

# Chapter 2

## Garments

August 2019

**This chapter should be cited as**

ERIA (2019), 'Garments', in Ambashi, M. (ed.), *Development Strategy of Five Selected Sectors in the Lao People's Democratic Republic (2020-2025)*. ERIA Research Project Report FY2018 no.7, Jakarta: ERIA, pp.27–44.

## Chapter 2

### Garments

#### 1. Current State

##### 1.1. Current State of the Garment Industry

According to an announcement by the Association of the Lao Garment Industry (ALGI), the Lao PDR's export of sewn products in 2017 amounted to \$175 million, an 8.8% increase from 2016. The ALGI reported that worker shortage is a chronic issue within the Lao sewing industry, leading to a decline in export values in the past several years.

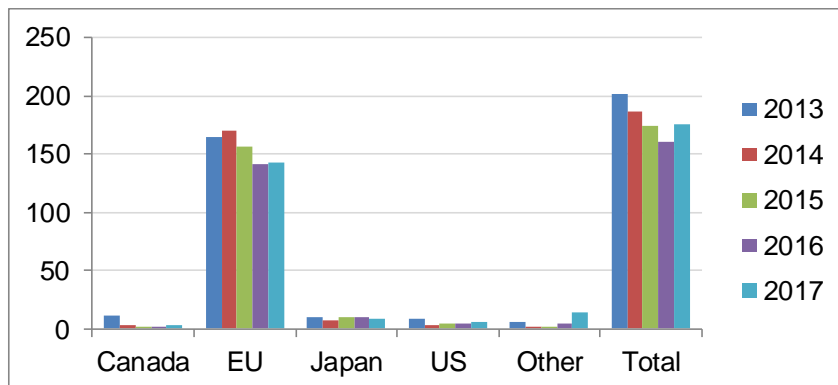
As of 2018, there are 78 sewing factories in the Lao PDR, located mainly in the capital of Vientiane and its environs. Of these, seven factories are owned by Lao capital. Japanese companies have made large investments in the sewing industry, followed by Thai companies. Of the 78 factories, 50 manufacture export-bound clothing while 28 handle both export-bound and domestic clothing. In addition, 28 factories manufacture clothing parts. These factories employ a total of 26,000 people, 90% of whom are women.

In 2017, exports from the Lao PDR to its major export counterparts increased and decreased year-on-year as follows (Figure 2.1): (i) the EU imported 31.04 million items valued at \$143.3 million (a 1.7% increase); (ii) Japan imported 1.78 million items at \$8.71 million (a 9.8% decrease); (iii) the US imported 1.74 million items at \$6.11 million (a 34.9% increase); and (iv) Canada imported 160,000 items at \$3.24 million (a 689.2% increase).

##### 1.2. Trends in the Volume and Amount of Clothing Exports

Figure 2.1 shows that the EU (depending on the generalised system of preferences [GSP] obtained) is the major destination of the Lao PDR's clothing exports, and that, while the value of goods exported to Japan may be small, the amount is stable. Figure 2.2 shows that, although export values have been plunging over the past several years, the average value is gradually expanding; and that, despite a temporary plunge in 2010, the unit price of goods is rising.

**Figure 2.1: Data on Trends in the Lao People’s Democratic Republic’s Clothing Exports to Major Export Counterparts (\$ million)**

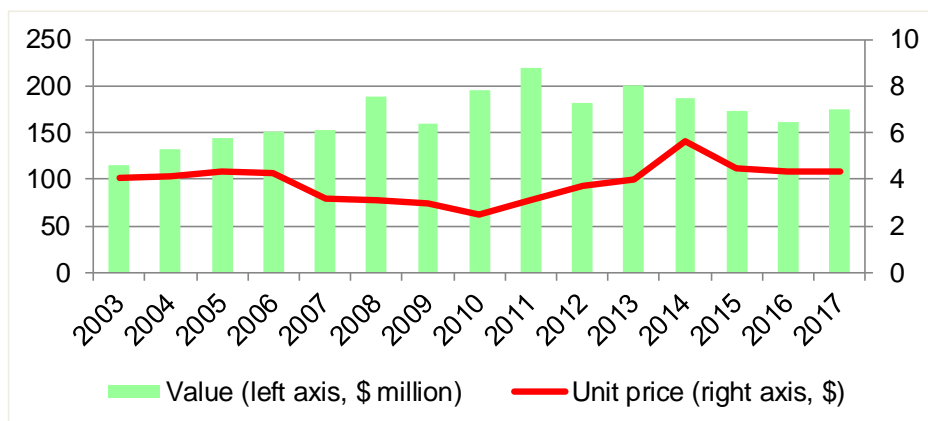


EU = European Union, US = United States.

Source: Ministry of Industry and Commerce, Lao Trade Portal.

<https://www.laotradeportal.gov.la/> (accessed 13 April 2019).

