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## LAOS. GENERAL ECONOMIC AND INTERNATIONAL VISION

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## I. BACKGROUND

The Lao PDR is the only land-locked developing economy (LLDC) located in the Southeast Asia region and has joined the Association of Southeast Asian Nations (ASEAN) in 1997 as a member. The population of Laos is fragmented in the region compared to other ASEAN members but not the land. Laos had a population of 6.9 million people in 2018, much lower than its neighbors Cambodia (16.3 million), Myanmar (53.9 million), Thailand (69.2 million), and Vietnam (96.7 million). The total land area of the Lao PDR is 236,800 km<sup>2</sup> and the population density is 28 people per km<sup>2</sup>, which is much lower than its neighbors (ADB, 2017b). However, this does not imply that more space is available for both residential and economic utilization including agriculture and manufacturing. This is because two-thirds of Laos is constituted of mountainous areas while one-third is contaminated with the unexploded ordnance (UXO) from the Indochina war, especially 1964–1973, making Laos the most heavily bombed country in the world in terms of the number of bombs per capita (UXO LAO, 2013). Less than 10% of such contaminated land has been cleared. Therefore, this currently poses a challenge to economic expansion in the Lao PDR, especially agriculture on which the majority of the population is dependent.

Major economic reforms in the Lao PDR began in 1986, 10 years after its independence in 1975 post the

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Indochina War (1946–1973) when the central planning system was replaced by the market-oriented system called “New Economic Mechanism (NEM)” introduced by the President Kaysone Phomvihane during the Fourth Party Congress of the Lao People’s Revolutionary Party (LPRP) in 1986. LPRP is the only political party ruling the country since its independence. Therefore, Laos is considered one of the most politically stable countries in the world. Its political system is similar to its alliances with China and Vietnam. Before 1986, Laos was a closed and centrally planned economy where production and price setting were decided by the central government. This isolation of Laos from the global economic integration resulted in the lagging of its economy (Hara, 2002). Nevertheless, with the new economic system (NEM), its economy has been gradually exposed to the global economy through several economic reforms such as trade, investment liberalization, agricultural reform, privatization, and pricing and exchange rate liberalization. The major economic reforms were the simplification of tariff structures and the creation of the foreign investment law in 1988. Even though the progress of reforms under NEW was slow (Than & Tan, 1997), the country’s external trade has since expanded, with total export value increasing from US\$43.8 million in 1984 to US\$216.5 million in 1995 and US\$5.7 billion in 2019. There were more than 70 trading partners and foreign investors from 52 countries investing in Laos (Department of Export and Import, 2018; Ministry of Planning and Investment, 2020). The major local trading partners are Thailand, Vietnam, and China, and the following products are exported to them: mining, electricity, agricultural products and live animals, and coffee. Simultaneously, imports rose from US\$162 million in 1984 to US\$6.49 billion in 2019, much higher than the exports making Laos a trade deficit country for many decades. Foreign investment also jumped from US\$2 million in 1988 to US\$2.32 billion in 2019. Along with the domestic policy reforms, Laos has increasingly engaged in international cooperation and relations. So far, it has relations with more than 130 countries and organizations such as the United Nations. Besides, Laos has actively participated in the sub-regional, regional, and international cooperation platforms such as the Great Mekong Sub-region (GMS), ASEAN, and World Trade Organization (WTO) that gives Laos more political power in trade and investment negotiations. This cooperation also drives domestic trade reforms such as regulatory and institutional reforms to access the regional and international markets, which is essential for Laos to overcome its current constraints as a small domestic market and land-locked country.

Because of the policy reforms, liberalization, and international cooperation, the Lao economy has a high recorded economic growth of 6.8% in 1990–2018 as one of the fastest-growing economies in ASEAN. Its income

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per capita jumped from US\$290 in 2000 to US\$2,627 in 2018, surpassing its neighbors such as Cambodia (US\$1,539), Myanmar (US\$1,440), and Vietnam (US\$2,546). This allowed it to transit from a status of low- to a lower-middle-income country since 2011, along with other new members of ASEAN namely Cambodia (2015), Myanmar (2014), and Vietnam (2009), according to the World Bank's analytical classifications. However, because the record economic growth has been strongly influenced by the natural resource sector invested in mainly by foreign investors, an unsustainable income distribution within the country could be observed. For instance, the employment in the resource sector was less than 1% of total employment in 2015 while the labor productivity (equivalent to real wage) in this sector was 12 times higher than the non-resource sector (Sayavong, 2017). Moreover, several development indicators such as poverty and human development for Lao PDR are not progressing as expected and still lagging compared to other ASEAN countries. Table 1 highlights some selected development indicators of Lao PDR in the ASEAN region. It found that, for instance, the national poverty rate in the Lao PDR was 18.3%, while the poverty in Cambodia, Thailand, and Vietnam was better off except Myanmar and Philippines. In terms of the Human Development Index (HDI), the Lao PDR was ranked at the bottom at the global level (140 out of 189 countries in 2019). Though the Lao PDR is likely to meet the Least Developed Countries (LDCs) graduation eligibility for 2021 because two of three graduation criteria, namely, Gross National Income (GNI) per capita and Human Asset Index (HAI) are already met, the Economic Vulnerability Index (EVI) is still far from being achieved, according to UNDP (2018). Besides, the Sustainable Development Goals (SDGs), which continued and expanded the Millennium Development Goals (MDGs), are targeted for completion by 2030 posing another formidable challenge for the Lao PDR to achieve in the years to come.

