

## Manufacturing Sector Brief

# LAO PDR



## COUNTRY OVERVIEW

Lao PDR is a landlocked country with a population of 7.1 million and a GDP per capita of USD 1,789 (2018). Lao PDR's average GDP growth rate has been 7.2% on average over the last 20 years. Its GDP growth rate is mainly driven by hydropower, mining and quarrying, wood, and agricultural products. Both the service and manufacturing sectors have been picking up pace in recent years in terms of their contribution to the economy and the manufacturing sector's role in the country's economic growth has also increased.

Lao PDR embarked on an economic reform in 1990s and became a member of the World Trade Organization (WTO) in 2013. According to ASEAN in Figures 2020, Lao PDR has a mixed economy with the main contributors to the GDP are agriculture (14%), industry (35.9%), and services (39.9%). The industrial sector comprises mining and quarrying, manufacturing, construction, electricity, gas, and water.

With the contribution of the manufacturing sector as part of the industrial sector is still small compared to its peers in the Mekong region (estimated around 7.64% of GDP in 2020) (GlobalEdge), Lao PDR continues to rely heavily on natural resources as a driver of the country's economic growth. The Mekong River runs through the country and approximately 85% of Lao PDR lies in the Mekong River Basin area. As such, it is endowed with significant natural resources explaining why its economy is still heavily dependent on capital-intensive natural resource exports derived from mining and hydropower.

**Table 1: GDP according to economic sector - Lao PDR (2019)**

● Economic Sector	● % GDP Composition (2019)
Agriculture	15.29
Services	42.65
Industry	23.43
Manufacturing	7.48

Source: GlobalEdge

About 80% of its population is employed in the agriculture sector, primarily small and subsistence farming, in comparison to only 1% employed in non-manufacturing industrial sector. Its exports are dominated by mineral products and electricity. Agriculture processing is considered a key industry in Lao PDR after mining and energy. Investing in Lao PDR is slow due to significant infrastructure gaps.

**Table 2: Percent GDP contribution by Industry Subsectors in Lao PDR**

● Subsectors	● 2017	● 2018	● 2019
Mining and quarrying	6.56	6.01	5.60
Food processing	1.48	1.43	1.50
Beverage and tobacco	1.31	1.27	1.30
Garment and footwear	1.16	1.15	1.10
Manufacturing (others)	3.54	3.60	3.70
Electric power	10.55	10.85	9.90
Water supply and wastewater	0.26	0.26	0.30
Construction	6.06	6.97	8.10
<b>TOTAL</b>	<b>30.92</b>	<b>31.54</b>	<b>31.50</b>

Extracted from Lao Statistics Bureau



# MANUFACTURING SECTOR OVERVIEW

Investment opportunities in the Lao PDR manufacturing sector may increase in the future as a result of the government measures to diversify its economy and to become less reliant on natural resource-intensive sectors. Investors may derive benefit from measures to:

- enhance enterprise competitiveness;
- create a business-friendly environment; and
- deepen economic integration.

Lao PDR aims to move up the added value through manufacturing and targeting high value markets (such as organic and fair-trade products). During the 2013-2017 period, the total value of manufacturing exports increased threefold from USD 270 million to USD 780 million. Key manufacturing subsectors of interest for expansion and investments in Lao PDR are organic and fair-trade products.

Lao PDR created Special Economic Zones (SEZs) as a platform to bring in new opportunities and drive stronger economic growth. The SEZs help in creating clusters of emerging industries, drive innovation, and stimulate consumption in line with economic globalization and regional integration.

There are currently about 380 foreign and domestic companies located in SEZs. More than half are from China (181 businesses), Thailand (28), and Japan (30). Notable ones include Aero works, Essilor, Nikon, Toyota, Mascot, and others.

In terms of employment, SEZs have helped generate new employment opportunities. Between 2002 to March 2018, more than 20,000 jobs have been created across the 11 existing SEZs.

Since 2003, these well-planned SEZs have brought in actual investments of up to USD 1.83 billion, increased government revenue up to more than USD 20 million, and increased exports to more than USD 815 million. The SEZs' accumulated investment increased by 30%, from USD 1.2 billion in 2015 to USD 1.8 billion in 2017.

Investments in the manufacturing sector are concentrated in the economic zones (EZs). Lao PDR has two types of economic zones: Special Economic Zones and Specific Economic Zones. Two key Special Economic Zones are: Savan-Seno Zone in Savannakhet Province and the Golden Triangle in the North close to the borders with Myanmar, Thailand, and P.R. China. The other economic zones are designated as Specific Economic Zones, most of them located near Vientiane Capital.

● Free Trade Zones (Special/Specific Economic Zones) in Lao PDR		
1	Savan-Seno Special Economic Zone	2003
2	Boten Beautiful Land Specific Economic Zone	2003
3	Golden Triangle Special Economic Zone	2007
4	Vientiane Industrial and Trade Area	2011
5	Saysetha Development Zone	2010
6	Phoukhyo Specific Economic Zone	2010
7	Thatluang Lake Specific Economic Zone	2011
8	Longthanh-Vientiane Specific Economic Zone	2012
9	Dongphosy Specific Economic Zone	2012
10	Thakhek Specific Economic Zone	2012
11	Pakse-Japan SME Special Economic Zone	2015

Lao Brewery Co. Ltd. is among the few large manufacturers in Lao PDR, producing beer, bottled drinking water, and soda water. SAYA is a new player in the garment sector producing high-value products made of cotton.



