management company's provision of investment target company's information to Myanmar state-owned bank, the consent of the company seeking the loan will be obtained in advance in an appropriate manner.

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26 The disclosure of due diligence information will boost the efficiency of screening, but it is essential that strengthening the domestic bank's operating capabilities be carried out systematically. As a measure to achieve this, we examine the use of JICA technical cooperation in the following pages.

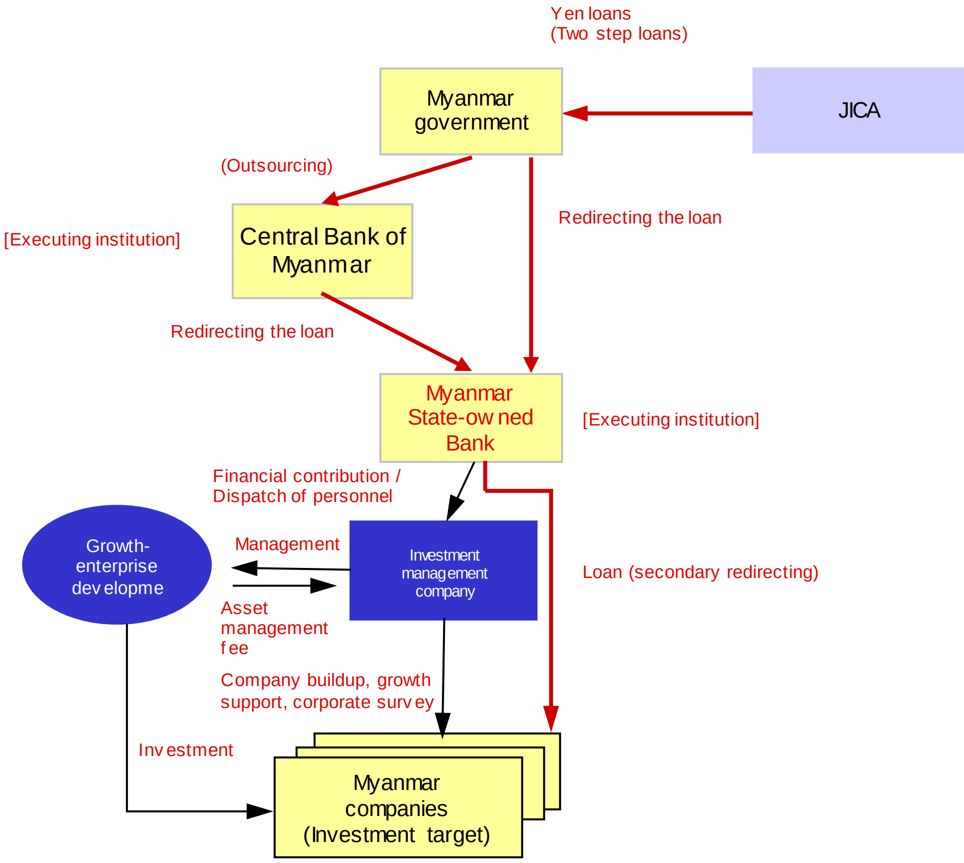

Chart 7 Tie-up between GEDF and two-step loan program (image)

- Currency, interest, and financing period

We believe the loans JICA grants to the government of Myanmar are in principle denominated in yen.

Referencing yen loans granted thus far, in most cases, the lending rate for financial institutions that participated in two-step loans was based on central bank interest rates, government bond interest rates, and LIBOR. Financial institutions that actually carried out financing, set a spread that took into account a margin on the interest rate of the redirected loan or credit risk.

The period for which the loan is extended to a company is set to provide a long-term and stable supply of capital. Also, it is necessary that the loan period be set longer than one year, at minimum, because the majority of bank financing in Myanmar is for periods of less than one year. It is advisable that, for the purposes of fund procurement for capital expenditures, the loan period be flexible, such from five to ten years.

- Implementation schedule

At this stage, the GEDF is scheduled to be set up in summer 2013 or thereabouts. Fund investment is slated to be executed over a three-year period from the time of establishment. Given that investment is to be implemented after the fund is set up, it is advisable that the necessary procedures, including the signing of an agreement, be carried out at the earliest possible opportunity (within 6 months after the fund's establishment) to secure a credit line.

iii) Other items requiring examination

As with the overseas investment and financing discussed earlier, we believe it is crucial to confirm that the implementation of two-step loans is in accordance with the "Japan Bank for International Cooperation Guidelines for Confirmation of Environmental and Social Considerations" (established on April 1, 2002).

