

## Chapter 11

### **CHALLENGES, PROSPECTS AND STRATEGIES FOR CLMV DEVELOPMENT: THE CASE OF LAO PDR**

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#### **ABSTRACT**

Within the context of regional economic integration, Lao PDR is facing numerous challenges for being one of the least developed countries (LDC) in the world. Hence, the Lao Government has called for a long-term socioeconomic development strategy with the goal of graduating from the LDC status by year 2020. To achieve this goal, the Lao Government has made great efforts to build a relatively comprehensive development strategy framework, which includes the Industrialization and Modernization Strategy, the Six National Development Plan(2006-2010), the National Growth and Poverty Eradication Strategy(NGPES), and the sectoral long-term development strategy. However, to implement the Government's development strategy framework more successfully and narrow the gap of the country's development in the region, some policy recommendations from a research perspective should be taken into account, namely: 1) Infrastructure development by focusing on land-linked country and economic corridors; 2) Strengthening private sector development by promoting SME development and market development (financial market development, labour market development, real estate market development); 3) Tourism development by promoting cultural, eco-based, and historical tourism in the country as a sustainable tourist-friendly destination; 4) Keeping a natural resource-based industry that is both environmental friendly and economically efficient; 5) Developing the processing industry in the country for export and domestic consumption; and 6) Human resource development with focus on vocational schools and training for skilled labour.

## **1. INTRODUCTION**

This paper, which is under the ERIA research project on CLMV, discusses the Lao Government's development strategy and the author's recommendations from a research point of view. The paper is broken down into four main parts. Part I provides an assessment of recent development performance. It gives an overview of the Lao economy, overall achievements at the macroeconomic and sectoral levels, and some lessons learned. Part II identifies some of the main challenges and constraints to economic development. Part III focuses on the development strategy perspective for the Lao PDR. It examines the potentials and opportunities for development and reviews the Government's development strategy framework. Part IV gives some policy recommendations for promoting sustainable growth in the Lao PDR.

## **2. RECENT DEVELOPMENT PERFORMANCE**

### **2.1 Context**

From mid-1997 to the end of 1999, the economy of the Lao PDR faced arduous difficulties, especially the significant negative impacts of the Asian economic crisis and recurring severe natural disasters. However, since 2001, the Lao economy has recovered and developed under more favourable conditions. The economy has begun to resume expansion and build up the potential for growing at a faster pace in the following years. Production forces and socioeconomic elements have built the necessary initial base for future growth. The legal frameworks were gradually adjusted and their positive impacts on socioeconomic development have since increased. The market-oriented economy emerged further and operated in a more efficient manner. Political and social stability

were enhanced. Relations with countries in the region and outside on economic and other fronts were expanded, with significant strengthening of the capacity and standing of the Lao PDR in the region and the global community. The developments outside the country also significantly provided favourable conditions. Stability and economic recovery in the Asian region and at the global level, scientific and technological innovations, and globalization brought about many opportunities to overcome the difficulties and obstacles.

Meanwhile, the global situation developed in a complex manner after the 11th September 2001 event in the United States and the Afghanistan and Iraq wars that followed. Terrorism and antiterrorism became dominant issues, but peace and development cooperation remained major priorities at the international level. The global and regional economies have been recovering, with firm continuation of globalization and increasing competition. Within Southeast Asia, SARS, Avian Flu, and floods and droughts have occurred. These developments have imposed severe difficulties on the Lao social and economic bases.

## **2.2 Economic Growth**

During the five-year period (2001-2005), the Lao economy has maintained rapid and sustainable growth. On average, the GDP grew at about 6.24 percent per annum, which is about 0.3 percentage point higher than the average growth rate in the previous five-year period (1996-2000). The growth rate failed to reach the target set in the Government's Plan and the full potential of the economy was not utilized. However, it is heartening to note that the growth rate achieved is higher than that recorded in the previous Plan period (1996-2000). It is also useful to highlight the relative growth rates

of the domestic private sector output, output from foreign direct investment (FDI) enterprises, and State output. The average economic growth rate in the Lao PDR during the past five years is among the highest in the region (e.g., Cambodia, 5.5%; Indonesia, 4.2%; Malaysia, 4.3%; Philippines, 4.2%; Singapore, 3.7%; Thailand, 4%; Hong Kong, 2.8%; South Korea, 4.7%; Taiwan, 4.2%; Viet Nam, 7.5%). By 2005, the GDP per capita reached US\$491.

### **2.3 Sectoral Performance**

All the economic sectors experienced growth, which has been linked to structural changes and the enhancement of product quality. The sectoral performance is presented in the following:

#### *2.3.1 Agriculture Sector*

During the past five years, the Government, line ministries, and sectoral and local authorities of the Lao PDR have concentrated on the development of agricultural production, following the direction set, i.e., orienting the agriculture sector from subsistence and semisubsistence to commercial production to ensure the enhanced supply of raw materials to processing industries, meeting the growing domestic requirements for agricultural products, and rapidly expanding agricultural exports. The composition of production and products has been restructured positively with increasing economic effectiveness. This therefore allowed a stable growth in agriculture, forestry, and fisheries production, albeit under constrained development conditions. Over the last five years, the value of production in the agriculture sector has increased on average by 3.4 percent per year.

By 2005, the production of many crops increased significantly compared to the last year of the fourth five-year Plan (2000). For example, maize (corn) production tripled to 372,560 mt as compared to that in 2000. Maize is grown largely in the northern provinces, such as Bokeo, Sayaboury, Houaphanh, and Xiengkhouang, and in some central provinces. The production of coffee, which is concentrated in the provinces of Champasack, Saravane, and Sekong, increased by six percent reaching 25,000 tons. Peanut production, largely found in the provinces of Sayaboury, Luang Prabang, Vientiane, Saravane, and Champasack, doubled to 26,990 tons. Soybean production, which is concentrated in the provinces of Luang Prabang, Bokeo, Houaphanh, and Champasak, also experienced a two-fold increase to 11,100 tons. Sesame plantation yielded 8,710 tons, up by 2.6 times, and was largely found in the provinces of Luang Prabang, Sayaboury, Oudomsay, and Vientiane. Mungbean production was up by three times to 3,700 tons, and was concentrated in the provinces of Luang Prabang, Vientiane, and Champasak. Tobacco planted in the provinces of Borikhamsay, Khammouane, and Savannakhet provided a total harvest of 28,100 tons. Sugarcane, which is concentrated in Vientiane Capital and in the provinces of Luang Namtha, Phongsaly, and Borikhamsay, had a harvest of 196,100 tons. Vegetable production increased by 17 percent to 744,450 tons. Most noticeable are the plantations of vegetables, such as cabbage, Chinese cabbage, bananas, potatoes, and ginger, on the Boloven Plateau for export. Having won popularity, rubber trees are extensively planted in the provinces of Luang Namtha, Oudomsay, Bokeo, Khammouane, Champasak, Saravane, Sekong, and Attapeu. Orchards are being grown in a number of provinces, particularly orange plantations in Luang Prabang, Sayaboury, Borikhamsay, Vientiane, and Vientiane Capital.

The move to commercial production is growing strongly in the high-potential areas. Prominent among these are the emphasis on the cultivation of rubber in Luang Namtha; cashew nuts in Oudomxay and Phongsaly; corn, vegetables, and fruit trees in Vientiane Province and Vientiane Capital; seeded trees for oil extraction and sugarcane in Savannakhet; and rice in Vientiane Province.

Emphasis is placed on research and the adoption of high-yield/high-productivity crops and livestock. Currently, several new varieties have been introduced, such as rice, maize, vegetables, beans, coffee, tobacco, tea, and fruit trees, as well as a number of domestic animals. By 2005, the farming sector ensured 80 percent of the seed requirements for the rainy season crop and 100 percent for the dry season crop. Many modern cultivation and animal raising techniques have been introduced.

