



**EXECUTIVE FORUM ON
NATIONAL EXPORT STRATEGIES**

**EXPORT OF SERVICES: HYPE OF HIGH POTENTIAL?
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**5-8 October 2005
Montreux, Switzerland**

**Developing Private Sector Services with the help of National
Chambers and Industry and Business Organisations in Laos**

**A paper contributed by
Oudet Souvannavong
President
Lao Hotel and Restaurant Association
Laos**

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Introduction

After decades of wars and central planning leading to destruction, poverty and isolation, Lao PDR started to rebuild its nation and economy in the 1980's. Since the introduction of the "New Economic Mechanism" in 1986, Lao PDR is making a fundamental political, social and economic transition abandoning the Soviet model of central planning for a way of socialist market orientation. The economic crisis that affected the fast growing countries of East and South-East Asia in 1997-98 confirmed the risk of letting loose market forces, without appropriate political and institutional frameworks. It was only during the 1990's that the economic changes have been put into place and the economy grew up quickly. Lao PDR adhered to the Association of South East Asia Nations (ASEAN) in 1987 and is in the process of trade liberalization under the ASEAN Free Trade Area since 1997. The implementation of the new economic reforms with the promotion of private and foreign direct investment and the privatization of state-owned enterprises has quickly enabled the private sector. Since the late 1990's, the private sector is growing fast and plays an ever-increasing role in the economy. However, the business environment in Lao PDR is not yet favourable. The creation and growth of private enterprises, especially SMEs, is obstructed by complicated business registration, licensing, and inspection procedures; by the limited access to financial and banking services; and by the lack of human resources. In addition, a complicated and unreliable tax system and the dominance of business monopolies and cartels, result in unfair competition.

The Lao National Chamber of Commerce and Industry (LNCCI) formed in 1989 as a part of the Ministry of Commerce with the responsibility to maintain the link between local industries and various government agencies with a view to expanding trade and investment. At the beginning of the new millennium, the role and function of LNCCI shifted from a public agency to an independent association. Following its new status, LNCCI is moving toward the promotion of the private sector through the facilitation of business forums, organizing training, organizing trade mission and networking with other National CCI in the world and especially within the ASEAN. The business organizations also moved faster to be the engine and mastermind in the growth of their specific industry by providing professional services to their members in trade negotiations, vocational training and skill development, promotion and marketing, and in consulting and advocacy. The effort made by LNCCI and the Business Organizations is consolidated by the success on the negotiation on Normal Trade Relation with the USA in 2005, which will facilitate the accession to WTO. LNCCI and the Lao Business Organizations are definitely the pillars for private sector growth but persisting unfavourable business environment in Lao PDR, the impact of regional economies moving faster, and the increased price of crude oil are challenging such development.

The Lao Economy

The Lao PDR is a land locked country in South East Asia surrounded by the People Republic of China and Myanmar to the North, Thailand to the West, Vietnam to the East and Cambodia to the South. The country has a large area of 236,800 sq. km, a population of 5.2 million habitants and a very low population density of 25 persons per square kilometre. The country is mountainous in the North and the East and has in the West a number of plains along the Mekong River. The Mekong River and its tributaries are the main water resources with provide abundant natural resources with high socio-economic development potential in agriculture, forestry, fisheries, hydropower, and mining. Adding up to those resources, ethnic diversity and ancient Lao cultural heritage has put Laos as a well-known tourist destination. Despite the gifted natural and cultural resources, Laos is one of the least developed countries in the world. Its mountainous terrain, remote settlements, low population density, widespread poverty affecting 39% of the population, underdeveloped physical infrastructure and human resources, the largely non-monetized economy, and undeveloped public administration and governance frameworks resulted in institutional and regulatory deficiencies that are posing problems and challenges to development.

Since the introduction of the New Economic Mechanism, the economy grew by an average of 6.2% from 1990 to 1999 and of 5.5% from 2000 to 2005. GNP per capita increased to 320 US\$ in 2003 from 114 US\$ in 1985. Lao PDR remains one of the least developed countries in the world with life expectancy at birth of 53.1 years, an adult literacy rate of 47.3% and a human development index of 0.476.