Hence, this study aims to discuss the opportunities and challenges for economic development and international relations for Laos in the twenty-first century. To this end, it firstly reviews the historical background of Lao economic development and its international cooperation by drawing on outstanding events in previous years. Secondly, the outlook of Lao economic development and its cooperation with the external entities are discussed based on the available literature and government documents in terms of long term strategies. This study is divided into four sections. Section 2 reviews historical economic development until the most recent years. As Laos is a land-locked country, infrastructure development is essential for its economic development. Therefore, the background of infrastructure development is presented in Section 3. Section 4 highlights the international relations of

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Laos, whereas section 5 discusses its general vision for 2030 and beyond. Then, the study concludes in section 6.

TABLE 1. SELECTED DEVELOPMENT INDICATORS IN ASEAN

COUNTRY	POPULATION (THOUSAND PERSONS)	GDP PER CAPITA (USD)	NATIONAL POVERTY RATE (%)	GINI	HDI RANKING
	2018	2018	2017	2017	2019
Brunei	442.4	30,668.3	n.a	-	43
Cambodia	15,981.8	1,539.8	13.5	0.310 (2016)	146
Indonesia	265,015.3	3,923.8	10.6	0.393	111
Lao PDR	6,887.1	2,627.5	18.3 (2019)	0.364	140
Malaysia	32,385.0	11,067.2	0.4	0.463	61
Myanmar	53,625.0	1,440.8	24.8	0.381	145
Philippines	106,598.6	3,086.9	21.6	0.401	106
Singapore	5,638.7	64,567.3	n.a	0.459	9
Thailand	67,831.6	7,446.5	7.9	0.378	77
Viet Nam	94,666.0	2,546.2	9.8	0.348	118
ASEAN	649,071.5	4,577.5	na	na	na

**SOURCE:** Created by the author based on data from ASEAN Secretariat, 2019; LSB, 2020; UNDP, 2019

## II. THE LAO ECONOMY

Laos is one of the fastest-growing economies in ASEAN. In recent years, its macroeconomic development has shaped up pretty well in the ASEAN region. While the economic growth was relatively high in 2013–2018 compared to other ASEAN countries, its inflation rate was also low (Table 2). Nevertheless, the domestic market is small as the share of its GDP was less than 1% of the GDP of ASEAN amounting to US\$18 billion. When compared to that of its neighbors, namely Thailand and Vietnam, the size of the Lao economy was 4% and 8%, respectively. Also, its exports as a share of GDP are tiny though backed up by a resource boom, particularly mining and electricity hydropower projects. On the other hand, the manufacturing sector had not been well developed since its share of GDP stagnated at around 7–8% during the last decade. The main features of the Lao manufacturing sector are largely dominated by micro- and family-sized firms. The latest Lao economic census (2013) reveals that 15,573 manufacturing establishments (equivalent to 12.5% of all enterprises) are in operation, of which 74.5% are micro-enterprises with less than five employees (Lao Statistics Bureau, 2015a). As for the rest, 14.3% of firms employ between five and nine persons

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and 10.4% between 10 and 99 persons and only 0.7% with more than 99 persons. Large enterprises are mainly garment factories owned by foreign investors engaging in simple labor-intensive production, employing unskilled workers at cheap wages. As for those in the food-processing, furniture, and primary wood-processing industries they are mainly small and medium-sized enterprises. Heavy and high-tech industries such as chemicals, metals, electronics, and machinery and equipment are rare in its economy, so their share is less than 5% of all manufacturing. The share of the service sector is significant without a doubt. However, most of these enterprises (95% of total) are small and medium-sized too (Lao Statistics Bureau, 2015a). New shopping malls, telecommunications, and financial institutions are among the large enterprises in the service sector. Meanwhile, the share of agriculture to GDP declined sharply during the studied period, but the majority of labor (66%) is still in this sector. Rice, maize, cassava, coffee, and sugarcane are the main agricultural products of the Lao PDR sharing more than 90% of total agricultural land. The share of industries implies the rigidities of economic structural transformation of Lao PDR as well as its weak capacity to integrate more into the regional and global economy in the previous year although it has joined several bilateral and multilateral cooperation frameworks including the ASEAN free trade agreement and World Trade Organization (WTO).

TABLE 2. SELECTED KEY MACROECONOMIC INDICATORS

COUNTRY	REAL GDP (%)	INFLATION (%)	NOMINAL GDP (USD MILLION)	MANUFACTURING (% GDP)	EXPORT (% GDP)	IMPORT (% GDP)
	2013-18	2013-18	2018	2018	2018	2018
Brunei	-1.0	- 0.2	13,557	14.1	48.5	30.7
Cambodia	7.2	2.6	24,634	19.9	23.9	34.0
Indonesia	5.1	5.3	1,041,562	16.3	17.3	19.7
Lao PDR	7.2	2.7	18,096	7.5	30.6	32.3
Malaysia	5.1	2.5	358,412	21.6	69.0	60.7
Myanmar	7.1	6.7	77,264	23.9 (2017)	21.6	25.0
Philippines	6.5	3.1	342,693	19.1	19.7	33.6
Singapore	3.5	0.6	364,076	20.8	113.2	101.8
Thailand	3.1	0.8	505,060	26.9	47.7	38.0
Viet Nam	6.4	(0.2)	241,039	16.0	100.8	98.3
ASEAN	5.2	na	2,971,095.2	na	75.8	75.2

SOURCE: Created by the author based on data from ASEAN Secretariat, 2019; World Bank, 2020