The number of irrigation schemes has continued to increase from 19,170 in 2000 to 24,695 by the end of 2004. Irrigated crop areas during the dry season increased from 197,100 ha in 2000 to 215,000 ha in 2004, while the irrigated area during the rainy season increased from 296,000 ha to 315,000 ha. Due to the increase in irrigation and the introduction of new crop varieties, rice yield increased from less than 3.06 mt per hectare in 2000 to 3.6 mt per hectare in 2005. Rice production reached 2.65 million mt in 2005, which translates to an average per capita availability of approximately 457 kg per capita.

The livestock and fisheries sectors are developing quite rapidly mainly due to the industrial farming systems applied in many localities and because of increased market opportunities and reductions in marketing costs. In 2005, the livestock numbers rose to 1.09 million buffalos (6% increase over 2000), 1.27 million cows (15.6% increase),

1.82 million pigs (28% increase), 19.8 million poultry (51% increase), and 190,000 goats and sheep (56% increase).

Thanks to such rapid development, meat production in 2005 was projected to reach 96,000 mt (an increase of 17.5% over 2000). It is notable that about 10.2 percent of the meat production is provided by industrial farms with high technology, which grew at the rate of 9.8 percent in the 2003-2004 period. At the end of 2005, about 10 percent of the cattle and 20 percent of the poultry were raised in the commercial farms. More specifically, the farms have focused on raising new high-quality cattle and poultry species, with high productivity in the production of swine, chicken, and ducks.

Also, fish production rose to 143,000 mt (an increase of 15%), with fish farms accounting for 68.5 percent of the total and capture fisheries accounting for the rest (31.5%). Fish fingerling production rose to 320 million, which was adequate to meet about 50 percent of the national demand. Fish farms have achieved high productivity in the production of fish raised in baskets. In 2005, both meat and fish production met a large part of the population's consumption demands.

Forest conservation and development are given increased attention by line ministries and local authorities compared to the previous plans. The forestation movement by the people has regained momentum, especially in the central provinces, such as Vientiane, Borikhamxay, Khammuane, and Savannakhet,

More specifically, many areas have combined forestation with the development of high-commercial-value industrial trees, such as teak in the provinces of Luang Prabang, Sayaboury, Vientiane, Bokeo, Champasak, Bolikhamxay, and Attapeu, and rubber in the provinces of Luang Namtha, Khammouane, Champasack, Saravane, Sekong, Attapeu, Bokeo, and Oudomxay.

Between 2001 and 2005, about 325 tree nurseries were set up for the germination of tree saplings for afforestation and forest restoration. About 240,000 kg of tree seeds were used for the production of some 119 million tree saplings. During 2001-2005, afforestation covered 91,000 ha, accounting for 91 percent of the target (100,000 ha) while efforts were made on forest restoration on 481,000 ha.

According to data on forest exploration in 2002, the area of dense forest, which included forests of high and medium density with a canopy of over 20 percent, accounted for 41.5 percent (9,724,700 ha) of the country's total land surface. If the brushwood, bamboo forests, degraded forests, and mixed deciduous forests with a canopy of less than 20 percent were combined with the dense forests, the forestry coverage accounted for 72 percent (17 million ha) of the country's land surface.

The exploitation of perennial trees has reduced significantly in the last five years. In 2001, about 300,000 cubic meters of natural trees were exploited, which declined to 150,000 cubic meters in 2005. Wood exploitation is currently subject to more careful consideration (e.g., combining exploitation with the plantation of alternative trees).

In the past five years, over 1.09 million ha of arable land and 3.6 million ha of forestry land were allocated to 7,125 villages composed of 419,250 households, to reduce the practice of shifting cultivation while ensuring sedentary highland and lowland cultivation to reduce poverty among the ethnic people. As a result, the area under shifting cultivation declined from 118,900 ha in 2001 to 29,400 ha in 2005, mainly in the northern provinces (26,800 ha), with the remainder in the central region (2,600 ha). Shifting cultivation has ceased completely in the southern provinces. The number of farm families practicing shifting cultivation has reduced from 174,036 in 2000 to 32,790 in 2005.

The development of agricultural and rural economies has begun to diversify. A large number of farms have been established and the production of traditional handicrafts has been resumed. The development of traditional handicrafts has generated additional jobs for the local people and contributed to the changes in the rural economic structure as well as the improvement of the population's living conditions. The government has removed barriers to private sector investment and trade in the agricultural sector. At the same time, it has increased the population's purchasing power and contributed to the eradication of poverty in rural areas.

### *2.3.2 Industry and Construction Sector*

Industrial production has grown at a steady and rapid rate, with the sector-wide average growth reaching 11.3 percent per year, exceeding the Plan target of 10-11 percent. The mining industry increased by 33.87 percent; food processing, 9.17 percent; tobacco, 20.75 percent; textiles, 20.11 percent; garments, 11.15 percent; footwear, 7.57 percent; and wood processing, 1.17 percent. The sectors receiving foreign investment have achieved an impressively rapid growth, followed by the nonstate sector, with the domestic private sector growing slowly. In the past five years, the industrial sector has implemented several significant activities, such as the exploitation of gold and copper at Sepon; zinc in Vientiane Province; construction of a cement plant in Vangvieng and a steel factory in Vientiane; setting up of a number of motorcycle assembly plants; completion of the Nam Leuk and Nam Mang III hydropower plant and a number of other hydropower projects; expansion of the installed capacity of the Nam Ngum 1 from 150 MW to 155 MW; completion of a number of high-voltage transmission lines; and pilot installation of solar energy production systems. The total installed capacity of power plants by 2005 reached approximately 690 MW. The construction of some other

major power plants/projects, as part of the five-year Plan has commenced, including the Nam Theun 2 Hydropower Project. Trade liberalisation, improvements in the enabling environment for business, and reduced logistics and transport costs contributed to increasing incentives for investment in industrial production.

Most of the industrial products have achieved higher growth rates compared to 2000, including coal, salt, beer, soft drinks, tobacco, animal feed, soap, leather shoes, pharmaceutical drugs, plastic products, furniture, ready-made clothing, bricks, cement, manual agricultural instruments, and agricultural machinery. In particular, the operation of the Sepon gold mine in Vilabouly District, Savannakhet Province, started in 2003 with a production of approximately six mt each in 2003 and 2004, with a projected increase to 6.5 mt in 2005. The mining industry has developed rapidly, as illustrated by the investments by 90 companies in mining at the end of 2005, of which 34 are foreign and 56 are domestic. The number of handicraft businesses in the country also increased rapidly in the last five years, especially in Vientiane City and in a number of major urban centres. By 2005, there were 26,200 industrial-handicraft units (rising from 23,574 units in 2001).

Currently, a number of industrial zones have been established in such places as Vientiane and Savannakhet. They include many standard to modern technology zones, attracting investment from many enterprises. The development of such industrial zones has helped to attract more foreign investment. Industrial development in certain areas and focal economic zones was firmly maintained. Areas with a high proportion of industries, such as Vientiane City and the provinces of Champasak, Khammouane, Bolikhamxay, Luang Namtha, Xayaboury, and Savannakhet, maintained high growth rates.

The participation of different economic sectors (such as domestic and foreign private investors and the State) in the manufacturing industries has facilitated its diversification in terms of manufacturing scale, level of technology, types and quality of products. The industries are thus able to meet the various demands of the market. The industrial sectors were responsible for creating the most jobs.

### *2.3.3 Services Sector*

The services sector has taken positive steps forward to better meet the requirements of production, trading, and daily life. The availability and quality of products and services are higher compared to the beginning of the period. Over the five-year period (2001-2005), the growth in total retail sales and revenues from services averaged at 10 percent per year. The value added in the services sector grew at an average of 6.7 percent per year over the five years, which exceeded the GDP growth rate, although the growth rate was still less than the Plan target of 8-9 percent per year.

