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Statement by Mr. Ismael on the
Lao People's Democratic Republic
Executive Board Meeting 86/1
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1. During the First Five-year Plan (1981-84), the growth performance of the economy compared favorably with most developing countries at similar stage of economic development, despite the relatively unfavorable world economic environment and weak commodity prices. The average growth rate for the period was more than double the annual rate of increase in population, implying a significant improvement in the standard of living of the people. This achievement was accompanied by relatively stable current account deficits in 1981 and 1982, and by moderately higher deficits thereafter. Notwithstanding these achievements, an area of considerable concern for the authorities has been price developments where inflation rate of more than 50 percent per annum was envisaged.
2. The Laotian economy in 1985 continued to remain buoyant, with an expected growth rate of around 6 percent. It was largely as a result of favorable weather conditions that agricultural output is expected to register an impressive rate for the second consecutive year while the reduction of shortages of imported inputs through a proper streamlining of convertible foreign exchanges allocation was mainly responsible for a marked recovery in the output of industrial sector from a depressed state in the previous year. The increase in paddy production from 1.3 million tons in 1984 to 1.4 million tons in 1985, which is the target of the First Five-Year Plan, is viewed with optimism in terms of self-sufficiency goal in food grain production. The authorities recognize, however, that the consolidation of food self-sufficiency is conditioned upon further improvements in agricultural productivity and the adoption of the market-oriented pricing and incentive schemes. It is to be noted in this respect that certain progress has been made for the last three years in a number of areas as evidenced by the promotion of natural fertilizer usage, the introduction of suitable weed control and better planting techniques, and a more flexible policy regarding the structure of procurement and official retail prices in a number of commodities.
3. In the industrial sector, output rebounded strongly in 1985 from the decline experienced in the previous two years. Food and agro-industries, manufacturing, construction and mining are estimated to have grown by 57, 96, 461, and 19 percent, respectively. The aims of the authorities for the manufacturing sector, whose outputs are mainly geared towards satisfying domestic needs, primarily center around raising productivity and capacity utilization rate from the presently low level. Some policy measures have partially been put in place--in particular, the decentralization of public enterprise management, the removal of price distortions, and the introduction of a work performance bonus scheme for workers. As regard to the mining sector where steady output increases of the last 3-4 years are notable and

development prospects appear promising, the authorities have permitted exports to the convertible area in addition to the normal channel of exports to the nonconvertible area. The prospective expansion of markets in the convertible area for mineral exports, in combination with Lao's ample unexploited mineral resources, could provide opportunities for the authorities to strengthen the long-term development plan for this industry.

4. After a significant ease in price pressure in 1984, the price trend in 1985 was once again worrisome. The factors underlying such developments were the sharp adjustments in the official prices and continued monetary expansion. Price policies initiated by the authorities led to upward adjustments of rice prices, electricity charges, and bus fare. Monetary expansion, however, is expected to slow down as envisaged in the deceleration of cash in circulation from 41 percent per annum in 1984 to around 32 percent for the year ended June 1985.

5. The overall budget deficit in 1984 amounted to 3.4 billion kip, slightly higher than the deficit of 3.2 billion kip in 1983. Government revenue in 1984 as a proportion of GDP remained roughly at the same level as in 1983, whereas the proportion of expenditures dropped to 20 percent from 29 percent in the previous year, largely reflecting the continuous slowdown of capital outlays in relation to GDP. To a certain extent, total revenue was adversely affected by a less than anticipated transfers from public enterprises as a result of the lag in adjustments of official prices relative to costs. This shortfall was, however, partly offset by steep increases in profit and turnover taxes, following the improvement in collection and the adoption of the parallel market exchange rates for the evaluation of import levies. As traditionally practiced over the years, the budget deficit in 1984 was entirely financed by external borrowings and grants rather than by borrowings from the domestic banking system. Concerning the budgetary outlook in 1985, a widening deficit to 4.3 billion kip is expected as it appears that the budgeted expenditures are relatively high compared to the projected revenue. Since the government does not intend to rely on borrowings from the domestic banking system, the anticipated deficit would require an increase of 26 percent in the external borrowings and grants.

6. The external position of the Laotian economy remained fundamentally weak in 1985. According to the estimates, current account deficit was projected at about US\$95 million, an increase of US\$10 million over the previous year. The outturn reflects the slowdown of export growth from 10.5 percent in 1984 to 5.5 percent in 1985, while the growth of import accelerated from 3 percent to 6 percent per annum in response to sharp rises in industrial output and construction activities. An increase in exports to the convertible area appeared encouraging, but this was partly offset by a drastic drop in exports to the nonconvertible area. As the problems facing export are commonly known by the authorities--e.g., short supply of imported inputs, lack of managerial skills, insufficient infrastructure, lack of product diversification, and a distorted price structure--it is of considerable interest therefore to note

that some of these obstacles will be seriously tackled under the forthcoming Second Five-Year Plan (1986-90). In addition, the authorities are of the view that a substantial depreciation of the kip is essential to stimulate exports.

7. In the formulation of the medium-term development strategy in the Second Five-Year Plan, the authorities intend to address the problems of structural rigidities in a number of areas with the view to achieve their stated objectives--namely self-sufficiency in food, agricultural output diversification, adequate infrastructure, full utilization of natural resources, and industrialization based on domestic raw materials. For the past few years, some of the needed policy adjustments have been gradually carried out, though much remains to be done. Of notable importance is the move towards more realistic procurement and official retail prices and the elimination of consumer subsidies. The authorities undertook a significant step in 1985 by making an upward adjustments in deposit and lending rates in conjunction with the introduction of longer term deposits, while exchange rate for the private inward remittances was also adjusted. With respect to the public sector's management efficiency, greater autonomy has been granted to all public enterprises in connection with decisions on investment, production, employment, and to a limited extent, prices. Apart from this flexibility, profitability is now an important performance criterion for the evaluation of public enterprise management. These policy adjustments, coupled with future improvement in production efficiency and transportation network, are expected to put the economy on a better position to cope with unforeseen adverse circumstances.

On behalf of my Laotian authorities, I wish to express our appreciation to the staff for its comprehensive report and balanced views on the economy.