



**ANALYSIS
OF THE
SEVENTH NATIONAL SOCIO-ECONOMIC DEVELOPMENT PLAN (7TH NSEDP 2011-2015)
LAO PDR**



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1. Reference Documents

The Government of Lao People's Democratic Republic (Lao PDR) has produced a national development plan since the State was established, initially as a 3-year Interim plan 1976-1978 and then as a series of 5-year plans. The plan currently in force is the 7th Plan for 2011-2015, and this is a review of that document: 'The Seventh Five-Year National Socio-Economic Development Plan (2011-2015)'¹. Authorship is widely shared and the final draft is produced by the Ministry of Planning and Investment. In addition, this analysis takes into account the 2010 PEFA report² and the World Bank Public Expenditure Review³ of June 2011.

2. Country/ Regional Constraints, Challenges, Perspectives

Section 1 of the Plan analyses regional and national constraints. It is a comprehensive analysis of the challenges and opportunities of the country. The main advantages reported are political stability, sustained growth in the previous period and institutional support of the Party, Government and National Assembly, as well as the continued support of development partners (DPs). Sections below give a more detailed picture of the economic, political, environmental and social situation in Lao PDR, with constraints and opportunities.

2.1. Economic and social vulnerability, potential and regional integration

The government of Lao PDR established the New Economic Mechanism in 1986. Equivalent to the reforms in the USSR a sustained effort has been made since then to open up the economy ('perestroika'). The reform is a pragmatic attempt to address a deteriorating economic and social situation. Although at a slower and more controlled pace than in other former socialist countries, the transition to a market economy is carried out consistently, steadily and with some success.

In this context, regional and international integration have been key parts of government policy since 1986. Firstly, the government aimed at gaining membership of the Association of Southeast Asian Nations (ASEAN), ASEAN Free Trade Area (AFTA) and World Trade Organization (WTO) and is also particularly active in the sub-regional integration processes around the Mekong river basin, such as the Greater Mekong Sub-region (GMS) and the Mekong River Commission (MRC). Integration in these international and regional groupings is facilitated by the fact that they do not interfere on internal politics and regime, as membership is not based on any formal requirements on democratisation or human rights. Nonetheless, each requires fundamental changes in laws, rights and governance standards in various productive sectors. As a result, the institutions of the market economy are progressively converging on international standards. In this context, there is a clear traction to improve the rule of law in the commercial field in order to ensure an investment friendly climate.

Secondly, Lao PDR has opted for an export-oriented growth, mainly based on the exploitation of natural resources such as mining, timber, rubber and hydropower. On the positive side, these economic choices have led to a strong macro-economic position and relatively good economic performance. In 2012 the projected GDP growth is 8.3 percent⁴ and GDP per capita reached US\$1,386. GNP more than doubled from 2000 to 2008. There is a relatively large trade deficit (exports \$2,737 million, imports \$5,202 million including mining and HPP projects) and the overall balance of payments (BOP) is projected to be slightly positive with a surplus of \$ 49 million. Headline inflation fell to 3,6 percent (year-on-year) in June 2012 down from 9.8 percent in 2011 and mainly driven by rising food and commodity prices. The Bank of Lao managed to keep the exchange rate LAK/USD and LAK/THB relatively stable and there are clear signs of de-dollarization of the economy indicating increasing confidence in the Kip. Money supply (M2) growth is high at 25% but falling compared with previous years.

¹ Readers should be aware that there is a summary document, translated into English of the NSEDP. There are large disparities between the full version drafted in Lao language and the summary, including the table of contents. For further references consult the Round Table Process at <http://www.rtm.org.la/content/index.php>

² Lao PDR, Public Expenditure and Financial Accountability (PEFA), Public Financial Management Assessment, June 2010, report n° 61791-LA.

³ Lao PDR, Public Expenditure Review, June 30, 2011, World Bank report n° 63200-LA.

⁴ IMF Art IV Consultation Mission report, August 2012.

However, the economy still faces some major vulnerabilities and challenges: more than 70% of the population is still living from subsistence farming. The income-related benefits of growth do not trickle down, neither to the major part of the population (farmers), nor across the territory, while the infrastructure improvements related to the FDI do bring spill-over benefits. Indeed, foreign investment has limited economic multiplier effects into the domestic economy and market. This is a major constraint as domestic market and value chains remain underdeveloped. Much of the growth is not endogenous, redistributed or reinvested in the country. Furthermore, lacking 'in house' value-chains and processing know-how and infrastructure, Lao PDR is exposed to fierce international competition that translates in downward pressures on the conditions for FDI (low taxes, cost of labour, land, conditions in Special Economic Zones). Finally, such growth pattern increases vulnerability to conjunctural events such as the volatility of commodity prices, the slower growth in China and in other export markets.

Growth patterns are as important as growth rates in ensuing inclusive and sustainable economic growth for long-term poverty reduction. Development achievements to date in Laos have been accompanied by widening gaps between rich and poor, women and men, ethnic groups, and growing rural/urban and regional disparities. Urban areas and districts have experienced rapid growth and poverty reduction, but rural areas continue to lag behind. The northern part of the country remains poorer than the southern and central regions, and uplands are poorer than the lowlands. Poverty rates also vary according to ethnicity. The reduction in the national poverty rate is reflected in both urban and rural areas however, rural poverty rates still remain almost twice the urban poverty rates.