A number of services have developed quite effectively, such as trade, transport, telecommunications, tourism, hotels, and restaurants. More specifically, several services sectors essential for the development of new economic bases such as finance, banking, and insurance have experienced strong growth. An increasing and more diversified number of enterprises are entering the trade and services markets. In 2003, about 61,200 enterprises were registered. Trade infrastructure has been improved. By the end of 2003, there were 209 large markets, including 11 markets at international border cross-points and 28 markets at local border cross-points.

The service subsectors are currently being restructured and moved toward the market mechanism under state guidance. The legal framework has clearly defined the

direction for market operations. The Business Law, the Investment Law, decrees relating to business operations within the country, and export and price regulations have been put in place with increasing efficiency. The central Government is currently continuing the process of decentralization in order to enhance local ownership of the regulation of commerce, mainly in such areas as investment licensing, business licensing, issuing certificates of origin, and export permits.

The tourism sector has also developed rapidly compared to the 1990s, despite the unfavourable international context during the first three years including the Iraq War and the outbreak of SARS. Since 2004, with more favourable domestic and international conditions, tourism has regained momentum and resumed strong development. Tourism infrastructure was quite efficiently improved, with the number of hotels and guesthouses increasing from 468 in 2000 to 887 in 2003 and about 1,200 in 2005. The number of hotel rooms increased from 7,333 in 2000 to 20,000 in 2005. A number of new tours, including tours among countries in the Mekong Basin, have been designed and introduced, and are attracting a substantial number of international tourists. The different types of tourism are growing in a diversified manner, offering more attractive tourism products. By mid-2005, the country had 364 tourism sites to attract domestic and foreign tourists.

In the five-year period (2001-2005), about four million foreign tourists visited the Lao PDR, averaging at about 800,000 tourists per year, with 900,000 in 2004 and about 1.05 million in 2005. Overall, the total number of foreign tourists to the Lao PDR over the five-year period (2001-2005) increased annually by nine percent. The sector revenues reached over US\$100 million per year. The number of tourists from wealthy regions and countries, such as the United States, Canada, Belgium, Germany, Holland,

Norway, the United Kingdom, France, Japan, Sweden, and Switzerland, is increasing. Specifically, the proportion of tourists from the European countries increased from 11.7 percent in 2000 to 14.8 percent in 2003 and about 16.5 percent in 2005.

The strong growth experienced by the tourism sector in recent years was supported by the Government's increasingly open tourism policy, which upholds tourism as one of the eight focal economic sectors to be developed in the Five-Year Plan. The Lao PDR has established tourism relationships with many countries around the world with a focus on ASEAN members and countries in the Mekong Sub-Region. By the end of 2005, entry visa requirements were lifted for tourists from several countries in the region. Thirteen land border crossing-points were upgraded into international border crossing-points to welcome tourists, and facilities were provided for the issuance of visas on arrival. Also, participation in different events was ensured to attract tourism from different markets and a number of events relating to domestic and international tourism were organized in the Lao PDR. The country hosted an ASEAN Tourism Forum in 2004 (ATF 2004) in Vientiane Capital, which marked a cornerstone in the opening of a new era in tourism in the Lao PDR. In 2006, Luang Prabang was awarded a gold medal for being voted as the most popular town in tourism in a survey answered by over 100 travel companies in the UK.

The transport and freight services have shown quite positive and uniform development, with initial improvements in the quality of services, in spite of the severe impacts of the Iraq War and the SARS outbreak. The freight volume increased at an annual average rate of about 11 percent and circulation by 15 percent. The passenger volume increased by about seven percent per year and circulation by five percent per year. In particular, the volume of transborder shipping increased strongly at an average

of over 20 percent per year. The number of deaths due to road accidents was reduced significantly from 19 per 10,000 vehicles in 2001 to 10 in 2005.

During the last five years, the transportation sector emphasized the implementation of different projects, including the maintenance of existing roads and bridges and the transportation system as a whole. Simultaneously, the construction of regional roads, national roads, a railway system, airports, bridges, and a number of important local roads has continued. Significant achievements include the completion of the construction or paving of many roads to ensure smooth year-round transport. A number of important projects including new construction, improvement, and upgrading of over 1,130 km of roads and 39 bridges with a total length of 2,611 metres were completed. The number of transportation services by land and river has increased by about 10-12 percent per year. At the same time, many ports were built and upgraded, especially along the routes of the Mekong River. The airport system was also built and upgraded, including the improvement of the Wattay International Airport and the upgrading of the Luang Prabang and Pakse airports to international standards. About 14 kilometres of the railway along the Friendship Bridge to Kham savat village was surveyed and designed. Also, the survey and feasibility study of the railway project from Thakhek to Kiumuya was carried out.

The telecommunications services have continuously developed and reached both urban and rural centres, including in mountainous and remote areas, with the quality of services significantly improved. The number of telephone users has increased, with the landline and mobile telephone subscribers reaching 87,500 and 327,000, respectively, by the end of 2004/05. The number of public telephone booths increased to 404. In general, telephone subscribers of all types reached 415,900, with an average coverage of

7.3 lines per 100 people, which exceeded the Plan target of 2.5 lines per 100 people by 2005. There are 2,570 internet shops all over the country. By 2005, 80 percent of the districts and 60 percent of the communities will be contactable by telephone. There will be around 130 post offices in 104 districts and about 23,247 public post boxes. Postal and telecommunications services are being provided to accelerate modernisation. Freight, mail, and money order (transfer) services in the country and internationally have increased at a moderate level.

The finance, banking, insurance, and other services have also continued to be established and expanded. The insurance market has been established with the participation of both domestic and foreign actors.

## **2.4 Foreign Trade**

Foreign economic activities developed well. The Lao PDR has been more proactive in regional and global economic integration. The Lao Government needs to work with potential domestic and foreign investors to ensure that the country benefits from the liberalisation of trade in agriculture products under the ASEAN Free Trade Agreement and various bilateral agreements.

### *2.4.1 Exports*

The aggregate value of exports over the five-year period (2001-2005) is expected to reach US\$1.83 billion. Export growth rate averaged at about seven percent per year, exceeding that achieved in the previous five-year period (1996-2000) (average of 1.6 percent per year). However, the growth rate was lower than the Plan target of 8.6

percent per year. The average value of exports per capita was US\$86.7 in 2005; it remains far lower than that in other countries in the region.

Until now, a group of key export products have been developed, including electricity, coffee, wood, handicrafts, garments, and minerals, in addition to a number of new emerging products with potential such as tea, rubber, vegetables, fruits, oil plants, fragrant rice, corn, and many types of beans. The share of agriculture, forestry, and fishery products in export revenues shows a decreasing trend. In contrast, the proportion of light industry and small industry products in exports increased significantly with garments ranking at the top.

Conducive foreign policy has allowed the Lao PDR to gradually integrate into the regional and international economies and has helped to diversify its markets. From the period when traditional markets consisted of Thailand, Viet Nam, and China to the end of the Plan, exports are now destined to 40 markets, which include the larger markets such as the European Union, USA, Japan, Australia, the United Kingdom, France, and Germany. Border trade has also developed strongly. More prominently, during 2001-2005, many FDI enterprises have invested in export-oriented manufacturing activities.

In 2005, export revenues reached approximately US\$456 million (US\$ 500 million was planned for 2005) of which agriculture and forestry exports represented 10.2 percent, heavy industry (electricity, electronics, machinery, etc.) and minerals covered 42.8 percent, with light industry and handicraft products accounting for the rest (47 percent). The exports accounted for 1.5 percent of GDP.