## SUBSECTOR/SEGMENT

Lao PDR's manufacturing sector is concentrated in SEZs. For example, electronics and telecommunications equipment are in Savanh-SENO and Vientiane Industrial Trade Area (VITA) Park and food processing are concentrated in Saysettha Development Zone in addition to Savanh-Seno and VITA Park. In addition to electronic and food processing, Lao PDR's garment manufacturing sector is also on the rise.

● Manufacturing Subsector	● Export Share (%) in 2016
Machinery and Electronics	11.4
Processed Food	10.9
Garment	4.8



## BRIEF PROFILE OF MICRO, SMALL AND MEDIUM ENTERPRISES (MSMES) IN THE MANUFACTURING SECTOR

Only 5.4% of the registered manufacturing establishment in Lao PDR are large while the rest are MSMEs. As the World Bank survey noted that the competitiveness of the MSMEs in the manufacturing sector appears to have deteriorated since 2016, investment in the manufacturing sector needs to consider and factor in costs of reskilling or upskilling the workforce.

Domestic investors or startups may find access to finance, practices of competitors in the informal sector, and electricity tariff as main constraints in their endeavor.

However, businesses can expect an improved investment landscape as Lao PDR implements the National Strategy on Socio-Economic Development (NSSD) 2025 (2015-2025) by scaling up Lao PDR's industrial base to at least 32% of GDP contribution and 19% by agriculture. It is encouraging to note that the focus of the NSSD are the private entities under these two sectors. The Prime Minister Order No. 2 on Improvement of Regulations and Coordination Mechanism on Doing Business in Lao PDR, which aims to improve the business environment, is anticipated to gradually facilitate more diversified investment in the non-resource sector.

Similar to its peers in the Mekong subregion, Lao PDR's strategy to establish SEZs have been successful to some extent in encouraging growth and foreign direct investment in the manufacturing sector. Investors, both domestic and foreign, can expect the same tax incentives and business registration procedures. Foreign investors can expect:

- easing of restrictions on bringing in foreign nationals to undertake investment feasibility studies.
- easing of restrictions on bringing in foreign technicians, experts, and managers if qualified Lao nationals are not available to work on investment projects.
- permission to lease land for up to 20 years from a Lao national and up to 50 years from the government.
- permission to own all improvements and structures on the leased land, transfer leases to other entities, and sell or remove improvements or structures.
- facilitation of entry and exit visa facilities and work permits for expatriate personnel.

Investors and private sector may still have to take into account constraints in terms of limited skills development for the workforce. Lao PDR's physical connectivity has one of the lowest logistics performance index (LPI) in ASEAN. Both private sector and the government will face challenges in terms of integrating the manufacturing sector into the ASEAN and international value chain.

Logistics performance index (LPI) in ASEAN, 2018

● Country	● LPI
Brunei	2.71
Cambodia	2.58
Indonesia	3.15
<b>Lao PDR</b>	<b>2.70</b>
Malaysia	3.22
Myanmar	2.30
Philippines	2.90
Singapore	4.00
Thailand	3.41
Viet Nam	3.27

Source: World Bank



## CHALLENGES AND RECOMMENDATIONS

The ease of doing business score of 50.8 in 2019 ranks Lao PDR 154 among 190 economies, falling from 141 in 2017. According to the World Bank report, businesses cited the practices of (and competition among) firms in the informal sector who tend to operate outside or avoid rules and regulations as one the main challenges. They also cited issues related to transportation, electricity, and insufficient skilled or educated workers to power the manufacturing sector that aimed at producing high-value goods. Enterprise surveys conducted by World Bank continue to report similar constraints faced by private sectors in Lao PDR, among them: access to financing, access to reliable and affordable electricity supply, wide-ranging lack of transparency, policy uncertainty, and inconsistent application of the laws and tax rates.

In order to address skilled labor shortages, focus should be given on:

- further expansion of vocational education and training institutes in key economic zones and improving the quality of education and continuous learning; and
- incentivizing skills development undertaken by private sectors.

Affordable financing to MSMEs in strategic manufacturing subsectors should support the manufacturing sector in enhancing productivity through acquisition of appropriate technology, materials, machineries, and up-skilling of manpower.

The thriving informal sector is partly due to complex business registration processes and requirements. Thus, polices should make it easier to register a business and help to formalize these companies.

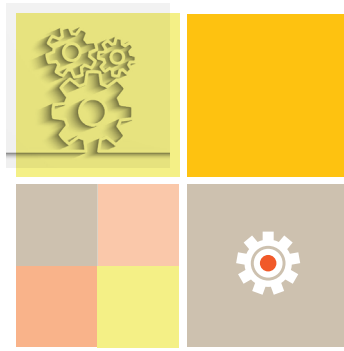
The current tax system is essentially negotiation-based, and therefore, should reflect and tax firms accurately based on their actual turnover.

To strengthen the manufacturing sector in Lao PDR, a promotion of quality investment, innovation, human capital development, advanced and smart technology, and supportive infrastructure and logistics, in addition to effective use of big data would be conducive.



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