Education is among the better-performing sectors in Lao PDR, as reflected in continuous progress across all key indicators. Net enrolment rates in primary schools rose from 58 percent of primary school-age children in 1991 to 86 percent in 2007. Progress in the primary school completion rate, however, is slower rising from 45% in 1990 to 77% in 2007. Literacy rates have been increasing, although the increase in the secondary school age groups is more modest. As is the case with other MDG indicators, there are variations across regions. Provinces with low enrolment rates are often those with high proportions of rural, poor and children of different ethnic dialect speaking groups. Significant differences persist in literacy rates between Lao native-speaking and ethnic dialect speaking groups

The challenge for poverty reduction in Laos therefore is to sustain the level of economic growth achieved over the previous decade while enhancing the equitable distribution among the population and across provinces and to rural areas.

Despite impressive gains in economic growth and reduction of poverty in recent years (from 46% of the population in 1992 to 27% in 2008), challenges remain in other areas, such as the high levels of (chronic) malnutrition and food insecurity. This holds especially true for the most vulnerable group of children under five, of which 37 % remain underweight, and 40 % are stunted. This rate has not declined over the past ten years. Under-nutrition also affects other vulnerable groups including pregnant and lactating women: 23 % of the population is undernourished. Lao PDR is likely to fail in reaching the target of reducing malnourished children to 30% by 2010 (NSDP target) and to half the 1990 level by 2015 (MDG target). Consequently, the government and development partners are putting a much stronger focus on nutrition.

In addition, according to WHO standards and the most recent surveys, Lao PDR faces multiple health and nutrition related problems requiring urgent action. These include lack of breastfeeding, Vitamin A deficiency, Anaemia, Iron Deficiency, and parasitic infections.

2.2. Country and state stability and capacities

State formation is recent and followed more than 30 years of overlapping wars. Indeed, it was only with the creation of Lao PDR in 1975 that the main attributes of statehood were reunited: border control, revenue collection and bureaucracy. Lao PDR started almost from scratch: the bureaucracy was deprived of qualified human resources due to the long lasting war and forex accounts were almost empty. From 1975-1991 Lao was governed directly by the party without any Constitution or distinction between the political, party and administrative apparatus (Party-State). Only in 1991 and 1992 were the first Constitution and budget adopted, paving the way for the modern state of Lao.

According to WB CPIA, Lao PDR has improving scores for the public sector management and institutions cluster and for the social inclusion and equity cluster.

CPIA Scores (scale 1-6)		
	Public Management and Institutions	Social Inclusion and Equity
2007	2,7	3,2
2008	2,9	3,4
2009	2,9	3,4
2010	3,1	3,5
2011	3,1	3,5

Source: World Bank (2011), *Country Policy and Institutional Assessment, Lao PDR*

The State administrative system is present throughout the country and reaches village levels. While the public management and institutions cluster score has improved, it is still on 3.1 on a 6 point scale. One weakness of the administrative system is the lack of horizontal coordination. There is also an underdeveloped civil service in some functions; unclear exclusive responsibilities between various layers of government and their consequent lack of autonomy and related accountability mechanisms; and finally, the intermingling of state institutions and party apparatus blurs accountability lines by preventing independent executive, legislative and judiciary to emerge.

2.3. Political situation and governance: fundamental values

In the EU legal basis, political governance refers to the EU fundamental values, which include democracy, rule of law and human rights. The situation in Lao PDR with regard to these fundamental values is mixed. The country is committed to developing its legal system, but it is not committed to multiparty democracy or to significant immediate increases in individual political and civil rights.

The Government is relatively tolerant in daily life but will react with severity when the political system is put into question. Civil liberties are set in the 2003 amended Constitution which covers obligations and fundamental rights, such as the right to vote, to work and to lodge complaints. The Constitution also provides the right of assembly and the freedom of speech and religious belief but in actual terms, the penal code severely restricts the exercise of these rights. The freedom of expression and the media are tightly controlled by the authorities (Ministry of Information) though over the last couples of months very harsh articles have been published in the English edition of the main local newspaper about corruption, abuse of power by government officials and about the much sensitive question of land use and land grabbing by foreign companies. Foreign print media are available and internet is not censored (but only 10 % of the population has access to internet).

One has to consider carefully though whether the intermingling between the three fundamental values (democracy, rule of law and human rights) is fully appropriate in the case of Lao PDR. One needs to avoid in any case that amalgamating these concepts leads to simplistic conclusions and missed opportunities on which to build the EU response as a contribution to pave the way for incremental reforms.

External requirements to integrate with the global economy and to accelerate economic development are probably the main drivers for the development of the legal system, but not for democratic transition. From a development perspective, such an evolution is still positive: stable rules are necessary to attract foreign investors and a precondition to the development of endogenous economic processes. Ensuring sufficient legal stability, predictability and incentives is crucial to provide an enabling environment for domestic investors and entrepreneurs. NSEDP recognises this challenge in its fourth objective ‘better public administration, rule of law and fighting corruption’.

The Lao approach to the rule of law is consistent with its double economic strategy of both filling the investment gap with FDI and ODA and generating endogenous growth. Rule of law in this context is a tool to rationalise social relations for economic transition. As such it can be considered as a first building block of a ‘social contract’ to help unify private interests and ensure uniform, impartial and efficient implementation of the law. By doing so, it establishes the necessary stability and

predictability for economic activities against state arbitrariness, increasingly perceived as detrimental to investment. This requires the government to be fully sovereign and capable of enforcing the law over its territory and population.