#### *2.4.2 Imports*

The total value of imports over the past five years amounted to US\$2.86 billion with an average annual increase of 4.9 percent, exceeding that in 1996-2000. However,

it remains lower than the Plan target of 8.6 percent per year. The value of imports per capita in 2005 was about US\$122.30. The composition of imports has changed in accordance with the capacity and requirements of the economy. More importantly, the proportion of rice and food products in imports declined significantly from 32.6 percent in 2000 to 9.9 percent in 2002 and approximately 4 percent in 2003. By 2005, the value of imports is expected to reach approximately US\$595 million, with equipment, machinery, and parts making up 39.2 percent; raw materials and fuel at 47 percent; and consumption goods at 13.8 percent. By 2005, imports accounted for 1.9 percent of GDP.

## **2.5 Foreign Direct Investment**

From 2001 to 2005, the Lao PDR has received 585 FDI projects with a total committed capital of US\$2.8 billion. However, only US\$1.07 billion worth of funds were actually brought in (disbursed) during the period. The agriculture sector received 14 percent of the total number of projects accounting for seven percent of the total investment capital; the industry and construction sector received 48 percent of the projects and 79 percent of the investment capital; and the services sector received 38 percent of the projects and 14 percent of the investment capital. In particular, in fiscal year (FY) 2004/05, a total of US\$1.3 billion of FDI projects were approved, with US\$449 million brought into the country during the year. In the five-year period, FDI disbursements reached US\$933 million of which US\$326 million was received in 2005. Capital injected from abroad reached US\$855 million, accounting for 91.6 percent of the total. Disbursements in the industry and construction sectors account for 69 percent, in the services sector at 27 percent, and in the agriculture, forestry, and fisheries sectors at 4 percent. The

proportions of investment in the agriculture and services sectors show an increasing trend.

Overall, FDI has made a positive contribution to the manufacture of goods, economic growth, and the restructuring of the economy. It also helped to develop the private sector. These achievements were attributed to the incentives provided by the Government and other measures, such as the decentralization of foreign investment licensing. From 2005 onwards, provinces have been delegated by the authorities to license foreign investment projects valued up to US\$2 million. This has led to significant increases in FDI compared to the beginning of the Plan period. Annual forums with investors and businesses were organized to discuss constraints and explore solutions. At the same time, the infrastructure has been improved rapidly providing better facilities to attract FDI. In October 2004, the National Assembly revised the Law on Foreign Investment including the incentives, thereby paving the way for more FDI in 2005 and thereafter.

## **2.6 Labour and Employment**

During the past five years (2001-2005), a number of articles in the Labour Code have been amended and supplemented. A Government decree guiding the implementation of the revised Labour Code, the Civil Service Law, the Law on Minimum Wages, and the Law on the Establishment of the Social Welfare and Social Security Reserves was promulgated. A vocational training centre was set up in Vientiane. From 2001 to 2005, about 100,000 people have undergone vocational training, lagging behind the Plan target of 300,000.

A new policy on foreign workers in Laos has been drawn up, especially applicable to technical workers in industrial plantations such as rubber, coffee, and cashew, and in a number of industries such as electricity, coal, cement, and agro-processing. Thanks to the policy, thousands of foreign workers (from Viet Nam, China, and Thailand) poured into the country and facilitated technology transfer. At the same time, sister cities and provinces in Viet Nam and the Lao PDR have established business networks to exchange experiences.

A number of labour centres were set up providing opportunities for Lao labourers to go to Japan, Malaysia, and Singapore. A Government decree guiding the movement of Lao labourers overseas was promulgated. Two state-owned enterprises (SOEs) and some private enterprises were established for employment promotion. Additionally, an Agreement on Labour Cooperation was signed between the Lao PDR and Thailand.

One of the aims of the Government's policy is to encourage private enterprises to provide technical and vocational training. By the end of 2004/05, there are over 100 private training centres in operation in the country. In particular, they provide training for highly profitable and low investment professions, such as English language, computer applications, and accounting. The Government also promulgated a policy, which allows foreign workers to open a human resources training centre in the country.

## **2.7 Poverty Reduction**

Poverty reduction is the core task in the socioeconomic development guidelines of the Party and the Government of the Lao PDR. Promulgated were the Prime Minister's Decree No. 10 and other resolutions to implement poverty reduction efforts, which have progressed significantly during the past five years. These initiatives have been

implemented aggressively by CPI (Committee of Planning and Investment), public organizations, and the four priority sectors (agriculture and forestry, education, health and infrastructure) in the localities with the participation of poor people, especially in the 10 pilot districts selected from the 47 poorest districts. The latter (47 poorest districts) include 2,935 communities with a population of around 1.2 million people in 111,850 poor households, which account for 55.4 percent of the total poor households in the country.

In 2003/04, CPI issued regulations and mobilized village development funds (including from the budget) for poverty reduction. By 2005, there were 192 village development funds with 10,925 members. The Government injected an input of 18.3 billion kip into the funds. With a loan of US\$20 million from the World Bank, the Poverty Reduction Fund has implemented 1,212 projects, valued at US\$8 million in 1,913 villages in 20 districts in five provinces. There are also other poverty eradication projects, including the projects supported through foreign cooperation that made progress and are well organised.

So far, the land-forest allocation program has presented 1.09 million ha of agricultural land and 3.6 million ha of forested land to 419,259 households in 7,125 villages. Areas under slash-and-burn cultivation have been reduced from 118,900 ha in 2001 to 29,400 ha in 2005, fulfilling 75 percent of the Fifth Plan target. Of this, 72,870 ha have been put under industrial trees.

Shifting cultivation and opium production have reduced in a most noticeable way. Almost 19,000 ha of opium fields were destroyed and nearly 30,000 ha of slash-and-burn fields were converted into industrial tree plantation areas. By the end of 2004/05, 10 provinces—Oudomxay, Luang Namtha, Bokeo, Vientiane, Phongsaly, Huaphan,

Xiengkhuang, Xayaboury, and Bolikhamxay—and one special zone were officially declared to be free from opium production.

The Government has designed and implemented economic development projects (in different sectors, including agriculture and forestry, and industry and construction) and invested in the construction of infrastructure, such as roads, schools, and electricity grids, as well as in the social sectors, such as health, education and training, culture, and communications with the purpose of reducing poverty. The labour and social welfare line authorities actively built and developed forms of model families in the poverty reduction movement through reorientation from shifting cultivation and opium production to the production of industrial crops, livestock, handicrafts, trade, and services to gradually uplift the quality of life of the affected populations.

In 2000/01, about 38 percent of the population was below the national poverty line (or classified as poor). According to the reports from the provinces, there were 304,100 poor households<sup>1</sup> in 2002 and the Plan target was to move some 150,050 households out of poverty. From 2001 to 2005, some 137,500 families graduated from poverty, achieving about 90 percent of the Plan target. Model associations of villages and groups were formed and tested for the development of commercial production including the establishment of development funds promoting commercial production. Similar models

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<sup>1</sup> The definition of poor families is based on the standards specified in the Prime Minister's Instruction No. 10, which includes income and access criteria. However, the number of poor households in 2004/05 will be much larger if the national (income) poverty line from the Second or Third Lao Expenditure and Consumption Surveys (LECS II or III) is used.

were formed and tested for the elimination of shifting cultivation and the eradication of opium production. Local potentials have been tapped to generate incomes for the poor.

Savings groups were being organized and credit funds were established by mobilizing the participation of poor households to assist the households to develop their production and increase their incomes through low interest loans. These funds are closely managed and shared equitably as demonstrated by the Women's Union Group of Somsavi Village (Saithany District, Vientiane Capital).

