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April 25, 1989

To: Members of the Executive Board

From: The Secretary

Subject: Lao People's Democratic Republic - 1989 Staff Report
on the Interim Article IV Consultation Discussions

It is not proposed to bring the attached 1989 staff report on the interim Article IV consultation discussions with the Lao People's Democratic Republic to the agenda of the Executive Board for discussion unless an Executive Director so requests by the close of business on Tuesday, May 2, 1989. In the absence of such a request, the draft decision that appears on page 26 will be deemed approved by the Executive Board, and it will be so recorded in the minutes of the next meeting thereafter.

Mr. Tilakaratna (ext. 7614) or Ms. Milne (ext. 7328) is available to answer technical or factual questions relating to this paper.

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INTERNATIONAL MONETARY FUND

LAO PEOPLE'S DEMOCRATIC REPUBLIC

1989 Staff Report on the Interim Article IV Consultation Discussions

Prepared by the Asian Department

(In Consultation with the Exchange and Trade Relations, Fiscal, Legal,
Treasurer's Departments and the Bureau of Statistics)

Approved by Douglas A. Scott and A. Basu

April 21, 1989

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Lao People's Democratic Republic--Basic Data

	1985	1986	1987	1988 Est.	1989 Proj.
(Percentage change, unless otherwise indicated)					
<u>Growth</u>					
Real GDP 1/	9.1	7.1	-2.5	2.0	4.0
<u>Inflation</u>					
GDP deflator 1/	84.8	42.8	26.1	67.9	20.0
CPI (end of period)	114.7	35.0	6.6	32.6	20.0
<u>Central government budget</u>					
Revenue 2/	108.2	79.6	8.7	40.3	41.6
Total expenditure	135.4	34.6	11.2	168.9	55.4
Current account (percent of expenditure)	3.8	13.9	13.8	1.9	4.7
Overall deficit (percent of expenditure)	-47.8	-30.3	-31.8	-64.4	-67.6
Foreign borrowing (percent of expenditure)	48.6	31.1	32.6	66.2	67.6
<u>Money and credit (end of year) 3/</u>					
Domestic credit	32.1	59.3	70.1	38.3	...
Total liquidity	34.8	70.0	79.0	42.5	46.9
Of which: Currency in circulation	(41.1)	(64.9)	(101.2)	(65.4)	(57.5)
Interest rate (1-year deposit)	9.6	9.6	9.6	14.0	...
(In millions of U.S. dollars, unless otherwise indicated)					
<u>Balance of payments 4/</u>					
Exports	53.6	55.0	62.1	57.6	63.8
Convertible zone	34.6	39.4	33.0	36.6	40.8
Nonconvertible zone	19.0	15.6	29.1	21.0	23.0
Imports	-193.2	-185.7	-216.2	-188.0	-232.6
Convertible zone	-77.6	-78.4	-81.7	-90.4	-133.6
Nonconvertible zone	-115.6	-107.3	-134.5	-97.6	-99.0
Current account	-143.3	-121.0	-144.7	-131.1	-179.0
Convertible zone	-41.5	-25.8	-35.3	-50.0	-98.0
Nonconvertible zone	-101.8	-95.2	-109.4	-81.1	-81.0
Overall balance (convertible zone)	20.8	8.7	-11.3	-4.5	-14.5
Current account ratio 5/	-191.3	-152.6	-163.8	-162.3	-205.2
<u>Reserves (end of year)</u>					
Gross official reserves	25.9	32.6	21.2	16.7	16.7
(in weeks of imports)	7.0	9.1	5.1	4.6	3.7
(in weeks of imports from convertible areas)	17.4	21.6	13.5	9.6	6.5
Net official reserves	22.9	31.5	20.2	15.7	15.7
<u>External debt (end of year)</u>					
Convertible	502.6	604.1	714.5	826.1	951.7
Of which: Use of Fund credit	160.9	171.8	178.7	195.1	244.3
Nonconvertible	2.1	--	--	--	--
	341.7	432.3	535.8	631.0	707.4
<u>Debt service ratio 5/</u>	22.3	15.9	15.8	15.6	20.3
<u>Effective exchange rate (percentage change; end of period)</u>					
Nominal 6/	-67.0	-8.7	-75.6	-20.4	-3.0 7/
Real 8/	-24.1	3.8	-73.9	22.3	...
(In millions of SDRs, unless otherwise indicated)					
<u>Use of Fund Resources</u>					
Tranche					
Repurchases	6.4	1.9	--	--	--
<u>Trust Fund and SAF</u>					
Trust Fund payments	2.2	2.6	2.5	2.6	1.5
SAF	--	--	--	--	--
<u>Present quota</u>			29.3		
<u>Exchange rate</u>					
Exchange rate regime				Managed float	
Present rates 9/				KN 470/US\$1 (buying)	
				KN 475/US\$1 (selling)	

Sources: Data provided by the Lao authorities; and staff estimates and projections.

1/ Official estimates of net material product, that are adjusted by the staff to include depreciation and services in order to approximate GDP, are considered to be substantially understated. Historical estimates of nominal GDP are biased by the use of unrealistic prices and exchange rates. Real and nominal GDP estimates should be interpreted cautiously.

2/ Official grants are treated as a financing item.

3/ From end-1987, monetary data reflect an improved classification of accounts and the valuation of foreign currency transactions at current market rates.

4/ Starting in 1988, trade data are based on customs data. Prior to that, trade was estimated based on flows through the banking system.

5/ As a ratio of exports of goods and services.

6/ Based on a currency basket comprising the currencies of the five most important partner and competitor countries of the Lao P.D.R. A minus sign indicates depreciation.

7/ February 1989.

8/ The nominal effective exchange rate adjusted for the CPI of Lao P.D.R. relative to the consumer price developments in the five partner and competitor countries. A minus sign indicates depreciation.

9/ February 1989.

I. Introduction

The interim Article IV consultation discussions with the Lao People's Democratic Republic were held in Vientiane during February 16-March 2, 1989. The mission met with the Vice-Ministers of the Ministries of Economy, Plan and Finance; Commerce; and Agriculture; the Vice-Presidents of the State Bank; Deputy Director of the Bank for Foreign Trade; and General Managers of several state corporations, as well as other senior government officials. The staff team comprised Mr. Tilakaratna (Head), Ms. Milne, Ms. Kappagantula (all ASD), Messrs. Luu (STA), Lutz (FAD) and Riess (ETR), and Mrs. Kime (secretary, ASD). ^{1/}

Lao P.D.R. continues to avail itself of the transitional arrangements under the provisions of Article XIV. It imposes restrictions on payments and transfers for current international transactions and maintains multiple currency practices, which are subject to approval under Article VIII, Sections 2(a) and 3. A description of the exchange and trade system is contained in Annex I of this paper. Lao P.D.R. is eligible for access to the structural adjustment facility.