**Figure 2.2: Data on the Value and Unit Price of the Lao People’s Democratic Republic’s Clothing Exports**



Source: Ministry of Industry and Commerce, Lao Trade Portal.

<https://www.laotradeportal.gov.la/> (accessed 13 April 2019).

The top five export items in the Lao PDR are shown in Table 2.1 (for clothing) and Table 2.2 (for shoes) in 2016.

**Table 2.1: Top Five Items in the Lao People’s Democratic Republic’s Clothing Exports**  
(\$ million, 2016)

Product	Value	Export destinations
Non-knitted men’s suits	102.0	Germany: 41%, United Kingdom: 18%, Japan: 12%
Non-knitted men’s shirts	28.4	Germany: 19%, Japan: 13%, Netherlands: 12%
Non-knitted women’s shirts	19.3	Japan: 57%, Germany: 19%, Denmark: 9.9%
Knitted women’s shirts	17.9	United Kingdom: 34%, Japan: 29%, Italy: 15%
Knitted men’s undergarments	17.4	Germany: 38%, Italy: 26%, Canada: 17%

Note: Only the countries with the largest export shares are noted here.

Source: BACI International Trade Database, Centre d'Études Prospectives et d'Informations Internationales. [http://www.cepii.fr/cepii/en/bdd\\_modele/presentation.asp?id=1](http://www.cepii.fr/cepii/en/bdd_modele/presentation.asp?id=1) (accessed 13 April 2019).

**Table 2.2: Top Five Items in the Lao People’s Democratic Republic’s Shoe Exports**  
(\$ million, 2016)

Product	Value	Export destinations
Leather footwear	20.4	Japan: 62%, Italy: 9.8%, United Kingdom: 6.1%
Footwear parts	11.4	Thailand: 72%, Japan: 28%
Rubber footwear	3.9	United Kingdom: 55%, Japan: 26%, France: 9.0%
Fake fur	3.1	Japan: 71%, Thailand: 29%
Textile footwear	2.0	United Kingdom: 72%, Germany: 10%, Italy: 4.0%

Note: Only the countries with the largest export shares are noted here.

Source: BACI International Trade Database, Centre d'Études Prospectives et d'Informations Internationales. [http://www.cepii.fr/cepii/en/bdd\\_modele/presentation.asp?id=1](http://www.cepii.fr/cepii/en/bdd_modele/presentation.asp?id=1) (accessed 13 April 2019).

### **1.3. Orientation of the Five-Year National Socio-Economic Development Plan and its Assessment**

The Prime Minister’s Order No. 24 on the Five-Year National Socio-Economic Development Plan (7 May 2014) is based on the Ten Year Development Strategy for Manufacturing and Trade of the Ministry of Industry and Commerce: 2011–2020. The goals of the plan are as follows:

- (i) increased production efficiency and improved quality of workers to attract and promote labour-intensive industry;
- (ii) the establishment of a major clothing manufacturers group;
- (iii) increased productivity of the processing industry (priority areas: food processing and beverages, building materials, clothing, tobacco, and shoes);

- (iv) the promotion of silk and textiles (woven materials) as a new processing industry; and
- (v) the creation of global partnerships for development to increase exports by providing incentives, especially for agricultural goods, clothing, and textile goods.

Although approximately 26,000 workers are currently employed at sewing factories, the ALGI has determined that worker shortage is a chronic issue in this industry, and is preventing exports from increasing. However, according to a survey conducted by the MOIC, 30,000 unemployed people who have worked at sewing factories or similar companies in the past are seeking re-employment. Thus, it should be possible to secure about 60,000 people for the sewing industry. The 'worker shortage' identified by the ALGI refers to workers who have acquired the minimum required skills, while the 30,000 people identified by the MOIC are less skilled workers. Thus, it is essential to improve the skill quality of workers. Sharing the burden of providing the necessary education may be a major issue in the implementation of upskilling, that is determining whether employers will provide their workers with the education they need after receiving some kind of incentive from the government, or whether the government will provide education to workers directly.

Since the ALGI has been already established as the major clothing manufacturers group, a workers' organisation for clothing manufacturing is needed. Having such an organisation to maintain the working environment and educate workers may also be a means of improving labour skills in this industry.

Although the exploration of new markets and creation of global partnerships are extremely important factors, it is also necessary to conclude trade agreements and a broad range of GSPs with various countries including the United States in relation to trade (especially exports).

## **2. The Lao People's Democratic Republic's Advantages in Clothing Manufacturing: Preferential Tariff**

Exports of goods sewed in overseas factories are normally subject to tariffs, with some goods being subject to a tariff of 10% or more. In many developed countries, clothing is often subject to a considerable tariff. However, clothing and bedclothing exported from the Lao

PDR to other countries do not need to clear customs if 'Form A' or 'Form AJ' is obtained.