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The economic development of Laos has gone through several historical phases since its independence in 1975. According to Saignasith (1997), the economic development in the first period between 1975 and 1980 was the period of recovery from the destruction of the Indochina war (1946–1973). After that, the First Five Year Plan (1981–1985) was introduced at the Third Party Congress of LPRP in April 1982. The objective of economic development during this time was to formulate the administration for state control or centralized economic mechanisms including price control, subsidies, trade regulation, and public sector production and distribution system. The aim of the first 5-year plan was to expand the production from agriculture and forestry to manufacturing (Ministry of Planning and Investment, 2015). However, the outcome of centralized economic reform resulted in economic problems such as high inflation, large budget deficit, trade deficit, and inadequate public resource to finance the public investment projects and growing dependence on foreign borrowing from its alliances or socialized countries. Therefore, new economic reforms, namely the New Economic Mechanism (NEM), was introduced in the second Five Year Plan (1986–1990) at the Fourth Party Congress of LPRP in November 1986. Under NEW, several economic reforms included trade and investment liberalization, agricultural reform, privatization, and liberalization of pricing and exchange rates. The purpose of NEW was generally economic growth and sustainable development (Than & Tan, 1997) and specifically to (1) reform the macroeconomic policies ensuring a smooth transition from a centrally planned to a market-oriented economy, (2) improve the efficiency of the public sector, (3) accelerate socio-economic development and improve living standard by expanding economic and social infrastructure including health and education, and (4) halt the degradation of the natural resource base by developing better approaches to tapping natural resources in the long run (Saignasith, 1997). Consequently, Lao economic development was more exposed to external factors such as inflow of foreign direct investment (FDI), an increase of trade, and external shocks such as the Asian Financial Crisis (AFC). As a result, the economy faced slight setbacks during the AFC in 1997 and 1998, resulting in a lower economic growth of 4.2%, hyperinflation (128.4% in 1998), and high depreciation of local currency (161.7% in 1998). Before the 2000s, Lao economic development was largely characterized by agriculture, food processing industry (rice milling, beer, and soft drink production, etc.), garment industry, cigarette production, and wood processing (Domoto, 2002), which more than two-thirds of Lao population was intensely dependent on.

However, after the 2000s, the expansion of Lao economic growth was predominantly driven by the natural resource sector. The resource sector

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had been at the forefront of production, investment, and exports but not employment. The sector mainly consisted of mining and hydropower electricity. In terms of production, resource industries are among the fastest sectors driving the Lao PDR's economic growth since the early 2000s, leading to a change of economic structure towards a resource-based economy. For instance, the share of the resource sector to GDP increased from 4.3% (1998–2000) to 14% (2006–2010) to 11.4% (2013–2015). They also bagged more than 60% of total exports where the main foreign markets were Thailand and China. Major investments in resource sectors were mostly from foreign investors such as China, Thailand, Australia, and Vietnam. In 2019, in the case of the electricity generation industry, there were 63 power plants in operation, in which 55 power plants were based on hydropower, one on coal power, five on solar power, and two on bio-fossil power, respectively (Ministry of Energy and Mines, 2019). More power plants, mainly hydropower plants along the Mekong river and its branches are expected in the next five years since many proposed project investments have already been approved by the government. Hereon, the resource industry, especially hydro-electricity, is likely to play a strong part in the economy.

Furthermore, since the 2000s, the trend of economic diversification in the Lao PDR is sometimes regressive as the resource industry demonstrates, especially mining and electricity. The resource sector is outstanding in the areas of investment and exports as it accounts for more than half of the total approved investment and export values. In contrast, this sector contributes less than 1% of total employment (Sayavong, 2017). In the meantime, non-resource manufacturing such as garments and coffee gains a small proportion of the value in the global value chain while the majority of the service and agriculture sectors are engaged mainly in small scale operations. This conclusion remains in line with previous studies. ADB (2017), for instance, illustrates that the Lao economy comprises mainly low value-added products with little prospects for enhancing structural transformation. Therefore, the Economic Complexity Index Level of the Lao PDR, as one of the important indicators, has had a declining value at -1.18 annually during 2013–18 (Observatory of Economic Complexity, 2018). The declining value demonstrates that its export basket has continually comprised rudimentary products. This suggests that it still has insufficient structural transformation for production and lower export competitiveness, as well as low value-added products for export. In other words, it has limited capabilities due to limited value-added manufacturing and export diversification. Sayavong (2015)<sup>1</sup> reveals that the Lao PDR achieved only 48% of its export potential. This means

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<sup>1</sup> The study applies Stochastic Frontier Gravity Model and panel data.

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that nearly half of the export potential is considered export loss, primarily attributed to implicit behind-the-border constraints such as poor domestic trade facilities, weak infrastructure, and the limited technological capacity of exporters. Unlike Laos, the Economic Complexity Index of China, Malaysia, and Thailand has been on the uptrend representing more complexity in their export diversity and high value-added products.

According to the World Bank (2020a), the time and costs for documentary compliance to export in Laos are high—it takes 60 hours or 2.5 days and UD\$235 in processing fees respectively when compared to the average in the Asia Pacific region (55.6 hours or less than 3 days and US\$109.4). In particular, exporting to the European and Japanese markets, which have more stringent guidelines, is time-consuming as more documentation is needed for exports. The country's low levels of exports also show that it lacks supply chains connected to the international economy, which are comparable to Thailand or Vietnam. This is in line with Haddad et al. (2006) and Record and Nghardsaysone (2010), whose studies have identified some implicit behind-the-border constraints in Laos such as weak institutions, poor infrastructure (including customs and border procedures), and the rudimentary level of technological capacities in many firms. The Non-Tariff measures are still prevalent as Sitthideth (2019) shows that Laos has more than 500 Non-Tariff Measures (NTM) imposed on more than 7,300 trade items restricted by 13 agencies in 2018.