II. Background and Recent Economic Developments

Lao P.D.R. is a small, sparsely populated country, with one of the lowest per capita incomes in the world. Situated between Thailand and Viet Nam, it is also bordered by Democratic Kampuchea to the south and by Burma and China to the north. Its landlocked position and mountainous terrain, covering about 70 percent of the country, are natural impediments to external and internal trade. These have been exacerbated by the inadequate and poorly maintained transportation network and by the lack of communications infrastructure. The country, nevertheless, is well endowed with natural resources including fertile land, timber, mineral reserves such as iron ore, limestone, potash, gypsum, coal, gold, and semiprecious stones, and substantial hydroelectric potential.

The population, estimated at less than 4 million, is concentrated mainly in rural areas, with only about 15 percent residing in five urban centers. An estimated 80 percent of the population rely on subsistence agriculture, animal husbandry, and forestry for their livelihood. In the mountain areas, the nomadic hill tribes engage in slash-and-burn agricultural practices that have resulted in deforestation and soil erosion, giving rise to wider environmental concerns. Industrial activity is limited. The main industries are the generation of

^{1/} Messrs. Luu and Lutz preceded the mission by several days to prepare the monetary and fiscal data. The staff was also assisted by the staff of a parallel World Bank mission that was preparing documentation for a possible IDA Structural Adjustment Credit (SAC).

hydroelectricity, rudimentary processing of agricultural and forestry products, light industry, and handicrafts.

Following a protracted civil war that was waged intermittently from the 1950s until 1973, the Lao People's Democratic Republic was established in 1975 and the monarchy abolished. The economy was restructured along centrally planned lines, with the private sector replaced by state enterprises and cooperatives. In contrast to other centrally planned economies, however, agricultural production remained dominated by small family farms. Land tenure continued to reflect the traditional pattern: land ownership was vested in the state, but farmers possessed rights of usufruct and inheritance. Nevertheless, farmgate prices and trade in agricultural products were controlled by the State and trade between provinces was restricted to encourage regional rice self-sufficiency. The latter policy was supported by substantial investments in irrigation facilities in the rice-deficit areas of the northern plain. These projects and the development of hydroelectric generating capacity absorbed most of the country's development budget, to the relative neglect of other sectors of the economy as well as of the maintenance and expansion of social and economic infrastructure. Until recently, transactions in rural areas were mainly in the form of barter, with the monetized economy concentrated in the urban areas. Only a small proportion of public sector wages was paid in cash, with the remainder in the form of purchase book entries usable only in state shops.

The economy was characterized by low domestic saving, a distorted incentive structure, centralized control over investment and production decisions, and barriers to internal and external trade and to labor mobility. Inappropriate official prices and exchange rates led to the emergence of parallel markets for goods and foreign exchange. These parallel markets became increasingly important as inflation ^{1/} accelerated, averaging 55 percent in the 1981-85 period. Supply shortages worsened while demand pressures increased, reflecting mainly expansionary fiscal policy, accommodated by lax monetary policy. Although the Government had little direct recourse to bank credit, state enterprises had to transfer targeted amounts to the budget regardless of performance. In turn, these enterprises borrowed heavily from the banking system to finance current operations.

^{1/} The price index was constructed by Fund staff a number of years ago on the basis of selected free and official market prices. The commodity weights were revised following the freeing of prices in October 1988. A consumer survey is being undertaken, with bilateral technical assistance, and a new index is expected to be implemented during 1989. Information on price movements is maintained only for the Vientiane area. Since the capital is located in a rice-deficit area, fluctuations in measured inflation may reflect short-run disruptions in supplies of this staple. Longer trends, however, can be viewed as a proxy for price developments in the rest of the monetized economy.

The overvalued official exchange rate hindered export growth, encouraged unrecorded border trade and contributed to the substitution of Thai baht and U.S. dollars for kip (KN) in domestic transactions. Gross reserves reached a low of \$11 million (3 1/2 weeks of total imports) at end-1984. By 1985, the current account deficit had widened to \$143 million (192 percent of exports of goods and services), almost three fourths of which was with the nonconvertible currency area. External debt service had risen to over one fifth of current external receipts. Faced with large pending debt repayments to the U.S.S.R. that it was unable to meet, Lao P.D.R. negotiated a deferment of this debt until 1991. ^{1/}

1. Structural transformation, 1985-88

During 1985, the authorities introduced a number of measures aimed at redressing the mounting internal and external disequilibria. Some official prices were brought closer to prevailing parallel market prices. Special exchange rates of KN 270 and KN 300 per dollar were introduced for private inward remittances to Lao nationals and for transactions of mixed enterprises, respectively. The commercial exchange rate, at which most transactions continued to take place, was devalued from KN 35 to KN 95 per U.S. dollar, still substantially overvalued compared with the parallel market rate of KN 424 per U.S. dollar prevailing at end-1985.

In late 1985, the Government launched the New System of Economic Management (NSEM) in conjunction with the Second Five-Year Plan (1986-91). Initially, the NSEM focused on improving the efficiency of state enterprises by increasing their financial and managerial autonomy. The Government abandoned production targeting and introduced profitability as a criterion for evaluating enterprise performance. A limited number of enterprises were permitted autonomy to determine employment, production, and investment levels; adjust prices taking into account cost as well as social considerations; and set wages. Subsequently, the scope of the NSEM was progressively widened and supported by measures aimed at strengthening the role of the private sector and increasing reliance on market forces. In 1986-87, the principle of operating autonomy was extended to a large number of viable state enterprises. However, state enterprises were still required to transfer targeted amounts to the budget while receiving budgetary subsidies and enjoying liberal access to bank credit. Procurement prices were freed in mid-1987, and transactions shifted from barter to cash payment. Most retail prices, however, remained subject to government control, and subsidies were

^{1/} As described in the staff report for the 1987 Article IV consultation (SM/88/23, 1/19/88), page 16.

maintained on a wide range of consumer goods available to public sector employees. 1/

During 1986-87 substantial progress was achieved in liberalizing internal and external trade. In early 1987, trading companies were consolidated and provincial trade restrictions eliminated. Transport, which was a monopoly of state and provincial enterprises, was opened to the private sector. Mixed (joint public and private companies) and private companies were permitted to trade domestically and abroad in most goods. Exports of "strategic" goods, 2/ mainly those needed to comply with trade contracts with the nonconvertible currency area, continued to be reserved for state trading companies.