Since the reforms, the structure of the economy also changed with a decrease in agriculture and the increase in industry and service of the per capita ratio. Trade liberalization is one pillar of the economic reform and this has been accelerated when Laos as a member of ASEAN since 1987, agreed the ASEAN Free Trade Area (AFTA) in 1997. The desire of the Government is to develop the country's land-locked position to a land-linked one, leveraging on the market of the surrounding fast growing economies such as the People's Republic of China, Thailand and Vietnam by developing local competitiveness and enhancing the promotion of trade and services under bilateral exchanges, ASEAN economic schemes and projects and other regional development scheme such as the Greater Mekong Sub-region (GMS).

The Lao Private Sector and its Environment

The implementation of the new economic reforms brought changes in the roles of economic sectors. Price liberalization, land, agricultural, fiscal, trade, exchange rate, banking and financial sector, foreign investment and public enterprise reforms have enabled the private sector to increase its contribution to the economy by creating more incomes and employment. Since the early 1990's there has been a consistent and high rate of annual employment growth in the private sector growth of 10 to 15% per annum. The increased in manufacturing value added produced by the private sector, including private foreign direct investment has reached more than 4 times the manufacturing value added produced in state enterprises in the beginning of the century and about one third of the private manufacturing value added has been created by local private investors. In the service sector, private entrepreneurship rapidly evolved to occupy the majority of share in the economy and employment. However, the number of private business in Laos is small at 146,000 enterprises with 259,000 full-time equivalent persons employed in 1996 (MIH/GTZ), whereof most of the business or enterprises are classified as small and medium.

Private enterprises are important to the economy and are considered as the engine of growth in the National Growth and Poverty Eradication Strategy (NGPES). Nonetheless, they are facing some problems in realizing their full potential despite the on-going reforms. The general characteristics of environment surrounding private sector in Laos are:

- **Decentralization policy and process:** Since 1990 the Government is implementing a nation wide decentralization process and a significant amount of responsibility and authority is being devolved to provincial and lower levels. Provincial and lower level officials lack motivation, experience and skills in managing their added responsibilities and conducting their new tasks. Especially when dealing with the public and corporate governance issues and tax. Local auto-subsistence and protectionism policy in many provinces is impeding the free flow of products and commodities within the country and the development of new businesses.
- **Legislative process:** The legislative environment with the government organizing and regulating the business environment through laws, regulations and administrative practices shows little concern for stakeholders such as private entrepreneurs. Many regulations are not conducive to business and in many cases obstruct the free flow of raw materials and commodities and do not promote in-service training and private sector R&D.
- **Regulatory framework:** Private enterprises have to comply and are affected by many legislation and regulations. In general there is very little civil instruction and information about the legislation and regulation to the private enterprises so they are always found guilty and penalized for things they do not know.
- **Business registration and licensing:** Private enterprises creation and growth is encumbered by complicated and time consuming business registration so many businesses especially

the SMEs are not properly registered and operate in the non-formal market, thus creating unfair competition. The single door policy put into place by the government is only working in the capital city.

- Taxation: The tax system is complicated and allows for discretion in the case of small taxpayers. Value Added Tax is not yet applied, many companies have no proper accounting system so taxes are fixed and negotiable and not based on account statement. This also results in unfair competition.
- Trade regulation: The Government has imposed import ceilings (by value) on different inputs used by local producers to control trade deficit. Quotas and import ceilings for protection and management of trade balances increased the costs of doing business for the private enterprises. The use of tariffs and excise taxes is not been fully applied.
- Investment incentives: The Government has investment incentive to attract foreign direct investment. However, the broadness of investment description is engaging diverse interpretation at provincial levels and may be resulting in unfair competition for investors who have not applied for or are not able to pass through the investment promotion certification process.
- Access to finance: The formal banking system is monopolized by State Operating Commercial Banks (SOCB). Access to finance through the local banking system is hampered due to difficulties faced in repossession, sale of collateral and by the SOCB's large percentage of non-performing loans. Weakness in the banking system results in low level of available credit for the private enterprises.
- Supporting institutions and business organization: There are 18 formal business organizations established under the LNCCI in the capital city. However, the business organizations have an extremely low level of organization in the provinces. Many provincial business organizations are organized by the public agency governing the sectors or sub-sectors not by voluntary basis but for the public agencies to get "control" on the activities of the private enterprises. In example, the provincial hotel and restaurant groups organized under the provincial tourism authority have no marketing, promotional and training services.
- Information services: There are limited newsletters, television and radio program to provide information and services to the private enterprises. The internet is evolving in Laos with few internet providers and very few professional internet marketing domains to sell Lao products. Cost for communication and for the using the internet is high and not affordable for many SMEs.
- Training, consulting and consulting services: Formal and informal vocational training opportunities for the people are still very limited. Formal vocational education is provided by a number of public and private training providers. Public vocational and technical training suffers from the availability of recurrent budgets to conduct training, training material and equipment, and qualified teachers and trainers. The private enterprises need skilled workers in abundant quantities but the existing vocational education and training systems are not yet to produce workers with the technical and vocational level and skills needed by those enterprises. Few enterprises are organizing training of workers and staff at their own expenses but the training is not tax deduct able. In the hospitality industry, limited in service training is provided by hotels and restaurants because of the high staff turnover (40% per year).
- Public and private partnership: Under the LNCCI, a public and private dialogue is established with the organization of business forums. However, the dialogue between enterprises and the government has just evolved and is not well structured so problems and issues related to the private sector have been strongly addressed. Public and private sector activity in training and skill development is also evolving in 4 business organizations; The Textile and Garment Industry Association, the Lao Handicraft Association, the Lao Hotel and Restaurant Association, and the Lao Furniture Group.