In addition, although not always visible for external actors, there are some evolutions in the areas of democratisation, human rights and rule of law. The National Assembly (NA) increasingly plays a pivotal role in the national policy with its wide ranging duties and responsibilities. The capacity of the National Assembly to fulfil its constitutional mandate has increased in recent years in terms of independent advocacy, oversight on government and governmental institutions. Despite these significant achievements, the NA is still a young institution, which needs further support to fully contribute to a truly participatory and representative democracy.

The opportunities in each case are more likely the outcome of unintentional side-effects of ongoing reforms, rather than the outcome of a conscious and deliberated attempt at reforming state institutions. However, it clearly indicates that there is a certain domestic demand and more 'reformist' trend within the system itself. Indeed, the regime is not homogeneous. It still remains to be seen whether these initiatives will converge and pave the way for more structural reforms. This may depend on the outcomes and results of the 'experimentation' in certain policy areas and on their influence on the different forces at play. The rule of law, in particular the legislative function, is probably the one with most traction.

2.4. Environment

Sustainability is threatened by certain aspects of the directions of economic growth as regards the management of natural resources and land uses. Mining is by definition time-limited and contributes most to exports and economic growth. Forest clearance for agricultural and hydro-power development and infrastructure building threatens environmental sustainability and the rural livelihoods of the displaced farmers. Illegal logging and the depletion of primary forests and biodiversity corridors are real challenges for the Government. This is recognised in the plan document, but does not necessarily direct annual planning nor budgeting.

Moreover, hydropower development is potentially threatening river basin ecosystems as well as people's livelihoods. While providing considerable potential for socioeconomic development and, in particular, the generation of export income, the hydropower projects on the Mekong River and its tributaries – existing (14 dams), those currently under construction (11) and planned or proposed (70, including 10 on the Mekong mainstream) - come with considerable environmental and social risks. In order to ensure that benefits outweigh costs and that the entire population benefits from hydropower developments in a sustainable way, it is important to ensure the development of and the compliance with sustainability standards. Due to the trans-boundary nature of the Mekong River Basin, it is also vital to comply with international and regional agreements Laos has committed to – most notably the 1995 Mekong Agreement.

In addition, climate change and natural disasters such as the 2009 floods constitute a major challenge for the population, especially those for whom farming is the main activity and for the public powers to help prevent and mitigate. Extensive slash-and-burn farming is a cause of environmental and land degradation, especially where crop rotation cycles are being shortened.

2.5. Social situation and increasing inequalities

Uneven development is a major constraint on inclusive growth. In the 2005 Population Census, of the 2,738,893 who reported that they worked, 1,149,906 were working on their own account and 1,260,171 were unpaid family workers. The low population density and scattering of remote small settlements present a development challenge, both in terms of the provision of infrastructure and attracting investment. The uneven distribution of income and wealth manifests itself at the poorest levels of society in poor nutrition and in perinatal and infant mortality rates that are higher than those in the neighbouring countries. Access to clean water and sanitation are key health issues for a large part of the population. These are addressed in the Plan with support from selected development partners. The government is conscious of the uneven distribution of the benefits of the recent rapid economic growth and is addressing the issue with a programme of decentralisation, of rural development and education and health investment to alleviate the inequalities.

Rural development policy is partly based on the migration of farmers from upland areas and changing their agricultural methods. The Government has pursued a policy of resettling small villages into larger rural centres (Kumban Policy), in order to provide social services. This policy is designed to improve farmers' incomes but has not always been successful. At the same time, other displacement takes place from concession areas and farmers are moved to new locations, sometimes with proper compensations, sometimes not. Migration exposes upland people to new diseases and requires adaptation to a different diet. This has resulted in increased death rates and the creation of lower incomes for some displaced families.

In some areas, the resettlement goes into reverse as people discover that they cannot survive in the new areas and return to the old ones. In some cases the resettlement is only half-complete, and people retain dwellings (field houses) and land in the old areas⁵.

Unexploded ordinance (UXO) continues to be a source of vulnerability. Ten of the 17 provinces are affected and 25% of all villages. 41 out of the 46 poorest villages have UXO contamination. Over 50,000 UXO casualties have been recorded between 1964 and 2008, of which 60% resulted in death. There are around 300⁶ casualties every year. As well as the threat to human safety, the UXO problem makes development more expensive: in the contaminated areas, UXO must be cleared before there is any infrastructure building, commercial farm development, mine development or construction for schools and clinics. The cost of clearance can be equivalent to the cost of building.

3. Country Development Priorities and Objectives

The IX Party Convention of the LPRP in March 2011 committed the country to poverty-oriented development and to the achievement of the MDGs. The priorities are political stability, economic stability and poverty reduction. Although progress has been registered as regards some indicators, the government expressly admitted that it had not yet achieved all the objectives included in the previous 5-year plan period. This section assesses the government response to the identified challenges in terms of policy framework, relevance and credibility of the 5-year national development plan.

3.1. Government's response and credibility of the policy framework

3.1.1. Policy priorities in the 7th National Socio-Economic Development Plan

The 7th Plan, for 2011-2015 identified seven 'directions' to respond to the above challenges:

1. National economy
2. Rural development and poverty eradication
3. Educational reforms and human resource development
4. Better public administration, rule of law, fighting corruption
5. National defence
6. Increase labour skills
7. Industrialisation and modernisation

These are underpinned by a more general set of commitments: 'The targets and directions of the Five-Year Social-Economic Development Plan are as follows:

1. Ensure continuation of national economic growth with security, peace and stability, and ensure GDP growth rate of at least 8% annually and GDP per capita to be at least USD 1,700.
2. Achieve the Millennium Development Goals by 2015, and adopt appropriate technology, skills and create favourable conditions for graduating the country from LDC by 2020.