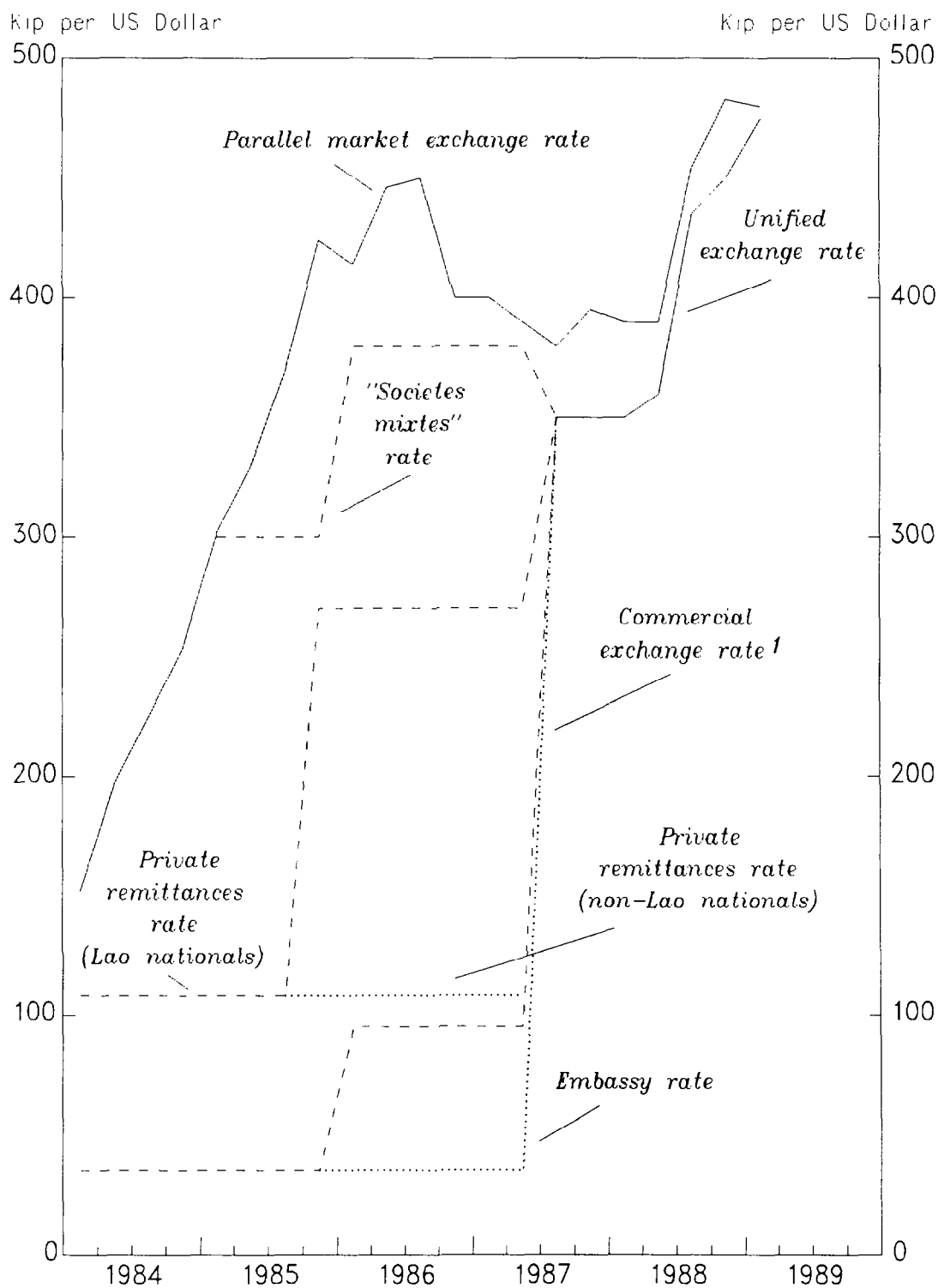
The exchange system was rationalized further to permit additional transactions to take place at rates closer to that prevailing in the parallel market. As border trade normalized and as the parallel market became legally tolerated, and an increasing share of transactions were shifted to it, the parallel market exchange rate gradually appreciated. In September 1987 the six official transaction exchange rates were unified at KN 350 (buying) and KN 385 (selling) per U.S. dollar, close to the prevailing parallel market rate of KN 390 per U.S. dollar (Chart 1). The representative rate of KN 10 per U.S. dollar, used to value foreign transactions with multilateral institutions and in selected monetary and fiscal accounts, remained unchanged.

During 1988, the reform process gained momentum. Most production, distribution and prices were decontrolled. Private sector participation was permitted in most sectors, including trade in most strategic goods. The Lao Food Corporation, which had a monopoly in the procurement and distribution of rice, was liquidated. Treatment of public and private enterprises was equalized in the areas of taxation and access to bank finance. In March, it was decreed that retail prices, except for those of electricity, water, post and telecommunications, minerals, and domestic air transport, were to be decontrolled. By October, all but these retail prices had been freed and reflected market conditions. To partially compensate for higher prices, public sector wages were increased and enterprises raised the share of wages paid in cash, thereby increasing private discretionary control over spending. A new foreign investment law, providing incentives and guarantees for foreign and joint direct investment, was promulgated at midyear.

1/ Consumption subsidies to civil servants and to public enterprise employees in 1987 were estimated by the staff to equal 115 percent and 85 percent of the average wage, respectively. The cost of those subsidies was reflected in the accounts of the now liquidated Lao Food Corporation.

2/ Coffee, tobacco, cardamom, benzoin, sticklac, logs, processed wood, rattan, cattle, wild animals, minerals, and other special goods.

CHART 1
LAO, P.D.R.
EXCHANGE RATES, 1984-89



Source: Data provided by Lao authorities.

¹ The commercial rate was the rate at which most official transactions took place up until September 1987.