Form A refers to a certificate used to enjoy general preferential duties, which is a system to apply a low tariff rate or make the goods tax-free. This is provided by developed countries to support developing countries' economic development through trade. For example, exports of goods to Japan from developing countries such as Thailand or the Lao PDR can be made on more favourable conditions than those from developed countries such as the US or Germany. Since the Lao PDR is one of the poorest of the developing countries, it enjoys the special preferential tariff for least developed countries (LDC). In particular, under the customs agreement between Japan and ASEAN, goods can be exported to Japan from ASEAN countries including the Lao PDR on favourable conditions if Form AJ is obtained.

Form A is based on the principle of the two-step rule. As an exception, Form A can be obtained for fabric clothing (Harmonized System Code Chapter 62: articles of apparel and clothing accessories, not knitted or crocheted), even if the goods have undergone a single process of sewing. However, in principle, to obtain Form A with respect to clothing and bedclothing, not only the process of sewing but also the process of weaving the cloth must be conducted in the producer country. In other words, two production processes must have occurred in the producer country. Based on the economic partnership agreement between Japan and ASEAN, this condition is relaxed if Form AJ is obtained. For example, the processes of weaving and sewing the cloth must be carried out in the Lao PDR under ordinary circumstances, but if the cloth used was woven in an ASEAN member state (AMS) such as Thailand, Form AJ can be obtained, even if only the process of sewing was carried out in the Lao PDR. Form AJ cannot be obtained when the clothing is sewed from cloth imported from a non-AMS country, such as China.

In exporting goods from the Lao PDR, Form A can be applied if, for example a silk fabric woven in the Lao PDR using thread spun in the Lao PDR is exported or if clothing sewed in the Lao PDR using cloth woven in China is exported. On the other hand, Form AJ is applied when clothing or bedclothing sewed in the Lao PDR using cloth woven in Thailand is exported. As described above, one of the major advantages of sewing clothing in the Lao PDR is the possibility of enjoying a preferential tariff rate both when goods are created by sewing cloth imported from an AMS, such as Thailand, and when sewing fabric clothing using cloth imported from countries other than an AMS, such as China.

### **3. Major Bottlenecks for the Developing Garment Industry**

The Lao PDR's sewing industry has seen a decline in recent years. The total export sales of the industry increased from \$87 million in 1995 to a peak of \$219 million in 2011, but have been gradually declining since then, falling to \$174 million in 2015. In addition, clothing accounted for approximately 36% of exports during 2001–2005, but this share declined to approximately 8% during 2011–2015. FDI in the sewing industry amounted to \$65 million during 1991–2000 but declined to \$29 million during 2001–2010, and even further to \$10 million during 2011–2015.

The revealed comparative advantage index of the Lao PDR's sewing industry was an average of 13 during 2001–2005 due to the emergence of other leading export items, such as mining, electricity, and electronic components, but has declined to no more than 4 during 2011–2013 (World Bank, World Integrated Trade Solution). Although the revealed comparative advantage index of the sewing industry narrowly exceeds 1 (meaning that the Lao PDR still maintains its comparative advantage in this industry), this is also a signal of a decline showing that the industry is gradually losing its competitiveness.

One major reason for this decline is the decreasing demand in the global market. The majority of the Lao PDR's sewing industry consists of the so-called 'cut, make, and trim' (CMT) service, which mostly consists of work subcontracted from large companies in neighbouring states. The Lao PDR's industry is much smaller in scale than that of its competitors in neighbouring states. Due to weak domestic demand, most of its sewing factories depend on export demand for their production volume. The sluggish demand in EU economies and other markets is directly connected to the decline in orders for sewing produced in the Lao PDR. According to the ALGI, not only have orders recently been decreasing in EU markets, but also demand has been shifting to cheap products.

As mentioned above, the labour shortage is also creating a bottleneck for this industry. As a result of the major increase in the minimum wage in Thailand in 2012, Thailand's labour market became enormously appealing to workers in neighbouring states, including the Lao PDR. In addition, competition for workers with other industries, such as the booming services sector and 'other manufacturing' sector, has also occurred in the domestic labour market, and such competition is becoming especially intense in special economic zones. Thus, it has

become increasingly difficult for the sewing industry to secure and retain its workforce, especially in major manufacturing hubs.

Low labour productivity in the sewing industry is leading to increased production cost per product. While the Lao PDR's nominal minimum wage is extremely competitive within the ASEAN area, its labour productivity is significantly low relative to that of neighbouring states. Therefore, the real wage calculated by adding labour productivity is substantially high, resulting in a very small profit margin. This trend is especially prominent in CMT-based factories, where wages account for more than half of production costs.