The Lao National Chamber of Industry and Lao Business Organizations and their role in the development of trade and services

LNCCI was formed in 1989 as apart of the Ministry of Commerce with the responsibility to maintain the link between local industries and various Government Ministries and agencies with the views to expand trade and investment. Today LNCCI has 685 members representing a broad cross-section of public and private business enterprise in Laos. At the beginning of the new millennium the role and function of LNCCI shifted from a public agency to an independent association with its own Article of Association and its own budget recognized at national level. Following its new status, LNCCI is nationally representing Lao employers and is moving toward the promotion of the private sector through facilitation of business forums, organizing training, organizing trade mission and networking with other National CCI in the world and especially with the ASEAN CCI. LNCCI successfully organized the 2nd ASEAN Business and Investment Summit in November 2004.

LNCCI plays an important role in providing information to local and foreign investor to identify potential investment projects and partners and in coordinating meeting with concerned authorities and officials. Other important services provided to its members are: (i) Arranging textile export visas through the agreement with foreign embassies; (ii) Issuing Certificate of Origin (CO) for products manufactured in Lao PDR; (iii) Organizing arbitration firms that are seeking neutral institution to adjudicate insider-standing that arise in the course of conducting business; and (iv) Preparing and publishing membership directory and newsletters.

In the 1990's, LNCCI promoted the formation of business organizations in the form of business groups. Nonetheless, the establishment of the business groups was more or less a haddock initiative to control price, to regulate importation, and to control the conduct of public and private enterprises by rather than providing business support services. The primary business organizations established were; the Lao Textile and Garment Industry Association; the Lao Handicraft Association; the Lao Coffee Exportation Association; and the Lao Hotel and Restaurant Association; the Food Stuff and Consumer Goods Group; Lao Agricultural Products Processing Group; Lao Construction Material Group; and the Vehicle and Spare Parts Group. The business organizations moved fast to be the engine and mastermind in the growth of the private sector in their specific industry. They organized themselves as separated associations with the affiliation to LNCCI and other regional and worldwide business organizations. They engaged in trade negotiation and providing professional services to their members such as in vocational training and skill development, in promotion and marketing, and in consulting and advocacy. The effort made by the Textile and Garment Industry Association and other business organizations is rewarded by the success on the negotiation on GSP privileges with the EU, Canada and Japan and recently in on Normal Trade Relation (NTR) with the USA, which would facilitate the accession of Lao PDR to WTO.

The LNCCI and the Lao Business Organizations are definitely the pillars for private sector growth, but the persistently unfavourable business environment in Lao PDR, the impact of surrounding regional economies moving faster, especially China, and the increased price of crude oil are challenging such development. However, in comparison with other developing countries, LNCCI and its Business Organizations are not very well developed as judged by the limited range of services it provides and the magnitude of revenues its generates.

Trading of services in Laos: constraints and opportunities

Trading services

The Government recently removed provincial red tape and barriers to allow free flow of merchandize across the country that increased the number of small traders and potential for trade services in Laos. In relation to limited industrial development, potential trade service to support the importation in Laos are in:

- (i) food commodities;
- (ii) spare-parts, tools and machineries;
- (iii) car and vehicle;
- (iv) earth moving equipment and heavy machinery;
- (v) household equipment and furniture;
- (vi) professional laboratory equipment;
- (vii) construction materials;
- (viii) garment and textiles; and
- (ix) electronic, computer and telecom equipment.