The process of granting autonomy to public enterprises was accelerated and, by end-1988, only utilities, and those corporations that were unable to produce financial accounts or were deemed nonviable, remained subject to ministerial or provincial intervention. Recognizing these operational changes, a new tax system was implemented with the 1988 budget. ^{1/} Profit taxes, ranging from 20-85 percent, were introduced, replacing the previous system of budgetary transfers and subsidies. Rates are set depending on the initial profitability of the sector and the socially desirable characteristics of the products. Taxes were also imposed on the profits accruing from exported goods, at rates ranging from 0-80 percent, replacing the previous ad valorem tax. While rates are uniform within each sector, profits accruing from the production of some goods are taxed less when exported than when sold domestically while the opposite applies to other goods. A timber harvesting tax was imposed and new turnover taxes were placed on businesses engaged in the handicraft, construction, transport, trade, and services sectors. From March 1988, import duties are calculated on the basis of the unified official exchange rate and not at the representative rate. At the same time, maximum duty rates were lowered from 200 to 70 percent. Generous direct tax incentives were provided for investment in new activities as well as in rehabilitated public enterprises.

The Government reordered its expenditure priorities during 1988. Subsidies to civil servants and consumer subsidies were eliminated, except for those items whose prices remain subject to control, as were subsidies to autonomous public enterprises. Civil servant wages were raised to partly offset the impact of higher prices; nevertheless, real incomes fell. Steps were taken to rationalize the level of employment through early retirement and provision of separation incentives. These actions resulted in a sizable reduction in central government staff.

A wide-ranging reform of the financial system was initiated in early 1988. The central and commercial banking functions of the State Bank are being separated, with technical assistance provided by the Fund and the Asian Development Bank. During 1988, two large branches of the State Bank in Vientiane were constituted as independent commercial banks. Efforts were also intensified, with Fund assistance, to improve the classification, coverage and timeliness of monetary data; in February 1989 a new reporting format was introduced. ^{2/}

Interest rate policy has also been modified. The distinction between private and public sector deposit and lending rates was eliminated. Generally, however, the private sector has made only limited use of the banking system, with public enterprises accounting for the bulk of loans and deposits. In October 1988, deposit and loan

^{1/} A detailed description of the new tax system is provided in Annex II.

^{2/} A description of the new reporting format is presented in Annex III.

rates were raised by 3 to 6 percentage points, respectively (Table 16, Annex IV). Rates, however, remained negative in real terms and those on selected long-term loans remained lower than for short-term loans. New high-interest deposit and loan instruments were also introduced to allow the newly formed commercial banks to compete with the informal curb market. Ceilings of 12.5 percent per month on deposits and 15 percent per month on loans were established by the State Bank, compared with a monthly rate of 20 percent for noncollateralized loans in the curb market. Only those funds mobilized by the new deposit accounts are permitted to be lent at the higher monthly rate. From January 1989, the deposit and loan rates presently offered by the two commercial banks on the new instruments are 3 and 6 percent per month, respectively.

In the external sector, the monopolistic position of state trading corporations, except for trade with the nonconvertible currency area, was eliminated. Exporters were allowed to retain their foreign exchange earnings and import licenses were granted more liberally to public enterprises and cooperatives, and to mixed and foreign trading corporations. During the year, the exchange rate has continued to be managed flexibly. The spread between the official buying and selling rates was reduced to below 2 percent in September 1988, thereby eliminating a multiple currency practice. The official unified rate was adjusted in line with movements in the parallel market rate and at end-1988 the spread between these rates was only 6 percent. ^{1/} In February 1989, the official exchange rate was devalued to KN 470 (buying) and KN 475 (selling) per U.S. dollar compared to parallel market rates of KN 480 (buying) and KN 487 (selling) per U.S. dollar, thereby reducing the spread between the mid-point rates to about 2 1/2 percent. The depreciation of the kip has substantially reversed the loss of international competitiveness, as measured by the real effective exchange rate, that had taken place during the early 1980s (Chart 2). The representative rate of KN 10 per U.S. dollar established in cooperation with the Fund for valuation purposes has not been changed.