⁵ Olivier Evrard and Yves Goudineau, 2004, 'Planned Resettlement, Unexpected Migrations and Cultural Trauma in Laos', *Development and Change*, 35 (5) 937-962.

⁶ National Strategic Plan for the UXO sector in Lao PDR 2010-2020 - the safe Path Forward II", November 2009.

3. Ensure the sustainability of development by emphasising economic development with, cultural and social progress, preserving natural resources and protecting the environment.
4. Ensure political stability, peace and an orderly society.

3.1.2. Policy formulation process and ownership: democratic centralism

In line with the principle of ‘democratic centralism’, NSEDP is formulated and implemented following various consultations: from Prime Minister to Village level and is approved by the National Assembly. The process of producing the plan is managed by the Ministry of Planning and Investment who produce the final draft, usually with some outside technical assistance.

The centrally led and the local planning processes are coordinated and supported by MPI and by the Provincial Departments of Planning and Investment (DPI) respectively. The DPIs are agencies under the Ministry of Planning and Investment (MPI) which promote and manage foreign and domestic investment on provincial level. They are responsible for supporting the formulation of five-year plans and annual plans before submitting budget requests. Corresponding planning offices exist at district level. The plans and programmes at provincial level are outlined in provincial socio-economic development plans and thematic (sector) development plans. The content and the projects in the provincial plans are broadly corresponding to the national-level plans.

The DPIs act as secretariat to the MPI (vertical) and to the Provincial Governor (horizontal) in mapping out the development strategy for the provinces. The Office of the Governor is the highest ranked official body in the province and is responsible for supervising and assisting the implementation of national and local policies and development programmes.

Ahead of each five-year plan exercise, DPIs organise meetings with all sectors to discuss strategy and direction for the plan and trends in investments. The actual planning is then carried out by planning divisions of all line sectors, and is coordinated and summarised by DPIs. Although, planning is carried out across sectors, there are overlaps in target-setting and related planning, particularly in the areas covered by the Agriculture and Rural Development sector and Natural Resources Management and Environment sector.

The 7th NSEDP was circulated to development partners before being finalised. On the implementation side, NSEDP is the first point of reference for all planning, programming and budgeting. The process of implementing the Plan consists of annual programming and planning by the Ministry of Planning and Investment, which is then reflected in budget allocations. The annual planning and budgeting process also involves consultations and consolidation of competing demands.

The process, however, is not watertight, as the interaction between ministries and provinces as well as between the Ministry of Planning and Investment and the Ministry of Finance involves a series of bids and negotiations as an annual round where priorities are negotiated. Moreover, the capital budget is produced by MPI and the recurrent budget by the Ministry of Finance.

The process is centralized because a single person with the appropriate authority is required to endorse all decisions. In addition, in a hierarchical culture, central priorities and high rank official decisions highly determine the outcomes of the annual bargaining and consultation exercises. Therefore, policy and the will to implement it rest mainly with the hierarchy, thereby assuring the leadership’s ownership and commitment to the plan. Also, given the reach of the state and of the party, all layers of the administration are familiar with the government’s priorities, including the achievement of the MDGs.

The outcome of these (annual) consultations is a list of projects that reflects actual prioritisation of the NSEDP’s objectives, rather than policy coordination. Indeed, during these bidding processes ministries, provincial governments, districts and departments compete for scarce resources. Despite monthly inter-ministerial meetings, inter-ministerial coordination is weak as ministries predominantly work in ‘silos’. The most striking example is the elaboration of the capital and the recurrent budget by two different ministries and with limited connection; there is no information sharing culture. Policy coordination is also difficult as many policy frameworks are still nascent. Finally, government, central and local bureaucracy and party’s responsibilities are blurred. This does not facilitate a division of tasks that is appropriate and conducive to predictable patterns of interaction and trust building between

policy actors.

The central-local relations illustrate this point: sub-national levels are part of the hierarchy from the central administration and bureaucracy. Reflecting this political centralism, governors have ministerial rank and are accountable first to the party and then to the prime minister. Governors have created their own bases and gained a degree of political autonomy for their provinces, leading to some differentiation in policy implementation between provinces despite the fact that none of the sub-national layers has been given a 'general mandate' with autonomous planning processes. Therefore, sub-national levels need to be understood as Sub-national administrations rather than local governments. The discretion of Governors needs to be understood in this centralised framework where their discretion has been acting as a mutually reinforcing factor of the party and of the administration at local levels, while asserting some local autonomy.

Some homogenising measures are being implemented, such as the establishment of budget norms for non-salary expenditures in education and health. These are positive steps but they are only one side of the coin, as reaching results at the bottom end of service delivery often requires a certain degree of autonomous planning and budgeting so that sub-national authorities can implement the priorities they have identified with the communities. While it is questionable that local preferences are fully and systematically taken into account by the upper levels, all projects put up for approval are put forward by the lower levels of the administration, subject to size limits at each level.

Two initiatives exist to progressively give some policy and budget autonomy to the districts: the District Development Fund and decentralisation to the district level. The government is closely looking and considering the results of these experiences.

It is not part of the remit of the NSEDP to resolve these issues and it does not define how policy coordination across departments and levels of the administration is to be achieved to implement NSEDP and to keep a balanced overall policy framework and budget. However, there is some progress as, first, coordination mechanisms are being established on a sector-by-sector approach, depending on the stage of advancement and priority. Second, through its objective 'Better public administration, rule of law, fighting corruption', NSEDP targets the performance of the public sector in implementing the reforms and delivering services, which indirectly requires strengthening policy coordination during formulation and implementation.