The Lao PDR's sewing industry needs more supporting industries. Most of the necessary materials are generally procured from abroad through parent companies, contractors, and buyers. Ironically, cardboard materials are the only materials that can be procured domestically. This lack of domestic materials limits the potential to incorporate upstream works. Since the Lao PDR's small-scale sewing industry has limited experience and little processing ability in the private sector, it has no choice but to specialise in the simple CMT service, which is only a small step in the regional or global supply chain. This shortage of supporting industries is inhibiting the development of the Lao PDR's sewing industry.

To develop this labour-intensive industry, it is paramount to secure its workforce. However, since merely increasing the size of the workforce will not lead to increased labour productivity, enhanced education for workers is necessary. A workforce for the sewing industry can be mobilised by encouraging the movement of labour from agriculture to manufacturing. To do this, it is necessary to widen the wage gap between agriculture and manufacturing sufficiently; however, if companies independently increase wages, this could cause a heavy burden on the industry. Therefore, to improve labour productivity, it is necessary to provide the industry with incentives to do so, while supporting the provision of education on labour standards and codes of conduct to workers.



**Box 2.1: What Next for the Lao People's Democratic Republic's Apparel and Textile Industry?**

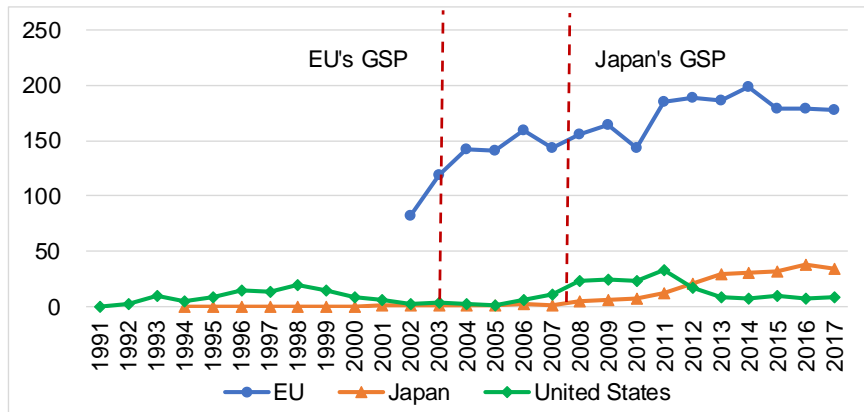
Industrialisation in most developed countries began with the apparel and textile industries. For example, the industrial revolution in Great Britain began in the 18th century with the introduction of steam-powered mechanisation in the textile industry. The apparel and textile industry played a major role in the emergence and expansion of factory-based production, and, thereby, industrialisation in most industrialised economies in Europe, the United States (US), and Japan.

The tradition of making clothes exists in all pre-industrial societies. The apparel and textile industry, which is literally the making of clothes using industrial means and methods, has undoubtedly smoothed the transition from traditional to industrial societies. Likewise, most newly industrialising economies kick-started their industrialisation through foreign direct investment in the labour-intensive apparel and textile industry starting in the 1970s. China did this in the 1990s, and has since made tremendous progress in industrialisation beyond the apparel and textile industry.

The apparel and textile industry can be an effective tool for facilitating the transformation of the Lao People's Democratic Republic (PDR) from a traditional to an industrial society. Since the 1990s, the Lao apparel and textile industry has grown to be by far the largest source of formal employment. Yet, in recent years growth has stagnated. Employment numbers declined from a peak of more than 50,000 to about 30,000 in 2017, and export volumes have also declined.

Thus, it is necessary to ask what can be done to regain the growth momentum of the sector. Examining the development of the apparel and textile industry in the Lao PDR so far (see Figure 2.3) provides a hint as to what may be done next. After foreign direct investment was introduced in the 1990s, apparel products began to be exported, partly as a quick and easy way to privatise the loss-making state-owned enterprises. Exports to the European Union (EU) market jumped from nothing to more than \$100 million by 2001. Although the EU's generalised system of preferences (GSP) was not formally given to the Lao PDR until 2002 upon official request, most exports since the mid-1990s had been carried out under such a scheme. In recent years, annual exports to the EU have amounted to \$150 million–\$200 million. Sizable exports to Japan, which also began with a GSP, amounted to around \$1 million annually between 1994 and 2007, and have sharply increased since 2008. Japan's GSP was effectively granted to the Lao PDR in 2007.