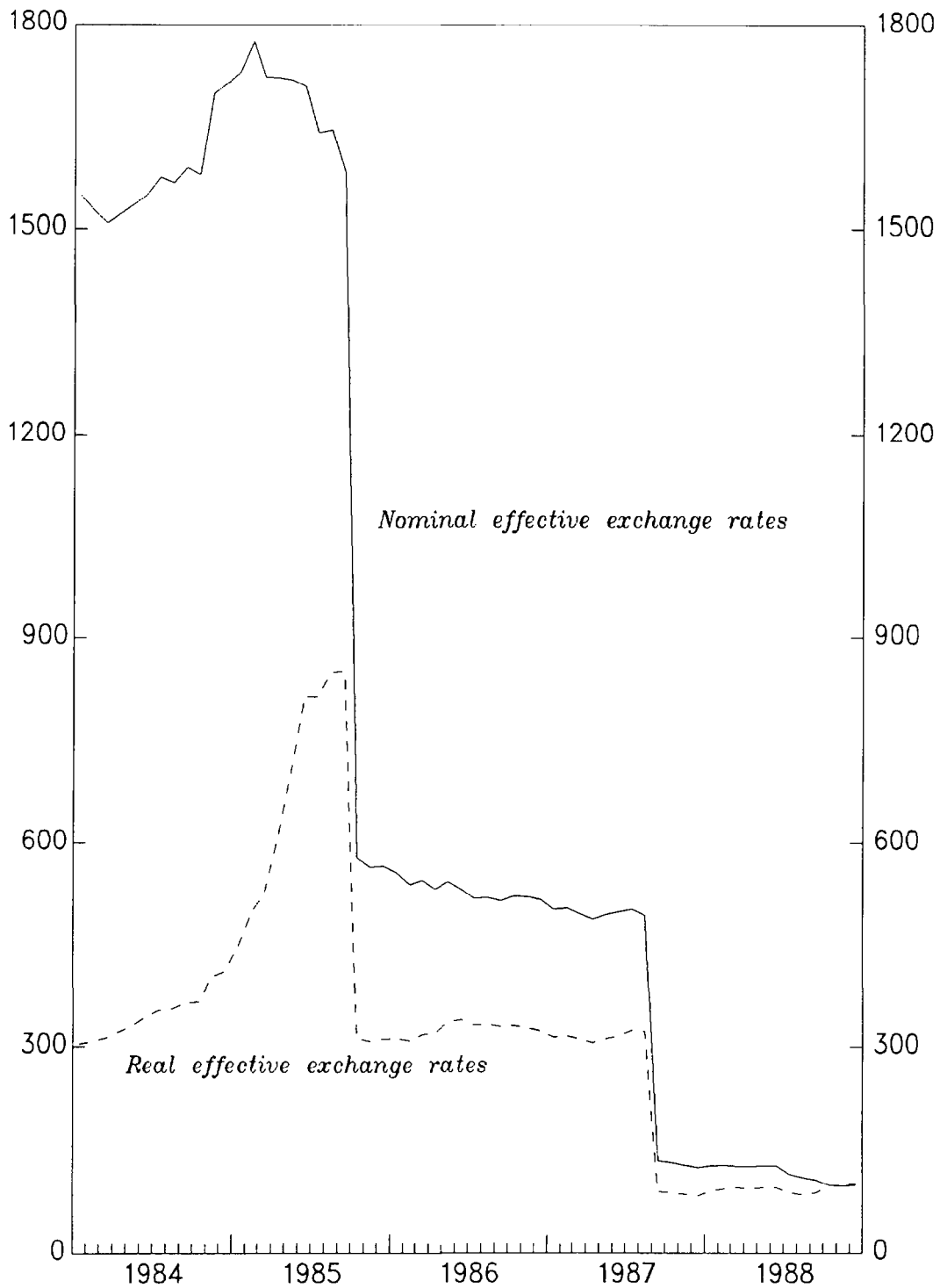
2. Economic developments, 1988

The reform process began to yield encouraging results in 1986 when real growth ^{2/} reached 7.5 percent and inflation fell to 35 percent

1/ As measured by the difference between the mid point of the official rates and the buying rate on the parallel market. Information on the parallel market selling rate for this period is not available.

2/ National income accounts are based on official estimates of net material product (NMP). These are adjusted by Fund staff to include depreciation and some service and private sector transactions in order to approximate GDP. Trends in real and nominal GDP have to be interpreted cautiously because of the earlier practice of targeting production and because of the use of unrealistic prices and exchange rates. Moreover, NMP is thought to be substantially understated, as it excludes a large element of subsistence agriculture and private sector activities. Expenditure data are not prepared by the authorities.

CHART 2
LAO, P.D.R.
NOMINAL AND REAL EFFECTIVE EXCHANGE RATES, 1984-88¹
(October 1988 = 100)



Sources: Data provided by Lao authorities; IFS and staff estimates.

¹ Based on a currency basket comprising the currencies of the five most important partner and competitor countries of the Lao P.D.R. A downward movement indicates a depreciation.

(Chart 3). The impact of the reforms on macroeconomic performance in 1987-88, however, has been masked by a protracted drought which adversely affected agricultural production and the generation of hydro-electricity. Real GDP fell by 2 1/2 percent in 1987 but increased by 2 percent in 1988, notwithstanding the drought and a decline in public sector investment because of strong growth in private sector activity. In 1988, price decontrol and the depreciation of the kip contributed to an acceleration of inflation to 33 percent, from 7 percent recorded in 1987. Rice prices on the parallel market rose only moderately despite the continued drought because stocks were released to the market following the freeing of prices.

The fiscal situation deteriorated in 1988, following significant improvements in 1986-87. Public enterprises, whose financial position had been strengthened by increased autonomy in 1986-87, were faced with rising wage payments, increased prices of domestically produced inputs and higher import costs related to exchange rate unification--factors which lowered enterprise profit margins. Earnings of the electricity corporation were adversely affected by the drought for the second consecutive year.

The budget position weakened and the current account surplus dropped to only 2 percent of total expenditures from 14 percent averaged in 1986-87 (Table 1). ^{1/} Budgetary revenues rose, although less than had been anticipated when the new tax system was introduced. Current expenditures also increased. The domestic value of imported materials and supplies and interest payments rose as the accounting exchange rate was raised from KN 95 per U.S. dollar used in 1986-87 to the unified official rate. The wage bill more than doubled, notwithstanding a

^{1/} Analysis of recent budgetary developments is made difficult by the restructuring involved under the NSEM as well as by shortcomings in the fiscal accounts. Prior to 1988, foreign aid flows and expenditures financed by these receipts had been recorded at exchange rates that were substantially above parallel market and other market-related official exchange rates, thereby understating capital expenditures and the overall deficit. Debt service payments to nonconvertible creditors are not included in the budget and amortization payments to convertible creditors are included as current expenditures. In an attempt to overcome these shortcomings, the data in Table 1 include only interest payments in current expenditures and amortization is placed below the line. An adjusted overall deficit, estimated using exchange rates that would have prevailed if the real effective exchange rate in 1989 had been maintained in earlier years, is included as a memorandum item to facilitate intertemporal comparison of the stance of fiscal policy. These data indicate that in the 1985-87 period the budget deficit was understated by about 20 percent of GDP. In 1988, the adoption of a more realistic accounting exchange rate for the budget narrowed this discrepancy to less than 2 percent of GDP.

Table 1. Lao P.D.R.: General Government Budget, 1985-89

	1985	1986	1987	1988 Est.	1989 <u>1/</u> Proj.
(In millions of kip)					
Revenue	10,300	18,503	20,108	28,210	39,949
Nontax revenue	8,902	16,748	18,138	6,801	7,499
Of which: Transfers from public enterprises (net)	(7,761)	(14,940)	(16,498)	(2,928)	(2,850)
Tax revenue	1,398	1,755	1,970	21,409	32,450
Of which: Public enterprises	(690)	(881)	(1,145)	(18,250)	(27,456)
Expenditure	19,726	26,545	29,505	79,350	123,273
Current expenditure	9,542	14,813	16,025	26,722	34,170
Of which: Wages and salaries	(2,520)	(4,760)	(5,135)	(11,250)	(13,880)
Materials and supplies	(6,809)	(9,875)	(10,640)	(14,238)	(18,214)
Foreign interest <u>2/</u>	(186)	(133)	(190)	(984)	(1,726)
Capital expenditure <u>3/</u>	10,184	11,732	13,480	52,628	89,103
Overall deficit (-) <u>3/</u>	-9,426	-8,042	-9,397	-51,140	-83,324
Net financing	9,426	8,042	9,397	51,140	83,324
Change in net domestic bank credit <u>4/</u>	-164	-211	-222	-1,396	--
Net external borrowing and grants	9,590	8,253	9,619	52,536	83,324
(In percent of expenditures)					
Revenue	52.2	69.7	68.2	35.6	32.4
Current account surplus	3.8	13.9	13.8	1.9	4.7
Overall deficit (-) <u>3/</u>	-47.8	-30.3	-31.8	-64.4	-67.6
(In percent of GDP)					
Revenue	16.4	19.3	17.1	14.0	15.9
Expenditure	31.5	27.7	25.1	39.4	49.0
Current expenditure	(15.2)	(15.5)	(13.6)	(13.3)	(13.6)
Capital expenditure <u>3/</u>	(16.3)	(12.3)	(11.5)	(26.1)	(35.4)
Current account surplus	1.2	3.9	3.5	0.7	2.3
Overall deficit (-) <u>3/</u>	-15.1	-8.4	-8.0	-25.4	-33.1
Memorandum items					
Overall deficit at equilibrium exchange rate (In percent of GDP) <u>5/</u>	-34.7	-28.8	-29.6	-26.6	-33.1
Exchange rate (KN/\$)	75	95	95	400	...

