Workshop on “The Belt and Road Initiative and the Economic Diversification of Landlocked Developing Countries: Opportunities and Challenges for Lao PDR”

Lao PDR’s Economic Diversification and Regional Integration

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Dr Hartmut Janus
RELATED Project Director
Table of Contents

1. Lao Economic Growth and Economic Structure
2. The Quality of Lao Growth
3. Regional Economic Integration and Cooperation
4. Laos‘ Integration into the ASEAN Economic Community
5. Selected Challenges for Economic Diversification and Regional Integration
6. The Role of Technology Transfer and Innovation
Lao Economic Growth and Economic Structure

• Since several years, the Lao economy experiences **high economic growth rates**, averaging around 7% per annum

• While maintaining the **level of growth**, the **quality of growth** might be further improved

• High relevance of the **Mining Sector** and the **Hydropower Sector** for the Lao Economy
  
  • Mining Sector and Hydropower Sector are comparatively **capital-intensive**
  
  • Natural Resources will be **exhausted** at one point in time
  
  • **Prices** of Natural Resources depend on world markets, cannot be influenced by Laos and fluctuate sometimes importantly
Lao Economic Growth and Economic Structure II

- The productivity in the *agricultural sector* can be further improved
  - More than 70% of the Lao *work force* are occupied in the agricultural sector
  - However, the Lao agricultural sector contributes only around 30% to the Lao *GDP*
  - Often, *raw materials* are exported; the scope of agro-processing can be further developed
- The *services sectors* are dominated by wholesale and retail trade
  - Substantial potential for further development for example of the *tourism sector*, the *transport and logistics sector* and *selected* other services sectors
Lao Economic Growth and Economic Structure III

- The **industrial base** in Lao PDR is still comparatively weak
  - However, during the last years, first signs for a **potential economic transition** can be detected
  - Substantial investments by some multi-national companies in the **manufacturing sector**: digital cameras, optical lenses, electronic parts, parts for the aviation industry
  - Factories in Laos are usually part of **regional value chains**
  - Investments are often **intense in unskilled labour**
  - Investments are concentrated in some **Special Economic Zones**, often close to the capital city, to transport corridors and/or to border posts
Lao Economic Growth and Economic Structure IV

- **Diversification** of the Lao economy might be further improved
  - On the **supply side**: high relevance of raw agricultural products, mining and hydropower
  - On the **demand side**: export structure is comparatively little diversified, concentrated on a limited number of countries (Thailand, Vietnam and China)
The Quality of Lao Growth

- Potentials to improve the **Quality of Growth**
- **Enhance the Inclusiveness of Growth**
  Inclusion of more Lao people into productive processes, creation of more productive jobs
- **Strengthen the Sustainability of Growth**
  Relying less on National Resources that will be exploited in a point in time; strengthening sustainable economic development
- **Improve the Smartness of Growth**
  Improving the productivity of parts of the Lao economy; strengthening the use of human skills, technology and innovation
- **Enhancing the Resilience of Growth**
  Diversifying the economic and export structure; becoming less dependent on goods, the prices of which are determined on the world market and fluctuate importantly
Today, development takes place in a globalised world. Economic activity transcends national borders. Regions are ideal gateways for connecting to the world market.
### Regional Economic Integration and Cooperation

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<th>Potentials</th>
<th>Challenges</th>
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<tr>
<td>• <strong>Tightness</strong> of domestic market is overcome</td>
<td>• Loss of <strong>tariff revenues</strong></td>
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<td>• Trade with <strong>perishable goods</strong> enabled</td>
<td>• <strong>Decrease of wages</strong> because of immigration</td>
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<td>• Integration into <strong>regional value chains</strong> improved</td>
<td>• <strong>Emigration of skilled workers</strong></td>
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<td>• Access to sea ports (to <strong>international markets</strong>) improved</td>
<td>• <strong>Domestic firms</strong> are pushed out of the market** by more competitive foreign enterprises</td>
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<td>• <strong>Attractiveness</strong> (of the whole region) for foreign investments improved</td>
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Laos‘ Integration into the ASEAN Economic Community