**Figure 2.3: Major Lao Apparel Exports and Destinations (\$ million)**

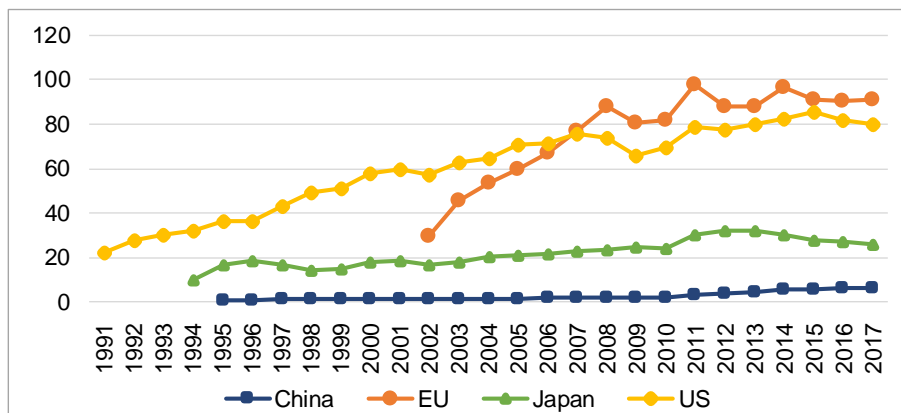


EU = European Union, GSP = generalised system of preferences.

Source: Global Trade Atlas. [https://www.gtis.com/English/gtis\\_about.html](https://www.gtis.com/English/gtis_about.html) (accessed 13 April 2019).

On the other hand, apparel exports to the US only amounted to around \$7 million in 2017. This is disproportionately small given the relative size of global imports by the US. As of 2017, the US was by far the second largest destination for apparel exports after the EU (Figure 2.4). Apparel exports to the US increased significantly after 2005, when normal trade relations were granted to the Lao PDR. However, benefits from normal trade relations and the GSP remain large, and only the latter can reasonably compensate for the high transportation costs and other locational disadvantages currently facing the Lao PDR. As has been the case with most newly industrialised economies since the second half of the 20th century, the US's GSP would undoubtedly give the Lao apparel and textile industry a big boost and effectively push forward industrialisation in the country.

**Figure 2.4: Major Global Apparel Importers (\$ billion)**



EU = European Union, US = United States.

Source: Global Trade Atlas. [https://www.gtis.com/English/gtis\\_about.html](https://www.gtis.com/English/gtis_about.html) (accessed 13 April 2019).

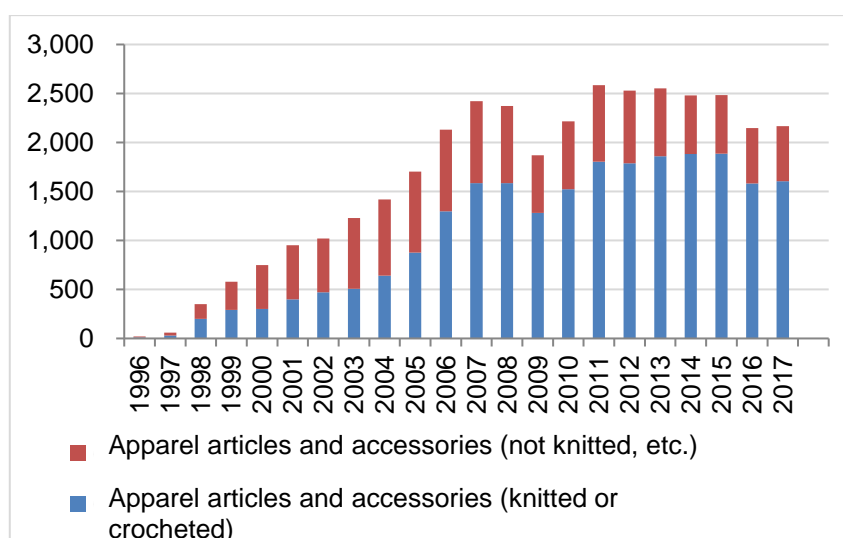
## 4. Policy Recommendations

### 4.1. Development of Export Infrastructure Based on Agreements Such as Trade Agreements and Generalised Systems of Preferences, and, in Particular, the Conclusion of an Agreement with the United States (Trade Agreement on Textile and Apparel)

Another factor prohibiting the expansion of exports is the stagnation in the expansion of agreements as such GSPs and the Textile and Apparel Trade Agreement (TATA). The expansion of domestic demand has had an extremely small effect on the promotion of clothing manufactured in the Lao PDR, and promotion measures centred on exports must therefore be taken.

To promote exports, it is first necessary to develop an environment in which it is possible to utilise agreements enabling the Lao PDR to export goods on more favourable conditions than those of other countries (i.e. trade agreements and GSPs). Of the Lao PDR's neighbouring states, Cambodia and Myanmar have already concluded agreements such as TATAs, and have sharply increased their export volume of textile products to the US (for Cambodia, see Figure 2.5). To resolve the comparative advantage with these competitors, the Lao PDR should conclude a TATA with the US to promote its current production network-type manufacturing industry. To promote the textile industry in particular, it is essential to conclude agreements with the US, where fast fashion is purchased in large amounts (for more details, see Box 2.1).