Sources: Data provided by the Lao authorities; and staff estimates and projections.

1/ Capital expenditures and overall deficit figures assume that the balance of payments financing gap is filled.

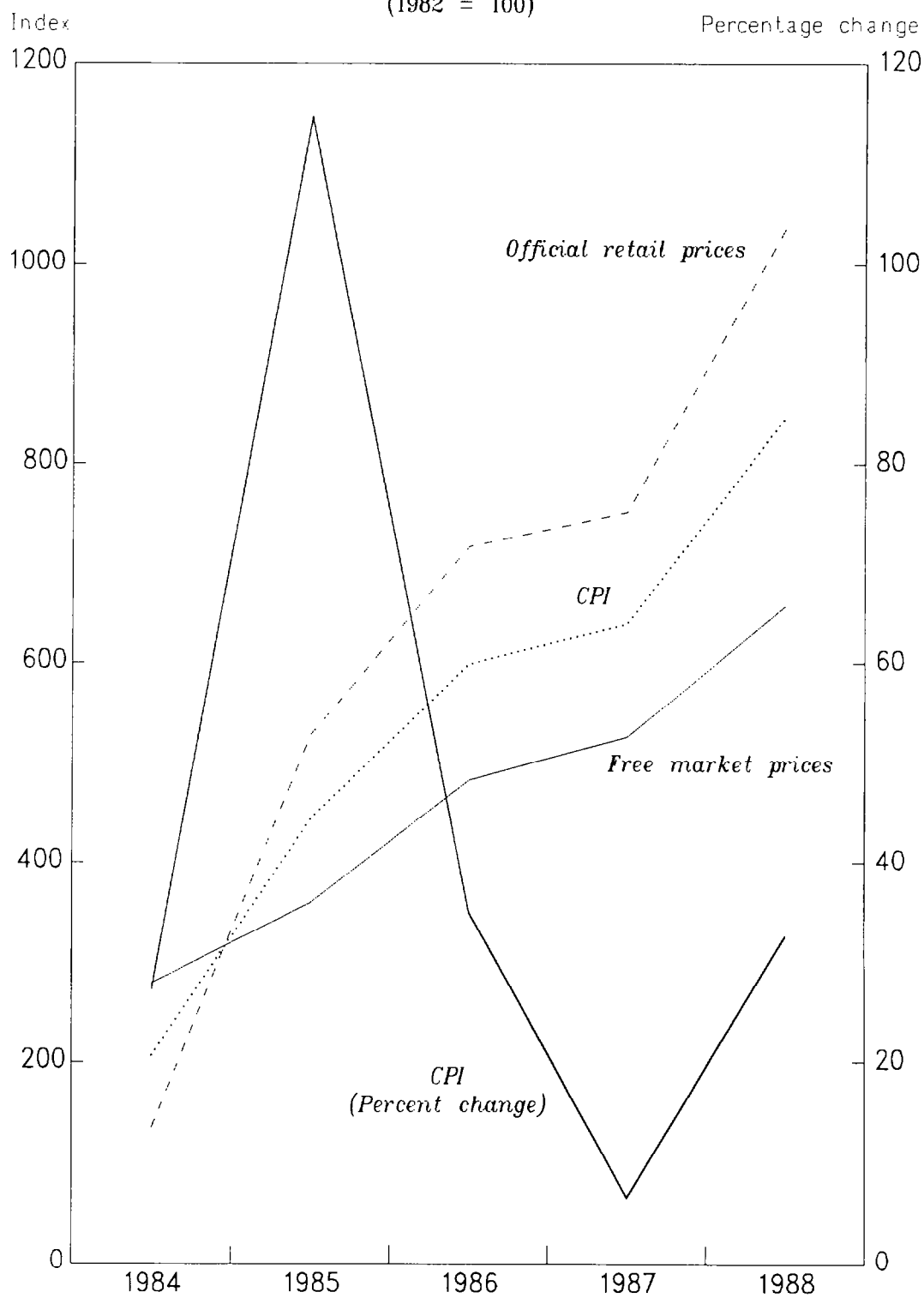
2/ Estimated on the basis of balance of payments data. Convertible currency debt service is not maintained separately for interest and amortization in the budget accounts. Amortization payments for nonconvertible debt are not covered in the budget but are included in this presentation.

3/ The budget investment and financing figures are understated to the extent that an over-valued exchange rate was used to value foreign assistance; that aid from the nonconvertible currency area was valued using rates different from those in the external accounts; and that some foreign technical assistance is not included.

4/ Reflects changes in deposits prior to 1988; thereafter this reflects changes in net domestic credit.

5/ This figure estimates the fiscal situation if all foreign assistance that is identified in the external accounts is included in the budget at the equilibrium rate and tax proposals are implemented as discussed.

CHART 3
LAO, P.D.R.
PRICES, 1984-88
(1982 = 100)



Sources: Data provided by Lao authorities; and staff estimates.

substantial reduction in staffing. The Government raised salaries to compensate, in part, for the loss of subsidies pursuant to the price liberalization. In addition, separation grants, equivalent to one year's salary, were introduced to encourage civil servants to take early retirement or seek employment in the private sector.

Public sector investment was sharply higher in 1988 also because of valuation effects, but is estimated to have fallen by about one-third in real terms. The reduction in the current surplus, plus a drop in commodity assistance from the nonconvertible currency area, contributed to a decline in counterpart funds available for projects. The overall deficit as a proportion of total expenditures was 64 percent, more than double that recorded in 1986-87. As in the past, it was fully financed by foreign aid; the Government's net use of bank credit declined.

During 1988, monetary policy, which had accommodated public enterprise credit needs in 1986-87, was tightened. The rate of growth of credit decelerated to 38 percent, ^{1/} from 70 percent in 1987 (Table 2). With the increased use of money in domestic transactions, the declining trend in velocity, in evidence since 1986, was sustained. Nevertheless, the decline in export earnings contributed to slowing the growth of total liquidity to 43 percent, about half that recorded in 1987.