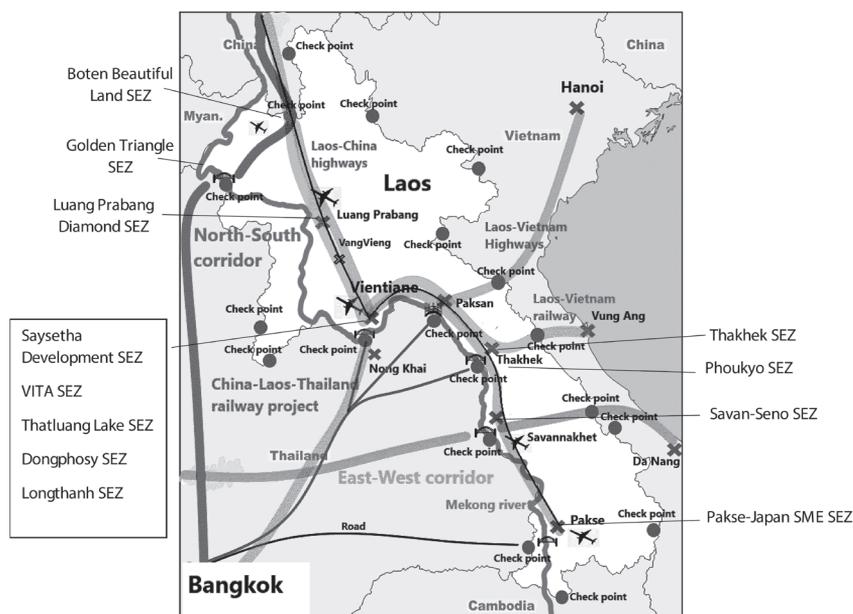
### III. INFRASTRUCTURE

Infrastructure development is crucial for economic development and trade for Laos and other countries in the region. Thus, investment in infrastructure development has been one of the government's priorities in promoting national development over several decades, with a special focus on expanding the road network for its population to access public services and markets domestically and regionally. As the Lao PDR is a landlocked country in ASEAN, connectivity to regional and international markets is necessary for the expansion of the country's economic development. Hence, the government has set a target to transform the Lao PDR from a land-locked country to a land-linked country as a logistics hub for the region by 2020 as outlined in the Infrastructure Master Plan. The aim is to facilitate the expansion of economic corridors or industrial areas or Special Economic Zones (SEZs) through rail and road transport connections. Hara (2002) and Domoto (2002) assert the location of Laos as a "land-bridge", importantly for transportation in the Indochina Peninsula, Mekong region, and between Southeast Asia and the Chinese and East Asian economies. If so, the development of transportation in the Lao section is significantly important for connectivity

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in the region. The major existing and planned transport networks in Laos, especially railways, are mapped in Figure 1. Each transport network is briefly discussed in detail afterward.

**FIGURE 1. MAP OF THE MAJOR TRANSPORT NETWORK AND SPECIAL ECONOMIC ZONES (SEZs) IN LAOS**



**SOURCE:** Created by the author. Note that  is under construction

Overall, road network development, as the most important transport to facilitate transportation for passengers and commercial businesses, is assessed as on track for progress but still poor in quality compared to other countries in ASEAN. Therefore, the current capacity of transport infrastructure in Laos is still unable to accommodate the medium-large scale industrialization. Only 15.4% of all road networks in Laos are paved, for instance, much lower than other ASEAN countries (ASEAN Secretariat, 2019). This circumstance makes it difficult to transport people and goods, especially during the rainy season. In ASEAN, nevertheless, the road conditions in the Lao PDR are slightly better than only Cambodia and the Philippines but similar to Vietnam (World Economic Forum, 2018b). Laos lags far behind Thailand as well as Malaysia. As a result, Special Economic Zones (SEZs) or industrial zones, regarded as strategic locations for attracting medium-large scale manufacturing industries, are mostly located near borders where well-connected infrastructure with neighboring countries is already in-use. The future seems to be bright for road transport infrastructure because a few

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construction projects for the expressway project from Vientiane to Vang Vieng (one of the most favorite tourist destinations in Laos) (113.5 km) and the Vientiane to Pakse (Southern city) highway project (approximately 491 km) are in the pipeline to connect major cities thus adding to the prospective development of road networks. While water transport might not seem important due to various limitations, the development of air transport is still considered to be in the early stages with a high potential to impact tourism rather than merchandise. Because of the limitations of water transportation, the construction of bridges on the Mekong River at the border was conducted to enhance road connectivity. Currently, there are four bridges in operation and one under construction as shown in Figure 1. Of these, five bridges are directly connected to neighboring countries. Most of them are new and are a part of the sub-regional strategic economic corridors, namely, the North-South Corridor (strengthening the trade between China and Thailand) and the East-West corridor (increasing the trade between Thailand and Vietnam).

Nowadays, railway development is lagging behind other countries. Currently, the only rail infrastructure in use is a 3.5-km extension from Thailand running from Nong Khai City across the Friendship Bridge to Thanaleng Railway Station, 20 km to the east of Vientiane. However, the Laos-China railway project under the Belt and Road Initiative (BRI) cooperation between Laos and China is under construction since late 2016 and expected to be finished by 2022. It will boost the trade and real estate as well as tourism sectors. The proposal for the Vung Ang-Vientiane railway project is another initiative between Laos and Vietnam that should also be taken into account. In this regard, it is an opportunity for Lao PDR to develop the railway network further, wherever it can, to connect domestic manufacturing industries especially small and medium enterprises (SMEs) to the major industrial hubs or SEZs and regional and global economies. The development of road and rail transportation will enable the Lao PDR to substantially transform its position from a land-locked to land-linked or land-bridge economy though this will require a huge amount of investment and time-consuming. More importantly, it will improve the competitiveness of the Lao economy radically as a result. Logistics services are currently one of the areas of most concern because they constrain the competitiveness of the Lao economy in regional and global markets. Despite progressive development, Lao logistics services are still costly and poorly managed compared to other countries in ASEAN. Therefore, logistics should be receiving a lot more attention during the period of economic transition especially in the areas of customs, logistics quality, and competence (World Bank, 2018). This is because the cross-border and truck services in the Lao PDR cost almost half of the total shipping costs to destinations outside of Southeast Asia. The shipping costs from Vientiane to

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Yokohama (Japan), for instance, as per a case study in 2014 and 2015 are at the highest level in the Asian region. Institute of Developing Economies (2017) reveals that the land transport costs from Vientiane to Nong Khai (a distance of 18 km) were US\$1,000 per container constituting 40% of the total shipping cost to Yokohama. Meanwhile, the transport costs from Nong Khai at the border to Laem Chabang Port in Bangkok (a distance of 718.9 km) was only US\$700 and the shipping cost from the port to Yokoyama (a distance of 4,599 km) was UD\$800. Such high transport costs from Vientiane to Nong Khai are mainly attributed to the high cost of truck services and cross-border processing at customs.