### **3. CHALLENGES AND CONSTRAINTS**

Although the achievements attained in the five-year period (2001-2005) are highly positive and praiseworthy, a number of challenges and constraints still remain, which are enumerated briefly in the following:

#### **3.1 Economic Growth in Real Sectors**

The growth of the economy remains unstable, and has not generated adequate investments nor realised its full potential. Although there has been progress, the quality of growth and the efficiency and competitiveness of the economy remain low and slow.

##### *3.1.1 Agriculture Sector*

In the agriculture sector, small-scale and subsistence production is still widespread. The production in this sector has not achieved the planned target and its full potential. The introduction of modern cultivation systems remains slow. Agriculture production is still concentrated on rice. Animal husbandry needs to be further developed. Crop production,

animal husbandry, and the quality of agricultural products, albeit increasing, are still low and seasonal, dependent on the weather. The structural modification of agriculture production and the composition of the rural economy are still slow and do not yet guarantee stable components. Commercial production in several areas is not linked to processing industries and market demands. Overall food production is sufficient to meet the domestic demand, but about one-third of the districts do not yet have a sufficient production of rice to meet the consumption requirements for the whole year. The most important constraints to agriculture development are weak market institutions, formal and informal barriers to national and regional trade, high transport costs, and lack of supporting urban infrastructure and service.

The use of inputs in the agriculture sector remains inefficient, more particularly in the irrigation subsector. Although agricultural production has increased significantly, it has not met the economic requirements. Many goods could be produced locally and efficiently, but insufficient efforts for their development resulted in substantial imports of these goods. The sector-wide quality and efficiency needs to be improved further.

### *3.1.2 Industry and Construction Sector*

The production costs in the industrial sector remain quite high. Very few enterprises use modern technologies and most of these are foreign-owned. Public investment in the industrial sector remains low due to the excessive focus on the agriculture sector (particularly irrigation), infrastructure (mainly roads and ports), and services. There is a lack of incentives for different economic actors to invest in industrial development. Coordination between line agencies and local authorities to encourage industrial

development remains weak. The handicrafts sector is not sufficiently developing at the local level. Although advanced techniques are used, its development remains limited.

### *3.1.3 Services Sector*

The services sector infrastructure is still very limited and is not adequate to meet the socioeconomic development requirements. As a result, the quality of many types of services is still low. Management of services shows several shortcomings, including control on investors, personnel management, and the management of family and private enterprises engaged in the provision of services. The coordination between Government officers and sectors at the local level in planning the development of infrastructure, tourism, and others is still very weak, resulting in low efficiency.

### *3.1.4 Infrastructure Use*

The application/use of infrastructure in the activities of many sectors is still very low since production is not developed at the same pace as the development of physical infrastructure. Most prominent is the very limited capacity to make efficient use of irrigation schemes, ports, airports, etc. This results in waste and a reduction in the cost-effectiveness of investments.

## **3.2 Financial Sector**

### *3.2.1 Savings and Investment*

The ratios of savings and investment to GDP, although significantly improving, are still low compared to the potentials and the development requirements. The difference between domestic savings and public investment is significantly high and requires the

use of foreign funds, mostly in the form of loans. The mobilization of savings for investment is still limited since the Government has not yet secured the sources of adequate revenues and the enterprises in different economic sectors have not yet sufficiently developed. Also, there are still no policies and detailed mechanisms to convert land and other resources into sources of capital.

The mobilized funds for investments are limited and are not concentrated on strongly encouraging structural adjustments for the development of the potentials of different areas, developing the skills of the labour force, eradicating hunger (scarcity of rice), and reducing poverty. Investments in infrastructure are scattered and the implementation of projects is often delayed. Debts incurred for financing the construction of infrastructure are substantial, and the debt service obligations create pressure on the budget and prices.

### *3.2.2 Financial Sector*

The use of foreign currencies in transactions by enterprises and the general population is still widespread.

Interest rates on loans extended to economic entities remain substantially high although the rate of inflation has declined significantly, thereby adversely affecting economic growth.

The financial market is developing within a limited scope. Credit is limited and meets only 15 percent of the requirements. The loan amortization periods are short and there is pressure on the operations of enterprises and the capacity of the commercial banks to recover loans. The volume of repayments overdue in the banking system is substantial and is concentrated mainly in the domestic commercial banks, which suffer

from poor financial capacity and quality of transactions. High nonperforming loans (NPL) are a drag on credit flow and high interest rates remain.

### **3.3 Economic Fundamentals**

Until now, the economic base of the country remains to be relatively small. The total GDP in 2005 amounted to only US\$2.8 billion, with an average GDP per capita of US\$491. These indicators for the Lao PDR are among the lowest for the countries in the region, and it remains one of the poorest countries in the world. The economy's growth rate is yet to reach its full potential. With the low economic base, even if the rate of growth of the economy accelerates significantly, the absolute value added to the GDP would remain modest. The gap between the GDP per capita of the Lao PDR and that of other countries in the region continues to widen.

### **3.4. Structural Adjustment of the Economy**

#### *3.4.1 Structure of the Economy*

The adjustments in the structure of the economy largely focus on the sectoral composition of GDP, concentrating on the rate of industrialization. They do not take into account adequately the goals in structural adjustment in line with the direction of industrialization and modernization, with strong technological and technical developments. Therefore, the development of domestic industries is characterised by obsolete technologies, high costs, and low efficiencies. This requires high protection/subsidies, thus reducing the competitiveness of the economic sectors in the long run in the process of international integration. Structural adjustments in the agriculture sector have only recently been initiated with the conversion of low-

productivity (and low-value) rice cultivation lands into industrial plantations. The economic components of the agriculture sector are not strongly linked to the processing industries and markets. The economic structure in rural areas is mainly and solely reliant on agriculture, which accounts for 84 percent of the people's livelihood. The sale of a number of agricultural products is difficult due to high production costs and low quality. Many products are not competitive.

#### *3.4.2 Geographic (Spatial) Structure*

The geographic (spatial) structure of the economy shows considerable disparity, with large variations in the growth rates and a relatively low level of development in many northern and southern provinces. The economies in many areas remain unbalanced and the territorial potentials have yet to be strengthened. At the same time, the economic transition still remains slow, and a large share of the land is in agro-forestry. The development gaps between urban and suburban, provinces/territories, economic sectors, and the ethnic groups are large. Therefore, it is difficult to identify the intrinsic (but concealed) potentials in each province/territory.

#### *3.4.3 Labour Force*

The skill level of the labour force is developing slowly compared to the improvements in the economic components in each sector and area. The capacity development of the labour force is characterized by self-improvement, with only occasional opportunities for training, resulting in casual labour. Without proper institutional arrangements and training programmes, it would be difficult to achieve the objective of appropriately

redistributing the labour force and population to meet the requirements of industrialization and modernization.

### **3.5 External Economic Relations**

#### *3.5.1 Foreign Trade*

Exports and imports still face severe constraints. Exports per capita are still extremely low due to constraints in large-scale commercial production and in processing higher quality products. The export of unprocessed and low value added agricultural products accounts for a major proportion (about 50%) of the export revenues. Therefore, the value of exports is low and may be reduced easily due to fluctuations in price. Moreover, more than half the revenues from Lao exports are generated from products for which markets are unstable (e.g., garments), or the volume has reduced (e.g., wood), or which suffer from price declines (agricultural products). Interestingly, the rate of growth of exports is not yet stable and is lower than the GDP growth rate, while the exports of many countries in the world are increasing twice as fast or faster than the growth in their GDP.

The foreign trade management policy framework and measures need to be further developed in detail. The existing framework and measures do not ensure overall coverage and lack long-term vision, affecting their efficiency. In many cases, they demonstrate a lack of ownership, especially in the management of imports. Coordination between central and local authorities on exports and imports is still weak and inefficient. There is still a widespread shortage of management officers, technical staff, and workers with high technical skills.