Moreover, by investing in the GEDF and providing two-step loans, albeit indirectly, JICA becomes both a shareholder and a creditor of the same company. This results in a conflict of interest between shareholders and creditors. This point came under scrutiny during the review of overseas investment and financing, but no concrete improvements were sought because no problems in particular had arisen thus far[27]. Furthermore, when taking into account the original objective of JICA's aid, we believe the risk of a problem arising from a conflict of interests is minimal. However, from the perspective of securing the transparency and accountability of the financial aid extended, we believe it is advisable to develop a system whereby conflicts of interest will not occur and that documentation to this effect is prepared.

[27] Overseas investment and financing packages 1 & 2, JICA October 2010

(2) Technical cooperation

In general, the investment management company provides assistance to portfolio companies in the form of advice in areas such as business plan, operational improvement plans, management hiring, group reorganization, and procurement of capital, and also helps to find potential business partners. We anticipate, as a part of the GEDF, the investment management company will offer advice or guidance upon monitoring the Myanmar companies in the portfolio. However, in Myanmar, which is still developing its market economy, we think there is a possibility that the management company's assistance alone will be insufficient to improve management of the invested Myanmar companies. For example, during due diligence of a potential portfolio candidate, it is possible that a number of problems could be discovered. In principle, the company is supposed to plan to solve these problems independently after it receives the investment. However, in the case of Myanmar, companies operating in the current domestic market economy considerably lack the knowledge and skills required. In light of this, it is necessary to prove basic training and also guidance and assistance from specialists. Accordingly, in addition to the aid provided by the investment management company, we are examining use of JICA's technical cooperation to provide guidance on improving management with the aim of nurturing the portfolio companies, and also to develop human resources that are capable of providing guidance on business improvements[28]. Because it is not possible to determine in advance in which companies the GEDF will invest, it is difficult to specify beforehand which of JICA's diverse schemes, including dispatch of specialists, trainee program, and provision of equipment and materials, will be necessary. Consequently, we will review the use of a technical cooperation project that combines a number of schemes into an optimal arrangement.

Japan's economic cooperation with Myanmar was basically suspended from 2003. The provision of technical cooperation has been limited to human rights areas (including health care, medicine, education, agriculture, and drug prevention). However, due to the establishment of a new government administration and reforms in recent years in Myanmar, Japan has been examining the expansion of aid. At the November 19, 2012 Japan-Myanmar Summit, development of industry, human resources, and legal system were brought up as key areas for aid. In other words, implementation of technical cooperation, in line with our GEDF, falls in line with the policies of the Japanese government.

To achieve effective teamwork among the activities of JICA's technical cooperation and those of our GEDF, based on information obtained through our recent survey, we first plan to draw up a menu (tentatively called the management improvement menu) that covers crucial items for supporting portfolio companies. The overall menu is divided into those categories that should be handled by the investment management company and those items that should be improved through guidance from external technical experts. We will plan specific details such as dispatching specialists or a trainee program in accordance with the latter.

With regard to items requiring external technical guidance, we plan to use the support center, which is discussed later, and the Japan Center, which is scheduled to be set up by JICA for supporting the creation of a market economy system.

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[28] Using two-step loans, which we discussed earlier, Myanmar's domestic banks will extend loans to domestic companies. Currently, domestic banks lack the necessary expertise to conduct screening. Accordingly, we believe it is difficult to provide financing based on an assessment of the validity of business conditions and business plans of a borrower. Even when granting two-step loans, in the same manner, we consider it would be effective to leverage technical cooperation to strengthen operating capabilities at domestic banks.

i) Plan (draft)

- Goal and scope of technical cooperation project

  The goals are: (1) to provide various guidance to portfolio companies in the GEDF to carry out management improvements necessary for listing on the stock exchange, and (2) to provide training for human resources at Myanmar state-owned bank so that they can provide business consulting and guidance for business improvements.

- Implementation structure

  At the request of the Myanmar government, JICA will plan and carry out a technical cooperation project to provide assistance to portfolio companies in the fund.

  When implementing this technical cooperation project, as it is necessary to have a counterpart institution from Myanmar. state-owned bank will set up a growth company support center (hereinafter referred to as the support center) within the bank and the investment management company will work in conjunction with the support center.