Table 3 summarizes the assessment of key infrastructures such as road, water, logistics, and human capital for economic development in Laos. Generally, the trend of Lao infrastructure capacities in science and technology, infrastructure, and human capital, has improved over time especially during the last decade. However, most of this lags well behind other ASEAN countries and some landlocked countries in Asia. In particular, infrastructure indicators such as airports, railways, logistics, human capital, and technological readiness need to be improved urgently to catch up with the levels of other countries in ASEAN. Given the limited resources, priority areas should be selected. After considering the current most problematic factors for doing business (World Economic Forum, 2018a), it is suggested that addressing the inadequately educated workforce or human capital should be the priority; the second is transport infrastructure, especially logistics and rail transport followed by technological readiness. Henckel and McKibbin (2017, 5) assert that transport and telecommunication infrastructure provide high spillovers for land-locked countries undergoing regional integration. This result could also apply to land-locked Laos.

**TABLE 3. ASSESSMENT OF KEY INFRASTRUCTURE**

NO	INDICATOR	ASSESSMENT		
		WEAK	MODEST	STRONG
1	Road Transport		✓	
2	Water Transport	✓		
3	Air Transport	✓		
4	Railway Transport	✓		
5	Logistics Services	✓		
6	Human Capital	✓		
7	Technological Readiness	✓		
8	Innovation		✓	
9	Energy			✓

**SOURCE:** Sayavong, 2018



#### IV. INTERNATIONAL RELATIONS

During the first two years after independence in 1975, the Lao government established diplomatic relations with more than 50 countries and cooperated with several international organizations such as the United Nations (Ministry of Planning and Investment, 2015). The foreign relations have since substantially expanded to 140 countries all over the world (Ministry of Foreign Affairs, 2017). Moreover, there are 23 foreign embassies located in Laos including from China, South Korea, Japan, and all nine ASEAN countries. This reflects the expansion of foreign policy of the Lao government in the region and beyond which is considered one of the behind-the-scene drivers for economic development and economic reforms towards the market-oriented economy from the central planning economic system as indicated in the NEM in 1986. The inflow of foreign direct investment (FDI) and Official Development Assistance (ODA) has increased as well as the escalation of trade as a consequence.

In previous years, the relationships between Laos and its alliances or socialist countries, particularly China, have expanded with higher frequencies of meetings and exchanges between their leaders since the announcement of the Belt and Road Initiative (BRI) by the Chinese president in 2013. The cooperation between Lao PDR and China has been demonstrated since the end of 2016 when the government of Lao PDR signed the Memorandum of Understanding (MOU) and other 20 documents with China on cooperation in various areas supporting the One Belt One Road initiative (Sayavong, 2019a). For instance, the Master Plan of the cooperation on developing the “One Belt One Road” between Laos and China was signed during the first Belt and Road Forum for International Cooperation in May 2017 in China. The master plan has identified seven prioritized areas of cooperation namely (1) infrastructure, (2) agriculture, (3) capacity building, (4) industrial park, (5) culture and tourism, (6) finance and banking, and (7) production promotion. In November of the same year, Chinese President Xi Jinping formally visited the Lao PDR where two governments reaffirmed their cooperation on the China-proposed BRI. For the Lao government, BRI is considered a strategy to overcome its disadvantage of geographic location by turning itself from a “land-locked” country to a “land-linked” one. The construction project of the Laos-China railway from 2016 to 2021 with the total investment of US\$5.9 billion or 35% of GDP in 2018 is, particularly, the top priority for the BRI cooperation between the two countries. This is because the Laos-China railway route is the main section for BRI cooperation in the Southeast Asian region or the Singapore-Kunming High-Speed Rail Link known as Pan-Asia Railway Network. That is why the construction of the railway in Lao PDR has started despite the construction of other parts in

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Thailand and Malaysia being still under negotiation. In April 2019, fortunately, China, Lao PDR, and Thailand signed the memorandum of cooperation on a railway-bridge to connect Thailand's Nong Khai at the border to Vientiane in Lao PDR which is a further step towards the Singapore-Kunming High-Speed Rail Link. Finally, a series of cooperation documents in various fields such as the economic corridor, digital Silk Road, electricity, science, and technology emerged. In the most recent second international Belt and Road forum held in Beijing during 25–27<sup>th</sup> April 2019, where the president of Lao PDR again participated, the policy cooperation between two countries has been pushed one step further by signing more documents for bilateral cooperation, especially the Laos-China economic corridor cooperation framework (LCEC). Nevertheless, there are opportunities and challenges for BRI cooperation for Lao PDR. The opportunities are mainly attached to the economic benefits, whereas the challenges are the social and environmental impact, particularly, from the large investment projects such as railway, expressway, and real estate development. Other challenges include transparency, accountability, and efficiency since the domestic capacity of both public and private sectors is still weak (Sayavong, 2019b).