Even though substantial imports have significantly contributed to the successful growth of domestic production and exports, they are increasing faster than the rate outlined in the Fifth Plan. The management of imports still faces severe difficulties. There is a general lack of market information and most of the imports are concentrated on smaller markets, and many technologies have been imported but obsolescence is still pervasive.

### *3.5.2 Foreign Investment*

Foreign investment increases at a slow pace. Investments in the agriculture, forestry, and fisheries sectors and areas with difficult access are very limited. At the same time, the capacity to attract investments in the industrial sector remains low. The licensing process is time consuming and cumbersome. Foreign investors face many difficulties due to the insufficiently open investment environment, inadequate facilities, and the lack of consistency and predictability. The costs of inputs such as fuel, electricity, telecommunications, and shipping are much higher than in many other countries in the region, restricting the competitiveness of Lao products and services and the attractiveness of the Lao PDR to foreign investors. Also, there are very few investors with the capacity to raise large volumes of funds from the regional and international economic groups.

One of the main causes restricting the growth of foreign investment in the Lao PDR is the insufficiency of skilled labour. Currently, skilled labour represents only two percent of the total labour force and is not able to meet the requirements of foreign enterprises that need highly skilled labour.

### **3.6 Social Development**

#### *3.6.1 Education and Training*

In the education and training sector, repetition and dropout rates are high and increasing. In 2005, the dropout rate was 8.9 percent at the primary level, 7.2 percent at the lower secondary level, and 3.2 percent at the upper secondary level. The repetition rates at primary schools, mostly in year 1, stood at 34.1 percent. Due to the low quality of graduates, few are accepted in the labour market, while the remainder are forced to work in sectors other than their areas of training.

The issue of insufficient teachers and substandard teachers has dragged on for many years, but efficient solutions have still not been applied. By 2005, about 19 percent of the teachers had not been properly trained. The curriculum is obsolete, while enrolment at the lower and upper secondary levels remains generally high. Current treatment of teachers and the management of the teaching corps are characterized by many inconsistent elements and fail to encourage teachers to undertake proper training as well as capacity enhancement activities. Teachers are paid very low salaries irregularly. Classrooms are insufficient to accommodate the rising number of students. This leads to a phenomenon where classes need to be rescheduled in lower and upper secondary schools. The ratio of students per class is high at around 70-80.

The literacy rate remains very low. The survey data show that in 2005, only about 68.2 percent of the people aged 15 years and over are literate, which include the 15-39 years age group with a literacy rate of 78.6 percent. According to another review, only about 45.2 percent of the population are literate with a breakdown of 53.7 percent for men and 36.3 percent for women. This review also indicated that only 37.7 percent of

the literate population have a normal level of application of their literacy skills and 30.8 percent are able to make good use of their literacy skills in their activities.

The training of personnel, workers, and skilled artisans does not meet the requirements of the labour market and the society. The development of education in isolated, ethnic, and highland areas is very slow. Illiteracy eradication efforts are not yet based on strategic plans and detailed procedures, and a substantial portion of the population is still illiterate.

The implementation of scholarship awards is slow. In 2005, only about 7.5 percent of persons with merit have received assistance, representing only 30 percent of the Plan target. (The Plan provides for the provision of assistance to 25 percent of students through different means.)

The education sector suffers from a severe lack of equipment and tools, particularly textbooks, learning materials, and school facilities. Teaching fails to meet the requirements. The ratio of schools meeting the standards set by the Government is still very low. The budget allocations made to education are very limited and not constant, with a peak of only 10 percent of the total budget expenditures. Within such allocations, up to 80 percent are provided from external grants, and the mobilization of these funds is subject to increasingly difficult conditions. The National Assembly agreed to allocate 12 percent of the budget to the education and training sector, but none of the provinces have yet received such an allocation.

### *3.6.2 Employment*

The need for new employment opportunities is huge, but employment generation is slow and there is a high level of unemployment. The allocation of the labour force is

shifting slowly, and has not brought about significant changes in socioeconomic development. Subsistence production results in the underemployment of labour and makes the management of social issues more difficult. The lack of external communication results in an inward-looking (insular) economy. The labour cooperation mechanism is not yet open to facilitate labour movement among districts and provinces, as well as other countries in the region.

### *3.6.3 Poverty Reduction*

In poverty reduction efforts, due to insufficiently firm coordination between the relevant agencies and unified guidance from the Government, each agency is left to carry out their sector's activities independently. The overall supervision, assessment, control, and monitoring of poverty reduction activities have not been entrusted to any agency.

Clear and specific credit policies need to be outlined to allow public funds to reach producers when required, and proper mechanisms need to be established to mobilize domestic and foreign resources to establish funds that would extend credit to the poor for the development of production activities and the reduction of poverty.

Civil servants including the technical staff of local administration authorities are insufficient in number and have inadequate capacities, and a substantial number have minimal qualifications. This is a major constraint to the dissemination of policies and programmes and the implementation of policy guidelines adopted by the Party and the Government, thereby affecting the efficiency of poverty reduction efforts.

### *3.6.4 Social Security*

The establishment of an efficient social security system for all Lao people to alleviate poverty is a long-term objective. Public servants are covered by a comprehensive range of provisions including pensions and health care financed partly through a six percent deduction from salaries and partly from the state budget. In 1999, the Government adopted a Decree on Social Security System for Enterprise Employees, establishing the foundation of a National Social Security Scheme. It called for the creation of a Social Security Organisation (SSO) that began operating in June 2001. The SSO administers the Social Security Scheme for enterprise workers in the private and the SOE sectors. The scheme provides protection coverage with respect to a range of contingencies/risks including the following:

- Access to health care from an approved health care provider for insured workers and their families;
- Long-term pensions in case of invalidity or old age and to surviving dependants;
- Short-term benefits in the event of incapacity to work by virtue of sickness or maternity; and
- Benefits in case of incapacity to work by virtue of an employment-related injury or sickness.

However, a very low proportion of workers are covered under the formal social security systems. Only 4.7 percent of the total labour force, with about 28 percent in Vientiane City, has social security coverage. In 2005, care and aid were given to only 7.5 percent of the total beneficiaries, accounting for 30 percent of the set target.

## **4. DEVELOPMENT PERSPECTIVES AND STRATEGIES**

### **4.1 Development Context**

On the positive side, there has been political and social stability over the past five years, and this situation is to be strongly maintained. The production capacities and abilities of many industries have increased substantially, and the economic structure has changed significantly. The enterprises and the national economy have adapted better to the international market, and the competitiveness of Lao products has improved steadily. The economic structure has changed progressively, and the implementation of the Party's instruction has been implemented methodically in priority projects. The market economy structure has been adjusted and progressively improved. The geographic location and natural resources of the Lao PDR attract tourism and investment. The country has been recognized as the transit center of the region.

Over the past five years (2001-2005), the production capacity and ability of many industries increased substantially, and the economic structure changed significantly. The quality of growth in many industries and regions has improved somewhat, with the enterprises and the national economy adapting better to the international markets. New and more radical policies introduced in the recent five years had positive impacts, attracting more investment from the society, especially utilizing internal resources for targeted investments, and bringing about structural changes in the economy.

The country has been recognized in the region and globally as having a dynamic economy within a stable political situation, and a safe destination for investment and tourism. Sociopolitical stability is an important foundation and an essential precondition for socioeconomic development, which is an advantage that the Lao PDR enjoys now.

The full membership of the Lao PDR in the regional and global political, economic, and monetary organizations including the World Trade Organization (WTO) will boost the dynamism of the economy and accelerate the country's development.