  The support center will devise and carry out a detailed program based on the management improvement menu (working name) provided by the investment management company. JICA will dispatch people to the support center to provide technical guidance and to train local staff to provide guidance.

  The parts of the management improvement menu (working name) that are predominantly classroom teaching in areas such as business plans, governance, and accounting are topics that are likely to be of general applicability, so instead of separately teaching each company targeted for investment, learning together with other business leaders would be feasible. Conducting this sort of program in collaboration with or together with the Japan Center's teaching programs, would make it possible to put together a very comprehensive program. For this reason, we aim to have the investment management company work with the Japan Center to plan, propose, and implement business training programs.

  As part of the management improvement menu (working name), we plan to have the investment management company work with the Japan Center to plan, propose, and implement business training programs.

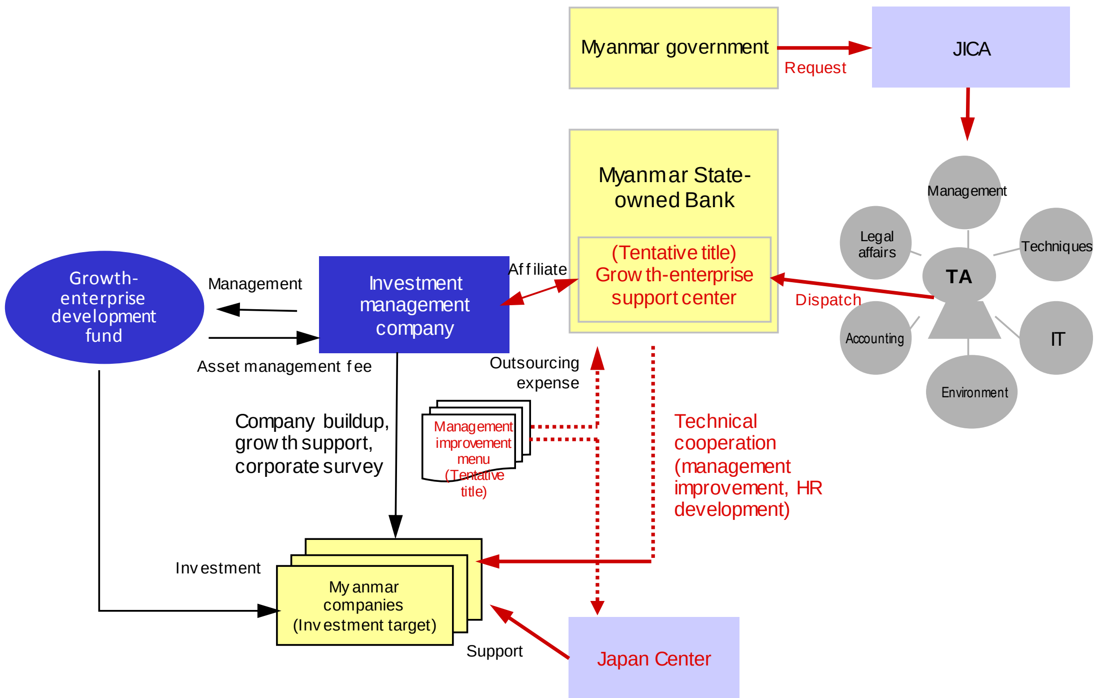

Chart 8　Tie-up between GEDF and JICA technical cooperation (image)

- Details of implementation

  The technical cooperation project will consist of technical guidance provided to the assistance center staff.

  Specifically, specialists and experts mainly in the fields of management, law, accounting, technology, environment, and information technology will offer guidance and training to assistance center staff and enhance staff capabilities by visiting individual companies, making analyses, drawing up reform proposals, and providing guidance on improving management.

  Also, should it be necessary, employees will be selected at the working level or middle management of Myanmar state-owned bank with the goal of improving their skills in fields necessary for corporate management, such as management, law, and accounting, with training offered by experts dispatched from Japan, training in Japan when needed, and participation in courses at the Japan Center. At Myanmar state-owned bank, management assessments will be implemented in areas closely related to loan operations, and from the perspective of nurturing human resources who will be able to provide advice on improving management, it is necessary to have a program that, in addition to content for companies, also allows participants to gain higher levels of skills.