The external position weakened in 1987-88 (Table 3). ^{2/} Drought reduced hydroelectricity exports in both years and coffee exports in 1988. Earnings were also affected by a lower export unit price of electricity which was negotiated with Thailand in 1987 *pari passu* with the drop in world petroleum prices. Imports, which had increased sharply in 1987 following trade liberalization, declined in response to the tighter monetary policy and the depreciation of the kip. The direction of trade also changed significantly, from the nonconvertible to the convertible

^{1/} This figure may overstate the increase in credit availability. Credit extended by the Bank for Foreign Trade, which accounts for 60 percent of total credit, is in part denominated in foreign currency. The new monetary reporting system values foreign transactions at the prevailing unified official exchange rate starting in 1988, rather than at the representative rate used previously. It has not yet been possible to separate the effect of the valuation adjustment on credit aggregates.

^{2/} Comparison of trends in external data between 1987 and 1988 is complicated by the change in methodology used in compiling balance of payments data. Starting in 1988, trade flows are based on customs data and estimates of current and capital transactions are based on residency criterion. Earlier data are based on information on payment flows through the Bank for Foreign Trade and clearly defined residency criterion were not used. Work is proceeding to revise the 1984-87 data accordingly.

Table 2. Lao P.D.R.: Monetary Survey, 1985-88

	1985 <u>1/</u>	1986 <u>1/</u>	1987 <u>1/</u>	1987 <u>2/</u>	1988 <u>2/</u>
(In millions of kip; end of period)					
Net foreign assets	147	238	-412	286	1,530
Foreign assets	259	326	212	10,948	13,281
Foreign liabilities <u>3/</u>	-113	-88	-624	-10,662	-11,751
Net domestic assets	2,133	3,639	7,350	15,609	21,134
Domestic credit	2,717	4,329	7,364	17,964	24,852
Net claims on Government	-273	-484	-706	2,523	1,127
Claims <u>3/</u>	--	--	--	3,586	4,965
Deposits	-273	-484	-706	-1,063	-3,838
State enterprises <u>4/</u>	2,740	4,044	6,935	15,331	22,855
Private, cooperatives, and mixed sector	250	769	1,135	110	870
Other items (net) <u>5/</u>	-584	-691	-14	-2,355	-3,718
Liquidity (M2) <u>4/</u>	2,280	3,876	6,938	15,894	22,663
Currency outside banks	635	1,047	2,107	2,091	3,486
Demand deposits	1,591	2,734	4,719	4,797	8,618
Time and savings deposits	54	95	112	112	1,084
Foreign currency deposits	--	--	--	8,893	9,475
Of which: Margin deposits for imports				(3,683)	(3,070)
(Percentage change)					
Net foreign assets	-467.9	61.8	-273.4	...	435.0
Domestic credit	32.1	59.3	70.1	...	38.3
Net claims on Government	(150.5)	(77.3)	(-9.9)	(...)	(-55.3)
State enterprises	(34.9)	(47.6)	(71.5)	(...)	(49.1)
Private, cooperatives, and mixed sector	(86.6)	(207.6)	(47.6)	(...)	(690.9)
Liquidity (M2)	34.8	70.0	79.0	...	42.6
Memorandum items:					
Velocity (GDP/average liquidity)	15.8	15.6	8.8	7.4	5.2
Currency/total liquidity	27.9	27.0	30.4	13.2	15.4

Sources: Data provided by the Lao authorities; and Tables 17 and 18 of Annex IV.

1/ Foreign currency accounts valued at KN 10 per U.S. dollar.

2/ Beginning end-1987, foreign currency accounts are valued at current market rates. In addition, the classification and coverage of accounts has been improved.

3/ Excludes Trust Fund loans; these loans are included as foreign financing of the budget.

4/ Adjusted, for analytical purposes, to include written-off loans by the State Bank to state enterprises.

5/ The large increase in "other items, net" in the new presentation mainly reflect valuation adjustment accounts.

Table 3. Lao P.D.R.: Balance of Payments, 1985-89 1/

	1985	1986	1987	1988 Est.	1989 Proj.
(In millions of U.S. dollars)					
Exports, f.o.b.	53.6	55.0	62.1	57.6	63.8
Convertible area	34.6	39.4	33.0	36.6	40.8
Nonconvertible area	19.0	15.6	29.1	21.0	23.0
Imports, c.i.f.	-193.2	-185.7	-216.2	-188.0	-232.6
Convertible area	-77.6	-78.4	-81.7	-90.4	-133.6
Nonconvertible area	-115.6	-107.3	-134.5	-97.6	-99.0
Services and private transfers (net)	-3.8	9.6	9.4	-0.6	-10.2
Services (net)	-7.3	5.9	5.9	-7.4	-17.7
Convertible area (net)	-2.1	9.5	9.9	-2.9	-12.7
Receipts	21.3	24.3	26.2	23.2	23.4
Payments	-23.4	-14.8	-16.3	-26.1	-36.0
Interest	(-2.5)	(-2.1)	(-2.7)	(-2.6)	(-4.4)
Technical assistance 2/	(-18.2)	(-9.5)	(-10.3)	(-21.4)	(-27.5)
Other	(-2.7)	(-3.2)	(-3.3)	(-2.1)	(-4.1)
Nonconvertible area (net)	-5.2	-3.6	-4.0	-4.5	-5.0
Private transfers (conv. area)	3.5	3.7	3.5	6.7	7.5
Current account (excluding grants)	-143.3	-121.0	-144.7	-131.1	-179.0
Convertible area	-41.5	-25.8	-35.3	-50.0	-98.0
Nonconvertible area	-101.8	-95.2	-109.4	-81.1	-81.0
Capital account	151.6	136.9	139.9	139.8	164.5
Convertible area	49.8	41.7	30.5	58.7	83.5
Official transfers	45.4	26.0	23.0	34.0	35.7
Long-term loans	1.1	12.1	4.0	15.5	34.4
Drawings	(12.1)	(20.8)	(13.4)	(23.7)	(42.4)
Amortization	(-11.0)	(-8.7)	(-9.4)	(-8.2)	(-8.0)
Private capital inflows	3.3	3.6	3.5	9.2	13.4
Nonconvertible area	101.8	95.2	109.4	81.1	81.0
Official transfers	4.2	4.5	4.0	4.5	5.0
Long-term loans	46.7	33.1	50.3	42.4	40.5
Drawings	(50.0)	(34.9)	(52.1)	(44.2)	(45.8)
Amortization	(-3.3)	(-1.8)	(-1.8)	(-1.8)	(-5.3)
Commodity credit 3/	50.9	57.6	55.1	34.2	36.0
Other 4/	--	--	--	--	-0.5
Errors and omissions	12.5	-7.2	-6.5	-13.2	--
Overall balance (convertible area)	20.8	8.7	-11.3	-4.5	-14.5
Financing	-20.8	-8.7	11.3	4.5	14.5
Change in net reserves (-increase)	-20.8	-8.7	11.3	4.5	--
Foreign exchange	(-14.8)	(-6.5)	(11.2)	(4.5)	(--)
Net Fund credit	(-6.0)	(-2.1)	(--)	(--)	(--)
Other (net)	(--)	(-0.1)	(0.1)	(--)	(--)
Financing gap	--	--	--	--	14.5
Memorandum items:					
Debt outstanding 5/	503	604	715	826	952
Convertible area	161	172	179	195	245
Nonconvertible area	342	432	536	631	707
(In percent of exports of goods and services)					
Current account	191.3	152.6	163.9	162.3	205.3
Debt service	22.3	15.9	15.8	15.6	20.3
Reserves					
(weeks of total imports)	7.0	9.1	5.1	4.6	3.7
(weeks of nonconvertible area imports)	17.4	21.6	13.5	9.6	6.5