## **4.2 Government's Development Strategy Framework**

### *4.2.1 Overall Development Strategy*

The overall development strategy for the Lao PDR is based on the Lao Government's national development strategy framework mainly: (i) the Long-Term Strategy of Socio-Economic Development to the Year 2020; (ii) the Strategy on Industrialization and Modernization; (iii) the National Growth and Poverty Eradication Strategy (NGPES); (iv) The Sixth Five-Year National Socio-Economic Development Plan (2006-2010); (v) the Regional Development Strategy; (vi) various sector, thematic area, and subsector strategies and plans; and (vii) the analysis of the international and domestic contexts for the development of the Lao PDR.

The 7th Party Congress has set out the Ten-Year Socio-Economic Development Strategy (2001–2010) for the country, which includes improving and building the economic infrastructure to ensure fast and sustainable economic growth, with emphasis on agricultural production, eliminating forest fires and deforestation, reducing the number of poor households, and promoting industrialization and modernization. The country's human resources are to be developed step-by-step both in quality and quantity to cater to the emerging needs and make the country a regional centre for exchange of goods and services. The strategy encourages a socialist-oriented industrialization and modernization with infrastructure development to prepare the nation for graduation from the Least Developed Country (LDC) status by 2020 and to achieve improved well-

being for all the Lao peoples. The objectives set out in the Strategy support the achievement of the Millennium Development Goals (MDGs) and the implementation of the Brussels Programme of Action for Least Developed Countries (2001-2010).

The Sixth Five-Year National Socio-Economic Development Plan (or Sixth Plan) covering the five-year period 2006-2010 plays a crucial role in implementing the socioeconomic development policy guidelines set out by the 7th Party Congress. It is the vehicle for facilitating the implementation of the second half of the Socio-Economic Development Strategy (2001–2010) approved by the Congress. The Sixth Plan institutionalizes and concretizes directives and tasks that will be carried out further during the five-year period 2006-2010, to ensure that the overall targets outlined in the Ten-Year Strategy (2001-2010) are achieved.

#### *4.2.2 Development Directions*

The directions set in the Sixth Plan (2006-2010) are to achieve the highest outcomes and make general changes along the following lines:

(i) Turn from underdevelopment to fast and stable development, producing high value-added goods both in quantity and quality step-by-step in order to meet domestic market demand and increase exports;

(ii) Increase competitiveness and utilize comparative advantages to implement effectively international economic commitments in the frameworks of ASEAN and other bilateral and multilateral commitments, including the WTO;

(iii) Strengthen links between economic development and social development, and protect natural resources and the environment. Social problems should be solved first,

with attention paid to such issues as the reduction of poverty, unemployment, and social evils, and keep the social and political situation stable: and

(iv) Accelerate the building of a comprehensive socioeconomic infrastructure and finalize the establishment of a market-oriented economy with socialist orientation to form the basis for industrialization and modernization.

Thus, the Sixth Plan (2006-2010) is seen to be a breakthrough plan for creating a fast but firm and qualitatively enhanced development, with increased capacity for economic competitiveness, lifting the society to new heights both in material and moral wellbeing, significantly improving the quality of life of all the people, and boosting the nation's status in the international arena.

#### *4.2.3 Overall Goals of the Development Strategy*

The 7th Party Congress identified the general goals of the Socio-Economic Development Strategy for the 10-year period 2001-2010 as follows: *“Improve and establish the basis for the economy to progress strongly in firm steps, especially to strongly develop the agriculture sector; entirely eliminate the slash-and-burn cultivation practices; complete the tasks in solving the problem of poverty of people; create the foundation for industry; prepare the quality and quantity of human resources to be ready for industrial development and gradually turn to industrialization; and develop our country to become the central point of transit of the region in the future.”*

The Party Congress identified the following key expectations: GDP in 10 years (2001-2010) to increase to an average of 7.5-8 percent per annum; GDP per capita in 2010 to be US\$700-750; and the population growth rate in 2010 to be reduced to about 2 percent per year.

The main goals of the Sixth Plan (2006-2010) are to maintain all targets and views that have been set in the 10-Year Strategy (2001-2010). Therefore, the goals for the Sixth Plan are as follows:

*“Accelerate economic growth and improve the people’s quality of life, restructuring the economy and employment in building a market economy, based on the country’s rich resources and international integration. Further build the market economy with a socialist orientation. Continue to enlarge and develop effective external economic relations. Create breakthrough changes in education and training in terms of quality and quantity, utilising the advances in science and technology, protecting the environment, and taking human, scientific, and technological players as vehicles for development. Develop culture and society in synchrony with economic growth. Continue poverty reduction, creating jobs, and eliminating social evils. Continue strengthening the socioeconomic infrastructure as fundamentals for development in the Sixth five-year Plan and for the next (Seventh) five-year plan. Maintain political stability and social security, protecting sovereignty, territorial integrity, and national security.”*

Based on the goals set out above, the following tasks and guidelines are to be followed:

(i) Economic growth should be increased to an average of 7.5–8 percent per annum, establishing the fundamental economic players to support the next (Seventh) five-year Plan. Accelerate the progress of economic systems and enhance the potentials of products by region. To do so, the quantity and quality of goods and services and the level of competitive ability of all business enterprises and economic sectors must be improved, paying attention to the development of information technology and establishing the foundations for human resource development;

(ii) Ensure the balance in economic development in parallel with social development and protection of the environment, solving urgent social problems, and actively solving other ill behaviours in the society. Create job opportunities, reduce unemployment, uplift the people's level of material and mental wellbeing and living conditions, improve salary scales, reduce poverty, and take care of people who are national heroes and who have sacrificed themselves for the nation;

(iii) Encourage economic development in the various sectors by paying attention to the state economy as the leading sector; concurrently establish and develop other forms of the economy: collectives and private and foreign businesses; establish and implement the instructions and regulations related to the market economic arrangements with socialist orientation as a strong step. Pay attention to the creation of facilitating environments for investment and business activities in a consistent manner, and ensure transparency and a high level of economic competitiveness in the region;

(iv) Promote and develop small and medium enterprises (SMEs) to expand rapidly, and create the conditions to strengthen the financial status of state-owned business enterprises step-by-step, including the improvement of their debt situation;

(v) Ensure the maintenance of existing infrastructure; establish additional infrastructure specifically to support the socioeconomic development activities aiming to promote trade, investment, and tourism; increase the investment in the infrastructure for socioeconomic development; explore national resources including human resources to be used as potentials for development in an effective manner; establish and prioritize investment projects to establish effective economic structures and to be in a good position and ready for competition;

(vi) Continue to broaden economic opportunities and upgrade the level of external economic relations; create facilitating conditions to increase exports; attract investment in terms of funding and technology as inputs from external sources to support the production of goods and exports while taking ownership in economic integration at the international level: and actively and strictly implement bilateral and multilateral agreements at the central and local levels;

(vii) Continue to improve and strengthen the financial and monetary sectors by increasing the capacity of the national financial administration bodies; solve the problem of long-standing debts by utilizing many financial sources including financial balancing at local levels. Implement national policies on economization strictly; maintain macroeconomic balance; establish and develop financial markets to meet the needs of socioeconomic development activities;

(viii) Continue with progress on new changes to create comprehensive development approaches in the areas of education and capacity building; implement compulsory primary education programs; apply science and technology; upgrade the level of quality of human resources to catch up with the new changes in the economic structures; apply advanced and modern technologies in areas with favourable conditions with primary focus on economic areas at the center and in the provinces, municipalities, and cities;

(ix) Enhance the public administration activities with strong steps and improve and upgrade the effectiveness of state organizations. The relations between the state bodies and local people and business enterprises must be organized with transparent approaches allowing audits to be conducted; solve the problems of bureaucratic phenomena and corruption; and uplift the capacity of government officials in performing their duties;

(x) Strengthen the areas of national defence, public security, social and political aspects, and broaden foreign relations; maintain the society with stability; and create a favourable environment to support the development and protection of the nation.