3.1.3. Coherence of the overall policy framework: NSEDP and sector policies

The most advanced sector, with regard to policy frameworks, is education, which has a 5-year Sector Development Plan and an Evaluation Framework. From the coming year there will be a costed education sector plan which will be used as a basis for the budget submissions for the sector.

Symbolically, NSEDP is a 5-year plan and not a policy. Lao PDR does not conform to an ideal type whereby governments concentrate in a first stage in establishing a comprehensive policy framework, then develop the tools for implementation with policy instruments including regulations, services and funds before starting any policy implementation. In Lao PDR policy experimentation is an important feature of policy-making at sector level. It allows testing and informing the formulation of policies accordingly. This characteristic has been reported for several reforms and new policy areas, such as justice, legal system, legislative changes, decentralization and poverty reduction.

In this context, it can be said that there is global coherence between NSEDP and 'sectors' in the sense that the former provides the general framework for such policy experimentation. It is large and wide enough to be flexible, and to provide a menu from which to choose during annual planning and to adjust to changing circumstances.

However, detailed coherence of the overall multi-annual policy framework, the budget and programs within the sectors remains a challenge. First, policy experimentation is still being conducted at sector levels. Second, sector policies are in process of being developed and can inform the elaboration of the NSEDP, while not being completely comprehensive. Finally, up to now Lao PDR has relied on a vertical planning process where a centralised mechanism was sufficient in the context of fragmented and project-based planning in sectors. However, the development of sector frameworks and policies is progressing and will likely lead to the emergence of more comprehensive sector policies. Over time,

the rigidity and verticality of the 'democratic centralism' may need to evolve to embrace some degree of decentralization to enable response to varying local socio-economic conditions.

More particularly as regards the fourth direction 'Better public administration, rule of law, fighting corruption', the following specific 'sector' plans need to be considered:

1. Legal Master Plan 2012-2020 that includes the Ministry of Justice, Supreme Court, Prosecutor and Ministry of Public Security. Many donors support the plan (EU, UNDP, JICA, UNICEF, UNODC, USAid and ADB for commercial legislation, LuxDEV, Asia Foundation, French Cooperation, Vietnam). The master plan is considered overambitious but is the reference for the government and the donor community.
2. PFM reform that has been supported by the donor community and has achieved some success.
3. Civil service reform has been given particular attention most recently, with the recent Politburo directive that defines the vision for 2020 (still under discussion), the creation of the Ministry of Home Affairs in charge of civil service, the decision to increase up to approximately 11 000 the staff and the decision to establish a financial incentive mechanism to attract staff to work in remote areas.

A further critique which could be made of the NSEDP is that the part that deals with progress towards the MDGs and is in large part funded through ODA is not well connected to the part that deals with economic growth, largely funded through FDI.

3.1.4. Credibility: link between the plan, the budget and sequencing

Implementation of the NSEDP and associated economic reforms is meeting considerable obstacles such as poor infrastructure, lack of financial resources and a lack of skills. Neither NSEDP, nor other plan's objectives are meant to be implemented within the given timeframes: it is widely recognised they are overambitious but that their real utility is to give the overall direction.

This also translated in the budget dimensions: first, there has been criticism by some that the 5-year plan is not costed. The Ministry of Planning and Investment, however, produced an MDG costing report in 2010 which attempted to estimate the resources needed for meeting the MDG targets in Lao PDR by the year 2015. The report followed the approach of 'total costing' i.e. all costs were accounted for: fixed and recurring, and those borne by the government and private sector (including private consumption). The findings of the report fed into the formulation of the 7th NSEDP. But the 7th NSEDP itself was never intent to include costs. And if it was costed it would likely be unaffordable. Second, NSEDP is not fiscally constrained and there is no MTEF. Finally, there is a clear challenge of harmonising sector budgets with the overall budget.

This does not mean there is no prioritisation. The 7th NSEDP plan sets objectives, which are then translated and prioritized in the annual versions of the plan and enacted through annual budgets. Therefore, the annual budget is the main tool to consider and it makes sense to 'get the basics right first' before pushing for MTEF. The main challenge of this approach relates to the opaque and unpredictable annual bidding process: it is a bottom up process based on needs. Proposals are made without having a clear indication of the size of the available envelopes.

One possible weakness of the current system is the proportion of total spending that appears in the national budgets. The PER stated that 'the budget is relatively comprehensive and this is improving further as a result of the recent centralisation of revenues...'. The Budget Law 2006 requires that: i) all revenues are part of a unified budget, including DP funding; ii) all revenues and expenditures are fully centralised and account for in the national budget and that no revenues shall be retained outside the budget system; iii) no separate funds may be established without proper authorization; the budget is unitary and covers all the levels of government.

Two elements may compromise the comprehensiveness: There are 8 separate statutory funds. The EU estimates that the total spending of these funds is around 5% and the Ministry of Finance directly controls the accounts and disburses only on requests of the respective boards. More importantly, it is expected that these funds will be included in the national accounting and treasury system with the Single Treasury Account; secondly: technical revenues or revenues retained by sector ministries and

provinces and which precise amount is not known. Yet, the PER gives an estimation: ‘anecdotal evidence suggests that the technical revenues reported in the budget plan account for only one third of what is actually collected by agencies’⁷.

In addition there are ODA funded expenditures which do not appear in government budgets at any level. Results of the 2011 Survey on Monitoring the Paris Declaration Survey suggest that overall approximately 60% of ODA for the government sector is implemented outside government systems.