The relationship with other individual countries is likely to be normal although there are some conflicts and uncertainties with a few countries such as Cambodia, Thailand, and the USA on the issues of border and human rights. In recent years, for instance, Laos and Cambodia had a border conflict in early August 2017 when the two leaders had an urgent agreement for conflict resolution at the meeting held in Vientiane on 12<sup>th</sup> August 2017 to withdraw their troops from the conflict areas (Xinhua, 2017). The incidence of border conflict occurred before the national election in Cambodia was held in July 2018; therefore, it is believed that this border conflict is unusual as it is likely to be a tool for domestic politics in Cambodia (Kang, 2018). The issue of the border conflicts with its neighbors, including Thailand, likely matters in the future because more than 10 spots in the border areas are still under negotiation for marker installation.

Numerous events of multilateral cooperation during the last three decades have advocated the efforts of Laos to integrate into the regional and global community. Joining the ASEAN community in 1997 implies that the purpose of Lao foreign policy is to contribute to the building of peace, stability, and cooperation for development in ASEAN (Ministry of Planning and Investment, 2015). In November 2004, Laos holding the 10<sup>th</sup> ASEAN summit in the capital, Vientiane, with the theme of “Advancing a Secure and Dynamic ASEAN Family through Greater Solidarity, Economic Integration and Social Progress” is another example for the same. The successful outcome at this submit was that all members agreed on the acceptance of the



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Vientiane Action Plan as A Vehicle to Building an ASEAN Community through realizing comprehensive integration. These hosting events in Laos have gradually accelerated the role of Laos in foreign affairs.

The multilateral cooperation, besides the bilateral cooperation, is one of the key factors for the integration of Laos into the global community. The cooperation in the Great Mekong Sub-region (GMS), ASEAN, and WTO was crucial for the success of Lao economic growth in previous years by attracting Foreign Direct Investment (FDI) and Official Development Assistance (ODA) and boosting trade. Therefore, it is worthwhile to have a brief discussion on this cooperation.

### MULTILATERAL COOPERATION

Laos is located in the Great Mekong Sub-region (GMS) specifically and generally located in the Southeast Asia region. It is to be noted that there are six countries in the GMS including Cambodia, Laos, Myanmar, Thailand, Vietnam, and Yunan province in China. As a result, Laos has been strongly and actively participating in regional cooperation programs including GMS, ASEAN, Asia Pacific Trade Agreements, Cambodia-Laos-Vietnam Development Triangle, and Ayeyawady-Chao Phraya-Mekong Economic Cooperation Strategy (ACMECS). For the Great Mekong Sub-region (GMS) cooperation program, for example, Laos joined this sub-regional cooperation that is strongly supported by the Asia Development Bank (ADB) in 1992. This program aims to stimulate economic cooperation in the Sub-Mekong region emphasizing infrastructure and trade facilitation. Since then, the economic corridors such as North-South and East-West economic corridors have been developed (see Figure 1). Laos was accepted as a full member of ASEAN on 23<sup>rd</sup> July 1997 and joined the ASEAN Free Trade Area (AFTA) in 1998 in which all members have to gradually remove tariffs under the Common Effective Preferential Tariff (CEPT) scheme through a timeframe commitment by 2015. After joining ASEAN, the growth of the Lao economy was at 6.32% annually during 2001–2005 which is higher than the growth of 4.8% annually from 1986–1996 (Ministry of Planning and Investment, 2015). In February 2013, Laos gained official membership in WTO after 15 years of negotiation initiated by the Ministry of Industry and Commerce (MOIC). As a result of the expansion of Lao foreign relations, the flows of FDI, trade, and Official Development Assistance (ODA) in Laos have significantly increased as a consequence, which is presented below.

### FOREIGN DIRECT INVESTMENT (FDI)

The Lao government has an open foreign policy to attract foreign investments into Laos since 1988 through the use of its rich natural resources,

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political stability, investment policy incentives, cheap labor, and the trade preferences granted by developed countries. As a result, foreign private investment has shown an increasing influx into Laos. From 1989 till 2019, there were more than 3,079 investment projects or US\$ 23.3 billion by FDI and joint-ventures from 52 countries (Ministry of Planning and Investment, 2020). Major foreign investors were mostly from neighboring countries while the investment from Europe and America was limited. Top 10 foreign investors are from China, Thailand, Vietnam, Korea, France, Japan, Netherland, Norway, and England. The most popular areas for FDI interest included the energy sector or power generation, mining, service, agriculture, industry, and handicraft, respectively. In recent years, the investment in infrastructure, especially the Lao-China railway construction project and special economic zones (SEZs), is outstanding. In 2019, there were 12 SEZs in the Lao PDR, and 810 firms are currently operating in the zones including 682 foreign companies, 86 domestic companies, and 41 joint venture companies (Promotion and Management Office of SEZs, 2020). The Lao government highly expected a large contribution from FDI for Lao economic development especially poverty reduction, tax collection, and the creation of employment, technological transfer, human resource development, and the outreach of development in the rural areas. However, the contribution of FDI is less than expected as most of the investment projects are in the well-established infrastructure located in large cities at the border. Therefore, the development gap between border and urban cities and rural regions or hinterland areas is large. Second, many investors investing in the labor-intensive industries, such as primary garment or Cut-make-Trim (CMT), provide limited technological transfer as well as human development for local labor and manufacturers. Thirdly, major investments are concentrated in the natural resource sector, particularly, hydropower generation and mining. This resource sector provides a limited number of employees with limited backward-forward linkage to domestic industries and is easily exposed to price uncertainties in the global commodity market. However, in recent years, the uncertainties of Thai politics and supply chain disruption in China due to the spread of COVID-19 in 2020 has created the strategy of Thailand plus one and China plus one by Japanese firms, which would likely benefit other ASEAN developing countries including Laos through relocation of Japanese production-base factories. Therefore, Japanese manufacturing industries are expected to generate a higher profile in the Lao manufacturing sector in the future.