**Figure 2.5: Transition in the United States' Imports of Clothing from Cambodia (\$ million)**



Source: United States Census Bureau. United States International Trade Data. <https://www.census.gov/foreign-trade/index.html> (accessed 13 April 2019).

As shown in Figure 2.5, exports from Cambodia to the US became notable in 1997, and the US granted Cambodian products 'most favoured nation' treatment based on the 1996 agreement for normal trade relations with Cambodia. Cambodian products also enjoyed tariff exemptions or were assigned a low tariff based on the GSP by countries such as the US and EU. This preferential treatment prior to joining the World Trade Organization in 2004 has helped to expand Cambodia's exports of sewn products. Even after the lapse of the Multifibre Agreement under the World Trade Organization, Cambodia was treated as an LDC, and many goods in addition to GSP items are covered by tax-free status or tariff reductions. Based on the preferential treatment granted to imports of Cambodian products by developed countries, the Government of Cambodia has given preferential treatment to foreign capital and further introduced aggressive measures to attract foreign investment by enacting the Investment Act in 1994. Such preferential treatment for import countries, including European countries and the US, aggressive measures to attract foreign investment, and the development of a cheap and abundant workforce have attracted many foreign companies to expand their businesses in Cambodia.

Factories in the sewing and shoemaking industries often choose countries and regions where low-cost production based on low wages is possible. In many production sites around the world where foreign companies are located, working conditions established by organisations such as the International Labour Organization (ILO) are not complied with in a strict sense. However, Cambodia has increased its exports on the condition that it complies with labour standards such as those established by the ILO. When the US granted Cambodia 'most favoured nation status,' its imports of sewn products from Cambodia increased sharply. Furthermore, the US–Cambodian Bilateral Textile Agreements concluded in 1999 are a system to grant a quota of textile products that can be exported to the US under special duties, on the condition that Cambodia complies with the core labour standard. Under this system, production in a bad working environment, such as one in which cheap labour and child labour are used, is prohibited, and compliance with the ILO-specified labour conditions is required. Therefore, the Government of Cambodia is taking various measures, including amending the labour law, allowing the organisation of labour unions, and accepting an ILO audit on working conditions to enable sewing companies to obtain an export license.

Name brands and retail stores in developed countries that delegate production to factories in developing countries require compliance with the international standard of work

environments and corporate code of conduct at the time of production from the viewpoint of the company's corporate social responsibility (CSR), and surveys are carried out not only by the companies themselves but also by independent organisations. As a result, ILO inspections and the increasing costs of improved working conditions are less likely to lead directly to the withdrawal of companies from Cambodia, and instead often produce a virtuous cycle in which an improved working environment leads to improved worker quality and productivity.

Accordingly, even if labour unions are allowed to organise in the Lao PDR, labour disputes are less likely to occur if salaries and worker treatment matching the skill of the workers are ensured. Moreover, a certain increase in costs is considered less problematic for international manufacturing businesses and retail stores complying with CSR. The acceptance of an ILO audit, with which the Ministry of Labor and Social Welfare is concerned, is unlikely to cause major issues. If the Ministry of Labor and Social Welfare cannot solve this issue, it could be understood externally as creating a bad working environment or facilitating child labour, making it difficult for foreign companies emphasising CSR to expand their business in the Lao PDR. It would also stymie the promotion of all industries and the improvement of worker incomes.

#### **4.2. Protecting Workers and Providing Basic Education**

To resolve the problems of relatively expensive wages due to a shortage of employable workers and insufficient basic skills of workers, it is necessary to encourage the movement of the workforce from agriculture to industry and to provide support to educate workers on labour standards and codes of conduct.

Priority matters include creating a job-matching pilot project with the support of international organisations or cooperating with foreign-capitalised textile factories, training trainers to educate workers (i.e. training of trainers), and developing teaching materials. From this point of view, education to enhance awareness of jobs (e.g. recognition of service, habits of punctuality, and compensation for labour) is required from the primary and secondary education levels. Moreover, it is vital to organise labour unions and allow them to suggest programmes that they think necessary for education from an on-site perspective, and thereby

seek to enrich workers' education with the cooperation of the public, private, and labour sectors.

Sewing factories in Thailand currently employ a considerable number of skilful Lao workers as line managers and in similar roles. Highly skilled people can be easily secured by using appropriate treatment to encourage these people to return to the Lao PDR to work. Thus, it is important to provide preferential treatment that supports such movement of labour.

#### **4.3. Possibility of Expanding to the Materials Field Prior to Intensive Processing**

With respect to the possibility of expanding to the materials field, only raw materials originating from and producible in the Lao PDR, such as wooden and silk products, are competitive products. Since silken threads are mainly produced by hand in the Lao PDR, it is necessary to improve and introduce silkworms to make the original yarn, introduce and spread the growing technology, introduce yarn twistors, and foster technical experts. Since the stable production of mulberry trees is essential for the stable production of silkworms, cooperation from the MOAF is also necessary. The Government of the Lao PDR must establish, as a state, the specific direction and goals that outline its future vision for the production of silk thread.