The table below shows that ODA and FDI have been, and will remain, important sources of development finance. In addition to representing a significant percentage of GDP, ODA also finances approximately one quarter of Government expenditure. FDI, which accounts for approximately 15% of GDP will be an important driver of growth and employment.

Table 1: Lao PDR Budget, ODA and FDI data

	2008	2009	2010	2011	2012 (proj.)	2013 (proj.)
Budget (% of GDP)	18.5	24.1	18.6	19.0	20.8	
External finance of the budget (% of GDP)	4.9	4.4	4.4	4.7	5.0	
External financing (% of budget)	26.5	18.2	23.6	24.7	24.0	
ODA (% of GDP)	9.4	9.7	9.0			
FDI (% of GDP)	17.3	14.0	10.7	13.6	15.3	
ODA	500.3	542.9	585.7			
GDP (USD million)	5,313	5,598	6,461	7,891	8,937	9,722
FDI (net, USD million)	921	785	692	1,071	1,374	2,439

(Sources: Lao PDR, Report for the 2011 Article IV consultation, IMF Country Report No. 11/257, August 2011, Table 2, p.23 and Table 3, p.25; Lao PDR Foreign Aid Implementation Report 2008/09)

Note: for simplification the table refers to calendar years. Lao fiscal year is 1 October – 30 September, hence 2007/08 is noted as 2008.

In an ideal world a five-year social and economic development plan would be directly translated into a medium term expenditure forecast and hence into a series of annual budgets. In Lao PDR such a watertight connection does not exist, for some of the reasons set out in the plan itself. However the NSEDP does provide a framework for all the actors in national development, from villages to ministries and including development partners to participate in a conversation about national direction. It is supplemented by an annual planning process and an annual budgeting process that enact those general directions.

3.2. NSEDP’s relevance to the country’s challenges

3.2.1. Challenges addressed in NSEDP

The priorities of NSEDP are consistent with the challenges and perspectives of the country as it considers lines of action that can contribute to support *sustainable inclusive growth, public sector reforms and service delivery*. Economic growth at a continuing high rate is the first priority, without which the other goals will not be achieved. However, the government recognises that growth will not automatically lead to the achievement of the MDG targets because of the social and geographical unevenness of development. Therefore, NSEDP includes parallel commitments to growth and improvement of social welfare through support to specific sectors and commitment to improve public

⁷ World Bank (2011) Public Expenditure Review, Lao PDR, page 45.

sector performance. This is reflected in the main NSEDP directions: the overarching priority is the exit from LDC status and the achievement of the MDG targets. Commitments on 'Educational reforms and human resource development', 'Better public administration, rule of law, fighting corruption' and 'sustainability and political stability' reflect this line of thinking.

Therefore, on paper, NSEDP follows the 'Asian style tradition': it commits to develop the country and orient national economy towards social utility as reflected in its development priorities. This is to be achieved through a 'governed market' based on public regulation of private interests through coherent policies and investment in social sectors. To this aim, and mirroring its Asian counterparts, including the so-called 'tiger economies' NSEDP aims at improving the formal rules by supporting the rule of law and public sector performance.

On the economic field, NSEDP pursues two types of development strategy simultaneously to respond to the challenges: On the one hand, the Investment gap model is based on the assumption that sustainable economic development requires investment by state and private sector at a level that exceeds domestic savings. The gap is filled by FDI and ODA until the country achieves a sustainable level of domestic savings and resource mobilisation to grow at 8% per annum. On the other hand, the 'endogenous growth model' is based on the assumption that development will take place through increasing factor productivity. Human capital development through education, training and health improvements; land development through irrigation, land management, farming practices and inputs improvement; capital development by improving financial intermediation and growing the financial sector. This latter is about generating local development and domestic value chains and markets.

The first strategy calls for large volumes of FDI and ODA, large land and mining concessions, large hydro projects and large-scale infrastructure development. The other requires development of human capital, improving farm yields through new seed varieties and farming methods, infrastructure in rural areas, small-scale credit to improve capital quality. The other part of the endogenous growth strategy consists of the various efforts to develop the private sector and especially Small and Medium Sized Enterprises. FDI in the garment and other manufacturing sectors is also a contributor to the improvement in factor productivity.

In practice the first strategy has taken precedence, as is shown by the sector growth figures. As a result, the economic growth strategy relies to a large extent on attracting FDI, in commercial farming, especially rubber plantations and other plantation crops, bauxite, gold and copper mining and hydroelectricity generation. The major inward investors in the natural resources sectors are from China, Japan, Vietnam, Australia and Thailand. The main attraction is natural resources: gold and copper are plentiful; land can be assigned to foreign investors through concessions, since all land is state owned. And the domestic value chains and markets remain underdeveloped. In addition there is FDI in non-natural resource sectors, such as hotels and tourism and the garment sector.

The government pursues a policy to turn land into capital by attracting foreign investors (plantations, mining, special economic zones). There may be constraints on the continuing conversion of land into capital in the way it has been done: resistance from those cleared off the land and part of the elite is creating discontent within and outside the party, although it has been kept under control until now. One of the side effects of this policy has been the misuse of the focal areas and resettlement policy.

In addition, to give access to services to the population living in remote areas, the Plan deals with this issue through the resettlement of population, both in Kumban settlements and Focal Areas, where people are grouped into more dense settlements and through the declaration of development villages. However, this approach leads to considerable problems, including resistance to the new settlers by established inhabitants, language and culture differences between those who move and those who receive them, health and social problems and, finally, loss of livelihood linked to lack of land availability for resettled people and due compensation.