### EXTERNAL TRADE

After joining ASEAN and engaging in other multilateral trade agreements such as the Generalized System of Preference scheme (GSP), the Lao PDR's

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exports grew at an average annually of 18.1% during 1996–2019 (World Bank, 2020b). In particular, the exports surged after 2005 due to the onset of gold and copper production from two large mining companies, namely Lanexang Minerals and Phou Bia Mining Ltd. The total export value more than tripled from US\$0.3 billion in 1995 to US\$5.7 billion in 2019. This growth was driven by mining, electricity, garments, and agricultural products. These sectors are a dominant portion of total exports. During 2011–2019, the share of mining and electricity in exports was more than half (63.4%). Meanwhile, the combined proportion of agriculture and garments was 16% of total exports. Based on market share in 2018, China and Thailand dominated the distribution of total trade. This figure stood at 71.4%. Figures for trade with Vietnam, Japan, the United States, India, and other trading partners stood at 17.2%, 1.7%, 0.5%, 2.5%, and 6.6% respectively. Although exports overall have performed well and trade liberalization has also been progressive over the last two decades concerning the dismantling of tariff<sup>2</sup> and non-tariff barriers through trade agreements, the export structure is more intensified in a few export items (electricity and mining) and a few markets such as China, Thailand, and Vietnam. This demonstrates that the external income of Laos is extremely dependent on its neighboring countries. As a result, Laos would face economic difficulties in the case of foreign affairs or political conflict with its neighbors, especially Thailand and Cambodia who have a different political system.

### OFFICIAL DEVELOPMENT ASSISTANCE (ODA)

From the time after independence until 1990, socialist countries such as the Soviet Union, China, Vietnam, North Korea, and Cuba were major donors of ODA for Laos. The ODA took made up more than 60% of total public investment (Ministry of Planning and Investment, 2015). During this period, the international relation of Laos was limited and the economy was heavily destructed by the Indochina War. Therefore, the Lao government was extremely dependent on its alliances for survival, recovery, security, and development. Later on, when the economic reforms under NEW were gradually implemented, the relations with socialist countries, especially Vietnam and China, dramatically expanded in several areas such as investment under the market-driven incentive or mutual benefits rather than subsidies. Besides, the relations with countries and international agencies in the region had escalated in numbers as well including Japan, Australia, Germany, France, Spain, Denmark, Norway, Netherland, South Korea, Belgium, Luxemburg, Thailand, United Nations Development Programme (UNDP) and agencies

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<sup>2</sup> In 2018, the overall trade tariff is 5 percent, according to WTO-Trade Policy Review. The source of information is from <https://beltandroad.hktdc.com/en/country-profiles/laos>.

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under UN administration, ADB, World Bank, European Union, and other non-government organizations (NGOs). As a result, the value of ODA in Laos increased steadily from US\$109 million in 1991 to US\$565.1 million in 2018 (World Bank, 2020b). China, World Bank, ADB, South Korea, and Japan are currently the major ODA donors. The technical assistance and training scholarships for the short and long term were also granted to Laos due to the expansion of foreign relations. ODA is currently used in line with the socio-economic development of the government. The roundtable meeting between the Lao government and its development partners held annually, and is the current mechanism to match the use of ODA from development donors to the socio-economic development plan of the Lao government (Ministry of Planning and Investment, 2015).

### V. LONG-TERM NATIONAL DEVELOPMENT STRATEGIES AND PLANS

The national policy and strategy of the Lao government are designed to reflect the updated situation of Lao economic development regarding the change of regional and international environment. So far, the 2030 Vision and 10-Year Socio-Economic Development Strategy during 2016–2025 published in early 2016 serves as the top policy framework for the Lao government to guide other national and sectoral policies or short-term policies such as 1-Year and 5-Year National Socio-Economic Development Plan (NSEDP) until the year of 2030. Note that the sectoral policy refers to the strategic line of the ministries such as the ministry of agriculture, ministry of finance, etc. Table 4 summarizes the main contents of the 2030 Vision and 10-Year Socio-Economic Development Strategy 2016–2025. It clearly shows that the vision of Laos is reflected in the condition of international development and issues related to foreign affairs by aiming specifically to upgrade its level of income from a lower middle-income country (current status) to an upper-middle-income country by 2030. Its neighboring countries have a similar long-term vision and strategy. Thailand, for instance, has a long term vision (20 years National Strategy 2017–2037) to become a developed country by 2037 (National Strategy Secretariat Office, n.d.). Likewise, the Cambodian government has set up a target or vision to reach an upper-middle income country by 2030 and a high-income country by 2050 (Royal Government of Cambodia, 2018). For Lao PDR, to reach the vision 2030, seven strategies were identified by the Lao government where the top three strategies are (1) sustainable and green economy, (2) achievement of the criteria for graduation from least developed countries by 2020 and implementing SDGs, and (3) human resource development. Later on, to reflect the realization of the strategies, the final draft of the National Green Growth Strategy came out in 2019 as a crucial platform to guide any policies and action plans toward the

priority of sustainable green economy. Also, the final draft of the National Human Resource Development Strategy as policy guidance has been completed mid-2016. Therefore, it is not surprising for Laos to have a similar long term vision as its neighbors in the 21<sup>st</sup> century specifically to become a high-income country. Nevertheless, the economic development of Laos should be ensured in the direction of green and sustainable growth.

**TABLE 4. 2030 VISION AND 10-YEAR SOCIO-ECONOMIC DEVELOPMENT STRATEGY (2016-2025)**

**VISION FOR 2030:**

- Lao PDR becomes an upper middle income developing country following a knowledge-based, green and sustainable socio-economic direction.