### **5. Participation in the Supply Chain**

It is important to establish an omnichannel for clothing and to streamline manufacturing and logistics. In particular, unless cost reductions in logistics and prompt readiness are realised, it will be difficult for the country to participate in the regional supply chain. Thus, policies to realise these goals are necessary.

Since fashion in clothing changes rapidly, sudden changes frequently occur even when production is scheduled in every quarter. As such, there are many cases where corrections must be made contrary to the import and export control stated in the current master list. However, since current circumstances make it difficult for the Lao PDR's apparel industry to respond to such cases, the expansion of Lao businesses is limited to factories that create simple and stable products (e.g. underwear and shirts). Thus, the Lao PDR's apparel industry must enhance its cooperation with the apparel manufacturing companies within ASEAN,

especially major companies that have expanded their business in Viet Nam, Thailand, and Cambodia. The country can obtain a better position in the global supply chain by being incorporated in a single integrated production block, with a labour sector based on the advantages and limits of each country.

In addition, the government must clarify its policy on the clothing industry and take proactive measures to restore the previous system of refunding value-added taxes, or give preferential treatment to business matching for rental factories or the rental of manufacturing lines, to promote the industry in the future.

**Box 2.2: Establishing an Omnichannel for the Garment Industry**

‘Omnichannel’ refers to a system in which consumers have multiple options to obtain information, order, pay, and receive the goods they intend to purchase. In terms of clothing, this leads to a concept known as ‘demanding consumers,’ where customers order goods after customising the size, colour, and design online according to their own tastes, and receive the product manufactured to their order. This concept is a transformed model of ‘customer-centricity,’ and is a result of extreme advancements in information technology and efficient distribution.

The establishment of an omnichannel in the clothing supply chain is producing the following changes.

- (i) Diversification of customer contact: Customer contact is expanding not only through conventional channels (such as phone calls and e-mails), but also through social media and chat functions, in both business-to-business and business-to-customer service.
- (ii) Acceleration and visualisation of logistics: Since customers expect to obtain products rapidly and to know where the product is at all times, it has become necessary to make logistics more efficient and to cooperate with both warehouses and brick-and-mortar stores.
- (iii) Information transmitted by customers: In addition to the information transmitted from companies, the evaluations made in social media have all been connected to customers’ decisions. Therefore, product planning and marketing must be based on the collection of information transmitted from customers.

### **5.1.Support for the Expansion of ‘Fast Fashion’ Business**

Since fast fashion is heavily affected by changes in fashion trends and requires promptness, environmental concerns are arising in many places. Therefore, in allowing the expansion of fast fashion business in the Lao PDR, it is important to support such expansion only after establishing certain limitations, such as standards (e.g. labour and environmental standards in a narrow sense). Although this is extremely difficult under the Lao PDR’s current circumstances, it may be possible to attract fast fashion factories in the future if workers’ skills are improved and the supply environment is developed.

## **6. References**

### **6.1 Company C (Japanese Company Operating in the Lao People’s Democratic Republic; Shoemaking Industry; 600 Lao Workers)**

#### **Present Business Operations**

Business is expanding smoothly, and the company mainly produces products for Japan. Due to the large number of factories that have moved into the surrounding areas, it is becoming more difficult to secure a workforce.

#### **The Advantages of the Lao People’s Democratic Republic**

Labour is cheap, and people are motivated since the country is young. Expenses including electricity are also relatively cheap. If proper educational methods are used, it will be possible to provide a thorough education based on the Japanese ‘5S’ methodology (i.e. sort, straighten, shine, standardise, and sustain).

#### **Present Bottlenecks**

It is difficult to provide operator education on machines, for example, as workers have an insufficient level of basic knowledge of industry. This should be taught in the subject of science at junior high schools in Japan. The personnel turnover rate is also higher than in other countries. When we started our business, the rate was approximately 10% per month; it has now settled to approximately 4% per month, but this is still high. Human resource development and the job retention rate are not balanced. Some people choose to leave their



jobs despite having acquired a certain level of skill and increased salary. This is extremely problematic for the company as it is directly connected to production.

### **Requests to the Government of the Lao People's Democratic Republic**

Certain issues concerning the refund of value-added tax need to be resolved. Although we have carried out the procedures as specified by law, we have not been refunded value-added tax since 2014. Another issue is that the master list cannot be established beyond the amount of capital. Under the current situation, basic factory management accounting by which capital and assets are separated cannot be implemented. Materials and other items are liquid assets, and production according to orders is the basis of factory production. While the production volume can be planned to some extent, in some cases the necessary volume increases rapidly due to economic trends, making it impossible to respond to such cases by production control based on the master list. It is difficult to handle the flow of increased orders, expansion of production volume, and expansion of the factory.