3.2.2. Country challenges that are not addressed in NSEDP

As mentioned above, political reforms linked to EU fundamental values are not considered in the NSEDP as they are not perceived as a challenge. However, NSEDP and ongoing other initiatives provide indirect entry points to pave the way for incremental approaches.

In addition, central-local relations have been for a long time an issue for public sector performance but were not dealt with as such and in a comprehensive manner in NSEDP. Some issues were addressed rather in a scattered manner under different policy directions. However, the government fears population unrest because of increasing inequalities and recent popular turmoil in various parts of the world. As a result, Politburo recently adopted a new resolution aiming to clarify central-local relations in 66 districts across the country. The real modalities and outcomes in terms of autonomy are still under discussion.

4. Consistency with EU Development Policy

Underpinning the joint EU strategy at the political level is the statement of the EU development policy – the "European consensus" - which is the framework of common principles within which the EU and its Member States each implement their development policies in a spirit of complementarity⁸. The common principles of EU development cooperation activities in Lao PDR are built upon the principles of ownership and partnership, dialogue on human rights, participation of civil society and promotion of gender equality.

The Communications 'An Agenda for change' and 'The future approach to Budget Support' lay down the priorities and guiding principles for the future. They identify two major priority areas: first, Human Rights, democracy and other elements of governance. Second, inclusive and sustainable growth, that covers: (a) social protection, health, education and jobs; (b) business environment and regional integration; (c) sustainable agriculture.

EU development policy is hence based on inclusive growth, political governance including democracy, human rights and rule of law, and sustainability in social and economic integration terms. As has been shown, NSEDP includes many elements, but not all, particularly as regards political governance. However, there are entry points and evolutions on which to build.

On inclusivity, the plan recognises the need to make economic development more inclusive and is taking steps to do so. Indeed, there has been a shift of circumstances from a situation where donor agencies were trying to make economic development happen under difficult circumstances, to a situation of increasing economic dynamism in Lao PDR that generates negative side effects in domestic processes and inclusion. This might require a shift in focus in order to address the new needs that have emerged with fast growth. NSEDP provides a basis to adopt such an approach.

As regards political governance, important conditions are not yet in place, including separation of powers, elections, multi-partyism, political and civil rights, rule of law. Lao PDR has conducted a 'perestroika' without a 'glasnost' and there is no sign of political will or deliberated attempt to reform in this sense in the near future. Nevertheless, there is dynamism, drivers of change and positive evolution over time under each fundamental value: democracy, rule of law and human rights, where policy experimentation is happening and may lead to institutional changes. Examples include a wider remit for the National Assembly, the possible creation of elected councils at District level and decree 155 on NGO registration. These indicate the presence of a certain domestic demand and that the overall direction of travel may be regarded as positive.

Governance arrangements are not always transparent and there is evidence of corruption at various levels of government. There are statutes outlawing corruption and there are plans for a more transparent accounting system for government expenditures, which should reduce the opportunities for mismanagement.

⁸ The European Consensus on Development was signed on 20 December 2005 by the Presidents of the Commission, Parliament and the Council (http://ec.europa.eu/development/icenter/repository/european_consensus_2005_en.pdf)

The policy of opening up the country to the world, with inward investment and trade has had consequences for the regime: integration in the ASEAN region has required conformity with a large number of laws, practices and standards. Membership of the WTO brings another set of changes in its wake. Economic liberalisation and the development of a market economy have brought about economic growth and improved living standards for some part of the society. It is likely that further economic growth may bring further positive developments in rights and democracy, especially as a younger generation is exposed more and more to the world beyond the borders, through education, television, internet and travel.

5. Performance Assessment and Monitoring

5.1. Past performance

Each NSEDP has a section setting out the achievements of the previous plan against targets. The main targets, GDP growth and growth by sector were over-achieved, apart from the industry sector which grew more slowly than planned. The banking sector grew more rapidly than anticipated. Inflation was mostly kept under control, especially towards the end of the plan period while the Kip gradually appreciated against the Baht and the Dollar.

The plan reported some shortcomings: the rate of poverty reduction was high, but not as high as the overall economic growth rate; the labour market was not functioning as it should with a combination of out-migration of Lao workers and immigration of workers from neighbouring countries to compensate for labour shortages in some provinces; exports are mostly from the natural resource sector and therefore not sustainable in the long run and ‘such an export pattern risks fluctuation in commodity prices and has little value added for the country.’

5.2. Domestic Performance and Monitoring framework

Performance and Monitoring frameworks are crucial for the formulation and implementation of the overall government’s policy. There are some building blocks for Performance and Monitoring framework, which, among others, includes the following:

1. The Consumer Price Index (CPI) monitors the overall implementation of the NSEDP and reports to the National Assembly on a bi-monthly basis. It also ensures the annual performance report on plan implementation but information collected is descriptive and incomplete.
2. The Department of International Cooperation (DIC) in the Ministry of Planning and Investments (MPI) is responsible for monitoring of ODA projects. It is based on plans at central level rather than on actual disbursements at project level. In the framework of the Vientiane Declaration Country Action Plan, DIC has developed an Aid Management Platform (AMP) , a system that in principle should track all projects (grants and loans) provided by DPs.
3. Ministry of Finance monitors all loans and technical assistance tied to loans.
4. The Bank of Laos monitors debt and debt repayment.
5. The National Economic Research Institute (NERI) publishes each year the Annual Economic Report that monitors and assesses the development of macroeconomic situation of the country
6. Each Ministry has a research institute whose main task is to compile statistics for reporting purposes as well as multiple monitoring and data collection systems in their sector in addition to those linked to donor’s projects.
7. MDG progress reporting as part of the annual Round Table meeting reports.