**SEVEN PRIORITIES OF THE 10 YEAR STRATEGY (2016-2025):**

1. Strategy for continued economic development in high quality, balanced, sustainable and green direction
2. Strategy for meeting the criteria for graduation from the Least Developed Countries by 2020 and implementation of the SDGs.
3. Strategy for human resource development
4. Strategy for sustainable, efficient and green-directed protection and use of natural resources
5. Strategy for improving the enforcement of the rule of law
6. Strategy for regional and international integration and connectivity
7. Strategy for industrialization and modernization

**SOURCE:** Author's summary based on Ministry of Planning and Investment (MPI), 2016a, 2016b

A task for the Lao PDR in the future or 21<sup>st</sup> century is to generate a higher income for its people in a green and sustainable manner. This requires it to diversify its current economic structure from a resource-based economy to a non-resource dependent economy or to more inclusive growth that can integrate into the regional and global supply chains. To this end, strengthening its infrastructure capabilities such as human resource, transport, logistics, and regional cooperation should be the dedicated area to ease as well as attract private investment for higher value-added products or high technology industries that create high skilled employment. This also requires cooperation from countries in the region, especially ASEAN, to be more diversified and competitive in the regional and global markets along with its neighbors. Some of human capital and infrastructure capabilities are discussed as follows.

Human capital, as an example, in Lao PDR, is relatively low in its current position compared to other countries in the region, putting the country at a shortage of skilled workforce, and as a result, the economy has been trapped in the vicious cycle of low quality, low value-added, and low skills and low wages which affect the competitiveness of the region. Despite the domestic demand for labor remaining unmet, a large number of unskilled workers migrate out of the country to seek jobs overseas, and especially neighboring countries such as Thailand. To support economic development in the direc-

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tion of industrialization and modernization, it is, therefore, required to build human capital, especially a skilled workforce with the self-discipline to unlock the door to modernization in the era of global integration and advancement of information technologies. The enhancement of human resources in Laos is expected to raise the level of competitiveness of the ASEAN region as a production hub in the world. According to LSB (2018), the share of the working-age population in Laos is anticipated to get slightly higher to 69.7% of the total population by 2045, increased from 62.2% in 2015. This implies an opportunity for Laos to benefit from the demographic change to support economic growth and sustainable development. However, this is conditional to long-term human development in the country that should be one of the top priorities since more than 60 percent of its labor in all industries in Laos have low education levels up to primary and secondary school (Lao Statistics Bureau, 2015b). The successful stories of Singapore and Thailand could serve as a lesson and this requires stronger cooperation from ASEAN members.

Besides, the development of transport infrastructure in Laos is critical for the competitiveness of the region since Laos is located in a strategic position in the region for regional integration. The transport section in Laos should be one of the main focuses of ASEAN. Typically, the transport network in Laos should be standardized comparable to its peers in ASEAN in a green and sustainable direction. The inadequate supply of infrastructure is among the top five most crucial major constraints in Laos as per business opinion (World Economic Forum, 2018a). More importantly, the position of the Lao business climate has generally lagged far behind the other developing countries in ASEAN except for Myanmar (World Bank, 2020a). This is because several developing countries made a significant improvement in facilitating their business climates in the same period, which as a consequence led to a drop in ranking for doing business in the Lao PDR. Vietnam, for instance, has improved its ease of doing business ranking by 12 places shifting to 70<sup>th</sup> among 190 countries from a previous ranking of 82<sup>nd</sup> in 2016.

For international relations, the most important principle for Laos is to be strict with the principle of peace, independence, friendship, and cooperation to strengthen the competitiveness of the region while limiting the conflicts, as much as possible, from the border disputes and political uncertainties in neighboring countries through diplomatic solutions. Practically, it is important to deepen the existing cooperation framework to maximize the mutual benefits while searching for new areas of deep cooperation with its partners especially Vietnam, China, and ASEAN to enhance the competitiveness of the region. This requires more contribution from ASEAN in terms of collective ODA. Improving the capacity of Lao embassies in foreign countries will help to maximize the potential investment, trade, politics, and cooperation



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between Laos and its partners while protecting its people, residing as well as working in foreign countries.

### VI. CONCLUSION

Since Laos is located in ASEAN as one of the most dynamic regions in terms of population, economy, and politics, a major question in the future for Laos is how to contribute to the sustainable development of the region. Some cooperation areas such as infrastructure and energy (hydropower electricity) connectivity can currently be recognized. The typical examples are the railway and high-way constructions in the economic corridors expected to connect the countries in the regions from North to South and East to West. However, this cooperation is still in the early stage. There are concerns about transparency, accountability, and the impact on local economies, inequality, environment, and society. The cooperation in human resource and transportation including logistics is the area of utmost importance for sustainable development in the region. The success of such sustainable development is, of course, without the political will from countries in the region or the support of the regional community. Though the cooperation among ASEAN is shown to be well-established in previous years, there is still an implementation gap in several areas as a large gap in development among members such as HDI, competitiveness index, ease of doing business ranking, etc., still exist. Reducing such gaps among ASEAN members should be taken seriously which requires a stronger contribution from each member of ASEAN.

For Laos, the long term development goal by 2030 or beyond, is to raise the income of people higher to be comparable to its peers by diversifying its economy to move from a resource and traditional based economy to non-resource based economy under the scenario of inclusive growth or sustainable development as the main focus. To this end, raising the degree of its economic diversification and advancing infrastructure capabilities including the use of digitalized technologies are needed to attract private investment, boost trade, and create skilled laborers. Besides, the expansion of economic cooperation and foreign relations for Laos is needed to drive the economic complexity while external uncertainties such as trade conflicts between the US and China, pandemics, climate change, political uncertainties in neighboring countries, and border disputes (land or sea) should be minimized as much as possible.

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