The goals coincide with the MDGs and those in the Brussels Programme of Action for Least Developed Countries (2001-2010).

#### *4.2.4 National Priority Development Programs:*

To implement the overall development strategy successfully, the Lao Government has determined and approved 11 National Priority Development Programs for 2006-2010, namely:

1. Stability and Security Development Program
2. Comprehensive Agriculture Development Program
3. Forestry and Wood Processing Industry Management Program
4. Basic National Industry and Industrialization in Potential Sectors Program
5. Tourism and Service Promotion Program
6. Poverty Reduction and Stop Shifting Cultivation Program
7. Economic Integration and Investment Promotion Program
8. Communication and Transportation Development Program
9. Strengthening Macroeconomic Management Program
10. Human Resource and Cultural Development Program
11. Strengthening Effective Governance Management Program

## **5. POLICY RECOMMENDATION**

Based on the challenges and problems discussed earlier as well as on the Lao Government's development strategy framework, policy recommendations for deepening integration, narrowing development gaps, and promoting sustainable growth in the Lao PDR are made as follows:

### **5.1 Infrastructure Development by Focusing on Land-linked Country and Economic Corridors**

- (i) Improve and developing transportation infrastructure with neighboring countries
- (ii) Develop the transport corridors to become economic corridors
- (iii) Develop missing links to provide a complete package of infrastructure along main economic corridors
- (iv) Link all provincial capitals (and other key centres) to power, transport, and telecom networks via the main economic corridors
- (v) Develop urban infrastructure in rural villages and towns.

### **5.2 Strengthening Private Sector Development (SME, Market Development)**

#### **a) Promoting private sector development**

- (i) Clarify and strengthen the supportive role of Government
- (ii) Strengthen the Lao National Chamber of Commerce and Industry and Business Association
- (iii) Promote and facilitate substantive dialogue with the business community
- (iv) Promote and facilitate public-private development partnerships

- (v) Simplify and clarify the policy and regulatory framework for private sector enterprise and investment
- (vi) Strengthen trade access to neighbour country markets
- (vii) Integrate with production networks, investment clusters, and trade hubs by establishing national and cross-border production chains and by urban planning and town development
- (viii) Mobilize financial resources and facilitate access to credit
  - Establish a sound banking system and extend the services
  - Perform selective use of directed credit
  - Mobilize and coordinate ODA support
- (ix) Strengthen competitiveness through regular training on related activities

b) SME development strategy

- (i) Create an enabling regulatory and administrative environment for SMEs;
- (ii) Enhance competitiveness of SMEs;
- (iii) Expand domestic and international markets for SMEs;
- (iv) Encourage investments and improve access to financing by SMEs;
- (v) Improve access to appropriate work premises;
- (vi) Create favourable conditions for and facilitate establishment of business organisations;
- (vii) Encourage entrepreneurial attitudes and characteristics within the society;
- (viii) Finance SME development measures (programmes and projects).

c) Market development

### Development of Financial Markets

- (i) Establish strong regulations to control monetary-financial markets to facilitate foreign exchange operations and make the transfer (trading) of money in the market simple and transparent, while monitoring the movement of the volume of currencies in the market to ensure that it is consistent with sound monetary management.
- (ii) Strongly study the development of the bond market, setting forth the interest rate to be consistent with the changing situation and the trading within the bond market. Terminate the sale of government bonds to commercial banks to solve the problems of triangle debts (of SOEs).
- (iii) Consider developing the state-owned banks to enable the Government to supervise and monitor the performances of the monetary-financial system to be more transparent in solving doubtful debts through auditing of the accounts and the categorization of debts in accordance with international standards.
- (iv) Promote microfinance , which can provide financial input for small enterprises in rural areas.

### Labour Market Development

- (i) The Labour Law should be improved in order to ensure the balance of benefits between employees and employers, promoting and facilitating the workforce to have jobs in both domestic and international markets. Promote all economic players (sectors) to actively contribute to the creation of jobs in both quantity and quality.

- (ii) Improve the regulations on employment agencies (job seeking business) and dispatch of labour to work abroad in accordance with the direction of creating the conditions to enable multiple players to increasingly provide such services (more and more), while simultaneously improving the ability of the state to monitor the situation.
- (iii) Establish an effective social insurance system, particularly the unemployment insurance, creating equality on providing social insurance for the employees of all economic sectors (e.g., public, private, and voluntary).
- (iv) Improve the management system of labour markets within central and local regions.
- (v) Promote the involvement of mass organizations and nongovernmental organizations (NGOs) in developing the labour market and assign them some responsibilities, such as training, skills upgrading, performance on the job, job creation planning, and supporting plans for start-up of enterprises.
- (vi) Enhance the role of the trade union as the representative organization of the employees in order to facilitate the involvement of the labour force in plan formulation, setting forth policies on the labour (workforce) market, and monitoring the compliance with (observance of) the Labour Law.

#### Real Estate Market Development

- (i) Consider developing the real estate market, with the rights of land usage and ownership of dwellings. Create mechanisms for facilitating transfer of rights of land usage and ownership of real estate. Provide opportunities for the citizens and enterprises that belong to other economic sectors to be able to

own land, and have long-term leases for use in farming, for operating businesses, and to serve their daily lives.

- (ii) Facilitate land usage to establish and develop medium and large-scale farms in the areas where there are good conditions.
- (iii) Continue to disseminate the regulations on land use by Lao people living abroad and foreigners who invest in Laos.
- (iv) Urgently formulate laws, especially the law on the real estate market, and the regulation on the registration of properties, along with the dissemination of legal documents.

### **5.3 Tourism development**

- (i) Develop and promote cultural, eco-based, and historical tourism in the country as a sustainable tourist-friendly destination
- (ii) Facilitate the development of a more competitive tourism industry
- (iii) Link the national and local tourism industry with neighboring countries
- (iv) Integrate tourism considerations in town and community planning

### **5.4 Natural Resource-based Industry**

#### **a) Must be an environment-friendly and environment-oriented industry**

- (i) Implement ecological zoning, establish a strong environment-friendly legal framework, and develop an appropriate implementation mechanism.
- (ii) Cooperate with neighbouring countries to stop illegal logging, especially in remote border areas (including the NBCAs bordering on China, Thailand, and

Viet Nam) that are hard to monitor. Greater cooperation among neighbouring countries is also needed to stop the illegal trade of endangered flora and fauna.

b) Must be an economically efficient and economic-oriented industry.

- (i) Set appropriate resource prices: In addition to timber royalties, prices for hydropower concessions, water resources, and other natural resources in Lao PDR are normally set far below their marginal opportunity cost (MOC), leading to inefficient and wasteful resource use. Forest royalties are far below the MOC. In addition, pricing does not incorporate environmental externalities; pricing should not encourage overexploitation, as is now the case.

### **5.5 Develop the Processing Industry in the Country**

- (i) Develop agro-forest processing industry for export and domestic consumption.
- (ii) Develop mining based construction material industry (brick, cement industry)

### **5.6 Human Resource Development**

- (i) Implement the policy of universal compulsory education at the primary level and continue to increase participation at the lower secondary level, ensuring that all people have the opportunity to apply their education to serve the socioeconomic development programme;
- (ii) Strive to completely abolish illiteracy among the population;
- (iii) Expand vocational, technical, and higher education to meet the needs of the new labour market and to improve the economic rates of return;

- (iv) Train skilled workers, technicians, professionals, and intellectuals to have the capability to apply modern science and technology to serve the needs of socioeconomic development;
- (v) Raise national education standards gradually to be closer to international standards;
- (vi) Take education as the core of human resource development and invest appropriately in education; and
- (vii) Make education a right and duty of all the people in society.