However, NSEDP identifies critical challenges and issues to address in the future years to improve the performance assessment and monitoring systems. The assessment of the M&E framework included in the plan is comprehensive and includes issues, such as the poor statistical basis for planning and the underdeveloped monitoring and statistics systems for the plan at local and national levels. In addition, the M&E system is fragmented across the multitude of actors as there is no real functional link or coordination between different mechanisms, multiple reporting and various data collection tools. This is further compounded by inadequate coordination between line ministries and agencies and lack of human and financial resources. Finally, M&E is not yet considered as a management tool.

5.3. Review mechanisms and aid coordination

The Government of Lao PDR, in collaboration with its development partners, has developed an elaborate structure of aid coordination with the aim to harmonise the aid programmes of various donors and to improve their effectiveness. Institutionally, the lynchpin of the aid coordination system is the Round Table Process (RTP) which has a vertical structure at the apex of which lies the Round Table Meetings (RTMs) which are organised every three years. Annual Round Table Implementation Meetings (RTIMS) usually take place in November and are the second-highest level of government-donor interaction. They represent an important event that gathers high-ranking government officials and the development community to exchange information on progress in the implementation of the NSEDPs and to discuss major development challenges and priorities. RTIMS increasingly provide an opportunity for open and frank dialogue between different stakeholders. The Round Table Process is largely government-led and managed with technical advisory support, mainly from UNDP and, to a lesser extent, from other development partners.

Within the Round Table Process, in 2006, the Government organised a Sector Working Group (SWG) mechanism co-chaired by Government and Development Partners which now includes ten SWGs and related Sub-sector and Technical Working Groups (TWGs) which are chaired by senior Government officials and co-chaired by Development Partners. These are:

SWG	Sub-groups or Technical Working Groups	Additional groups
Health	TWG Planning & Financing TWG Human Resources TWG Programme	
Education	Basic education WG Post-basic education WG Financial Planning and M&E WG Research Focal Group	Informal Education Donor Working Group
Governance	Public Service Improvement Sub-SWG Legal & Institutional Sub-SWG	Public Expenditure Management Strengthening Programme (PEMSP) is not formally linked to SWG mechanism, but content relates closely to 4th component of Governance strategy.
Macroeconomics		Poverty Reduction Support Operation (PRSO) is not formally linked to any SWG as the agenda cuts across sectors Lao Business Forum,
Trade and PSD		
Infrastructure	Water and sanitation Sub-group Transport Sub-group	
Mini-Dublin and Illicit Drugs Control	Crime Sub-SWG Drugs Sub-SWG	
UXO	Clearance TWG Victim Assistance TWG MRE TWG	
Agriculture and Rural Development	Irrigation Sub-group Forestry Sub-group Farmers and Agribusiness Sub-group Uplands Development Sub-group	
Natural Resources Management and Environment	Water Resources Sub-group Environment Sub-group	
		Informal Gender Working Group

The Department of International Cooperation, Ministry of Planning and Investment is the overall coordinating agency of the SWG mechanism. To facilitate the coordination of the Sector Working

Groups (SWG), the Ministry of Planning and Investment manages the quarterly meetings of the SWG Chairs and Co-chairs.

The SWGs and the Round Table Process are useful tools and mechanisms to exchange information on development priorities and to improve sector aid coordination and effectiveness. Evidence from the SWG review carried out in 2010 suggests that SWGs have played an active and productive role in supporting the Government of Lao in the development of the 7th NSEDP. Given that the 7th NSEDP projects that one quarter of its financing will need to come from ODA sources, partnerships established in SWGs are critical. In a country where ODA accounts for a very significant share of public investment and of the national budget, coordination and harmonization of aid assumes critical importance in the development process. However, SWG transactions costs are often high and current structures are overly fragmented and process-oriented offering limited scope for substantive policy dialogue.

Whilst SWGs foster the partnership between GoL and DPs, they are still lacking in intra-governmental collaboration. For SWGs to thrive they need to be complemented by dialogue within government across the relevant ministries/bodies or departments within them, as well as by dialogue across DP agencies themselves. Communication within line ministries, particularly where different departments or individuals lead the sector ministries inputs into different SWGs, need to be strengthened.

6. Conclusions

Lao PDR is on a trajectory from a closed, communist state to an open economy, supported by a large number of development partners. It has a development planning process which is inherited from the Communist era and centred on a five-year plan with annual planning and budgeting processes. All these processes involve participation by representatives of the hierarchy from central to village level.

The plan is very inclusive (at government level), as the process of writing it consists of the Ministry of Planning and Investment assembling the plans of ministries, provinces and districts and making it a whole.

The actions that flow from the plan include government actions at all levels, from central government through ministries, provinces and districts to the village level. It also sets the direction for actions by development partners, whose programmes and projects form part of the implementation of the plan and for the private sector that can see the direction the government is taking with regard to economic development.

The NSEDP is a central part of the creation of the national budget, although not all expenditures are contained in the budget and of the dialogue with development partners. While not perfect and largely silent on issues related to fundamental values as explained above, it has been the foundation of the national development strategy through the recent period of successful, rapid GDP growth.

Overall, based on this detailed analysis of the NSEDP – and notwithstanding certain shortcomings and omissions - it is considered that the Plan can be used as the basis for programming of EU aid in the context of the Joint EU Transition Strategy 2014-2015.