### **Policies and Improvements Required for Future Business Expansion**

Although the change in the legal system itself is of no consequence, if the system is not operated scrupulously in keeping with the law, it is difficult for the manufacturing industry, which is investing in factory equipment, among other things, to expand its business. Legal amendments can be reflected in management if notification of them is provided in advance. However, unless the laws are operated accurately, the company will lack reliable sources to help them decide whether or not to continue investment. Forms for export and registration, for example, must be unified and computerised. Much time is lost due to the many procedural corrections caused by frequent changes of forms and corrections in office procedures, which lack unity because they involve people at counters.

### **Measures Required for the Future Development of the Lao People's Democratic Republic**

Rapid development might be unnecessary for the Lao PDR. We believe that a certain level of developments that do not put the Lao PDR off its stride are relevant to the quality of the products produced in the factory.

Workers must acquire basic knowledge in the industrial field. People tend to continue working being satisfied with the same amount of experience on which they have been relying while lacking any basic scientific, physical, and industrial knowledge. This is reflected in the

quality of goods being produced. We believe that it is currently difficult for Lao workers to engage in the production of advanced industrial products, for example. While it may be unnecessary to teach detailed industrial knowledge at the elementary, junior high, or high school levels, it is necessary to implement education swiftly to encourage Lao workers' interest in basic knowledge and science. We believe that this is a major necessary step to secure the future of the Lao PDR.

## **6.2 Company D (Japanese Company Operating in the Lao People's Democratic Republic; Sewing Industry; 240 Lao Workers)**

### **Present Business Operations**

Business is on track with a focus on women's apparel and pants for men's suits; the company mainly produces products for Japan. The company also exports 100,000 items of women's clothing, and produces original manufacturing equipment every year.

### **The Advantages of the Lao People's Democratic Republic**

Labour is relatively cheap, and there have been no recent power outages, making the infrastructure stable.

### **Present Bottlenecks**

Worker quality is a major issue. Although labour is cheap, workers have a low level of basic knowledge about labour, meaning that the advantages of the low labour cost cannot be fully enjoyed. The annual turnover rate for factory workers is higher in the Lao PDR (20%–30%) than in other countries (less than 10%). Many processes, such as cutting, sewing, and shaping, are mechanised, and many workers leave their jobs without moving to another factory, despite having been trained as operators and reaching a sufficient level of expertise. Such circumstances make it difficult to improve the state's industrial level in this industry.

### **Requests to the Government of the Lao People's Democratic Republic**

The labour law is a major bottleneck. While the establishment of minimum wages was anticipated and is not disruptive, the establishment of payment for holiday or overtime work in such a manner as adding a specific percent to a worker's base salary makes it difficult to use managing members with high base salaries flexibly. To maximise the efficiency of the

factory, machines must be operated at all hours. Under the current provisions, unless we stop the machines during holidays and at midnight, the cost of operating the factory will prove prohibitive and investment recovery will take time, making it difficult to realise additional investments. We ask that the Lao government separate the provisions for simple workers from those for managing members, to permit more flexible operations. Equality in labour recruitment must be also ensured.<sup>1</sup>

### **Policies and Improvements Required for Future Business Expansion**

Issues concerning laws and procedures change every year, and the interpretation and operation of laws are carried out differently by each person in charge of the procedures at the counter. Policies lack consistency, making it difficult to grasp the specific direction in which the Lao PDR is seeking industrial development. Thus, as a manager it is difficult to determine the extent to which one should invest in facilities and the scope for expansion in the future.

### **Measures Required for the Future Development of the Lao People's Democratic Republic**

Settlement of human resources is required. In any industry, technology and know-how will not be accumulated unless experience in the same business is gained over a significant period of time. The mismatch between the improved skill level of workers and wages should also be resolved. If the Lao craftsmen had the same skills as the factory workers in Japan, we would treat them similarly based on the principle of equal pay for equal jobs. However, the differences between the two cohorts in terms of skills and attitude toward labour is so large that it is difficult to provide identical treatment under the current conditions. We believe that it is more urgent than ever to educate workers of all ages on attitudes toward labour. Based on the experience of managing factories in the Lao PDR for more than 10 years, we believe that a factory in which treatment and comfort are well-balanced is necessary for the Lao people.

---

<sup>1</sup> Of the intermediaries that introduce workers to the Lao PDR's sewing factories or other sewing factories owned by foreign companies other than Japanese companies, some offer workers guarantees that they will be treated better at the destination factory than at other factories, on the condition that they post a security deposit to the company (i.e. the act of having the company keep part of their salary or boost in pay for several months as a reserve), to prevent them from leaving their job. However, in reality, the deposit is not returned if there is no change in their treatment; and equality in securing workers is not maintained.