• **ASEAN**
  - 10 Member States
  - 625 million inhabitants
  - 2.4 trillion US-$ purchasing power

• **ASEAN Economic Community** established at the end of 2015

• **ASEAN Economic Community Blueprint 2016 – 2025** defines the regional economic integration agenda for the ten years to come

• **Regional Comprehensive Economic Partnership (RCEP)** currently negotiated among the ASEAN + 6

• **China – ASEAN Free Trade Agreement** effective since 2011; more comprehensive Economic Partnership Agreement under negotiation
Laos’ Integration into the ASEAN Economic Community II

• Pillar One of the AEC: “A Highly Integrated and Cohesive Economy”… facilitates the seamless movement of goods, services, investment (…), in order to enhance ASEAN’s trade and production networks, and to establish a more unified market for its firms and consumers.”

• Key concept for Laos to benefit from the AEC is Competitiveness. Enterprises in Laos have to increase their productivity, enhance their quality and reduce their costs to make use of the ASEAN Economic Community and to reduce its economic risks

• Laos should focus on those economic areas, where it has comparative advances
Laos’ Integration into the ASEAN Economic Community III

- **Comparative advantages** of the Lao economy, amongst others
  - Low wages of unskilled labour
  - Clean, comparatively affordable energy
  - Macroeconomic and political stability
  - Strategic geographical position in the heart of the Mekong area
  - “Risk diversification” of multi-national companies
  - Cultural ties with Thailand (same language)
Laos’ Integration into the ASEAN Economic Community IV

• AEC strengthens the development of and facilitates the involvement of companies in Laos into regional value chains

• Multi-national companies set up production networks in ASEAN, making use of comparative advantages of the different ASEAN Member States

• Lao PDR enters regional value chains rather at production steps that are intensive in unskilled labour and at agricultural processing
Laos’ Integration into the ASEAN Economic Community V

• In the **short term**: “First Phase” of Economic Transition
  
  • Increase in productivity in agriculture
  
  • People formerly employed in agricultural sector **move to the industrial sector** (and services sectors), are employed in production steps that are rather intense in comparatively unskilled labour
  
  • Way other successful economies diversified into the industrial sector a few years ago
  
• In the **medium to long term** (5 – 10 years), challenge for enterprises in Lao PDR will be to **step up the “value chain ladder”**, i.e. to enter into parts of regional value chains that are **more intense in human capital**
Selected Challenges for Economic Diversification and Regional Integration

• Comparatively low level of highly qualified workers

• **Business and investment climate** (Doing Business Index position 134)

• High costs of transport and logistics

• Difficult access to finance (in particular for small and medium enterprises)
The Role of Technology Transfer and Innovation I

- **Technology transfer** and **innovation** as important tools for businesses in Laos to **increase** their **competitiveness** and thus make use of the potentials as well as to reduce the economic risks of the AEC.

- Focus of technology transfer and innovation on **those sectors**, in which Laos has **comparative advantages** in the context of the regional economic integration process (AEC and RCEP).
  - **Agriculture** (in order to increase productivity in the agricultural sector)
  - **Agro-processing**
  - **Manufacturing**, in particular in those parts of the value chain that are more **intensive in unskilled labour**, **energy-intensive** or where the **ratio between value and weight** of products is **favourable** (taking into consideration high transport costs)
  - Selected **services sectors** (tourism, transport, logistics, ICT)
The Role of Technology Transfer and Innovation II

• Increase in competitiveness in services sectors such as Transport and Logistics as well as ICT has **two positive effects**:
  
  • Generation of jobs, value addition and incomes **in the services sectors themselves**
  
  • **Reduction in transaction costs** for all sectors of the Lao economy making use of these services
  
• Use of **appropriate technology** in Laos
  
  • Taking into consideration the **lack of skilled labour, lack of access to finance** etc.
  
  • In some cases, the technology used in Laos might be a technology, that has **already been successfully applied** in neighbouring countries, and that has to be **adapted to the Lao context** (re-location of production facilities e.g. from Thailand to Laos).