A few brands have representative sales offices especially for car and vehicle. Because of its border link the majority of the commodity come from Thailand with an increasing number of low quality item from China. There are few trade service provided to local industries because most of the factories are organizing the importation of raw material and exportation of their products by themselves. The Food Stuff & Consumer Goods Groups is providing consulting and advocacy services to companies involved in the trade services.

Trading of locally made products such as handicrafts, furniture, agriculture and food-based products as well as construction materials is made by the producers themselves and by a number of small trading firms and shops. However, local merchandize is localized and good products are not being traded around the country. There are possibilities to enhance local production and trading by establishing “local commodity shops” in major cities and tourist destination, which sell selective quality products from all locations of the country. The local commodity shops could also be linked to other regional and global commodity shops created in the model of the “Chinese Emporium” or the “Asiana Shops” where Lao products could be displayed in supermarket chains and department stores in major Japanese, European and US cities in the future. The Lao Handicraft Association has a design centre, which provides art and design training as well as consulting, and advocacy to members.

Banking and Financial Services

Actually there are five state-owned commercial banks, five foreign bank representative branches, and three joint venture banks. Only the State Agriculture Promotion Bank has outlets up to the district level but it is operating more or less like a development bank. The Government has recently endorsed a new regulation to authorize private banking, credit cooperatives and the establishment of a stock market. The rapid economic growth, social spending and the increasing number of enterprises and labour force mean that there is a potential to develop banking services in Laos.

Transport services

Airline service is provided by a sole national carrier, Lao Airline, which has limited capacity to connect the different cities in Laos. Few international carriers are flying into the country and international flights are only available in the capital city and Luangprabang, a well-known tourist destination. This situation impeded travellers’ connectivity and the growth of tourist numbers. The Government is in the process of restructuring the national airline, seeking a joint venture with other international airlines, and is also willing to authorize landing rights to budget airlines in different tourist destinations and major cities. Most of land and river transportation is privatized as well as the majority of public transport. Potential transport services are evolving with the opening of new routes like the East-West Asia Corridors connecting Thailand and Southern China in the North and connecting Thailand and Vietnam in the South. During the last decade the Government constructed and rehabilitated a large number of national roads and tracks opening up new local market for transport services. Actually the number of private transportation providers

are increasing most of them are organized into local transport associations. The Transport and Shipping Groups under LNCCI is providing consulting and advocacy services to companies involved in the trade services.

Health services

Health services are provided by public hospital and health centres. Private health services are limited to medical clinics. There are also traditional medicine and Chinese health clinics. Of the latter, many are operated by foreign doctors. In the main cities located nearby the frontier, people are using health and medical services in Thailand. The Government has not yet authorized the establishment of private hospitals despite the potential to develop quality commercial health services in the major cities of Laos.

Hospitality and tourism services

Since 1990, the number of tourist arrivals increased with an average growth of 39%, but with the September 11 tragedy, the war in Iraq, and SARS, growth has been decreasing since 2001. However, the number of tourists increased by far from 14,400 arrivals in 1990 to 894,806 arrivals in 2004. The tourism sector actually accounts for a large share in GNP and is estimated to generate about 119 Million US\$ in revenue. The number of hotels has also tripled, from 307 institutions in 1998 to 957 institutions in 2004. World heritage sites, such as Luangprabang, Champassack Watphou and eco-tourism destinations became favourite tourist destinations as well as investment spots for the hospitality industry. The potential for tourism development is large in Lao PDR but investment in the hospitality industry is not well structured there are few quality hotels and too many low budget hotels and guesthouses. Few world brands are represented (Novotel, Belmont, Banian Tree and Pansea). Laos organized the 15th ASEAN Tourism Forum in February 2004 which further boosted tourism in Laos during the forum the Lao Hotel and Restaurant Association (LHRA) and the Lao Association of Travel Agent (LATA) joined the ASEAN Tourism Association (ASEANTA) and since then participated in the many forums and activities to increase regional tourism competitiveness and the intra-ASEAN travel. The LHRA provides established standards of competency, vocational training, marketing and promotion over the internet (www.laohotelgroup.com), which is linked to the world hotel link, and consulting and advocacy for its members. LATA provides consulting and advocacy to members and organizes joint promotion and marketing activities for its members.