Sources: Staff estimates based on data provided by the Lao authorities.

1/ Data may not add up because of rounding.

2/ This figure reflects foreign technical assistance that is financed by grant aid from bilateral convertible currency area donors.

3/ Calculated as residual of transactions with the nonconvertible area. The terminology "commodity credit" is used because this item reflects mainly ex ante determined deficits under bilateral trade arrangements which are converted into long-term loans at the end of each year.

4/ Reflects balances under bilateral payments arrangements with the German Democratic Republic, Kampuchea, and Viet Nam covering noncommercial transactions related to expenditures of embassies of these countries in the Lao P.D.R. and vice versa.

5/ Includes short-term debt and foreign liabilities of the monetary authorities.

currency area. While the current account deficit fell by about \$14 million, to \$131 million (162 percent of exports of goods and services), the deficit with the convertible currency area rose by \$15 million. This increase also reflected a sharp rise in bilateral technical assistance, financed by grant aid. The reduction in the current account deficit with the Soviet Union was matched by a reduction in commodity assistance. ^{1/} At end-1988, gross official reserves declined to \$17 million, the equivalent of only 4 1/2 weeks of imports, compared with 9 weeks of import cover at end-1986. External debt service declined from 22 percent of exports of goods and services in 1985 to 16 percent in 1988, mainly reflecting the debt deferment by the U.S.S.R.

In qualitative terms the reforms have had a dramatic effect on the economy. The supply and range of goods available in the market is impressive, and new department stores are being opened. Private sector activity, particularly in trade, commerce, and transportation, has increased rapidly. State enterprises are expanding operations and seeking private domestic and foreign partners. New foreign direct investment has been contracted, particularly in the garment and wood processing industries. Additional agreements have been reached for the establishment of branches of two foreign banks in Vientiane, sapphire and gold exploration, a number of new tourist hotels, assembly of motorized rickshaws, and further investments in garments and wood processing.

III. Report on the Discussions

In concluding the 1987 Article IV consultation, Executive Directors urged that measures already introduced to move toward a more liberal and market-oriented system be fully implemented. With regard to fiscal policy, distortions arising from the new tax system should be reduced. Government expenditures need to be restrained, particularly through the removal of subsidies and civil service reform. Monetary policy should be tightened and the credit demands of state enterprises not fully accommodated. The monetary authorities should be empowered to implement an appropriate financial program and interest rate policy be made more flexible. With regard to price and exchange rate policy, Directors stressed the need for a reduction of subsidies, and the elimination of existing multiple currency practices, as well as the more realistic

^{1/} Countertrade arrangements are maintained with nonconvertible currency area countries, and in most cases such trade is expected to be balanced. However, under the present five year agreement (1986-91) with the U.S.S.R., Lao P.D.R. can import four times the value of its exports to that country. The composition and unit price of traded goods are determined annually. At the end of each year, the outstanding deficit is converted to a long term, noninterest bearing loan. Also, in the case of Hungary, imports are allowed to exceed exports by a margin of \$2.5 million.

valuation of foreign transactions. Finally, the Directors indicated that substantial improvements in the coverage and quality of economic statistics were needed.

As discussed above, substantial progress has been achieved in addressing the concerns of the Executive Directors. Key changes in the external environment are also supporting the structural reform. Relations with convertible currency trading partners, including Thailand and France, have been normalized, as have those with China. As a result, restrictions on transshipment of goods through Thailand were reduced and a new trade arrangement, with settlement in convertible currencies, has been negotiated with China. France has forgiven the outstanding official debt and rescheduled commercial credits into long-term concessional loans. Debt payments due to the U.S.S.R. have been deferred until the year 2000. Japan, under its debt initiative, is making additional funds available on a grant basis. The authorities, in the spirit of glasnost, were forthcoming in discussions about previously sensitive topics, facilitating a better understanding of economic linkages.

Against this background, development of a medium-term macroeconomic framework that would be consistent with the more market-oriented economy was considered to be a priority. The discussions with the authorities focused on the stance of macroeconomic policies as well as additional structural measures that would be needed to raise per capita incomes without putting undue pressure on internal or external balances. The authorities expressed interest in the possible use of Fund resources under the structural adjustment facility (SAF).

1. The transformation process continued

The authorities indicated their intention to persevere and deepen the structural reforms already under way. Nevertheless, the rapid transition from a centrally planned to a market-oriented economy has not been matched by the development of institutions, instruments, and management capabilities for the effective indirect control of macroeconomic aggregates. Despite significant improvements, the data base remains weak. The quantification and prediction of economic variables is further complicated by the recent sharp changes in relative prices, the increased monetization of the economy, and the private sector's practice of holding its savings in foreign currency, gold, or real assets.

The major challenge facing the authorities is to pace the reactivation of the economy without undermining financial stability. The authorities expressed concern about the recent acceleration of inflation. The experiences of other countries in the process of similar transitions--with the overheating of their economies, increasing inflation, and the eventual disruption of the reform process--have underscored the need to quickly contain excess demand pressures. To

this end, the staff urged that fiscal and monetary policies be tightened and that exchange rate policy continue to be managed flexibly to ensure international competitiveness. These policies would need to be supported by further structural measures in the areas of taxation, government expenditure control and improved project evaluation and monitoring procedures, as well as further financial sector reform and trade liberalization.

a. Economic outlook for 1989

The economic outlook for 1989 has again been adversely affected by drought conditions. The impact of the drought on growth, however, is expected to be more than offset by increasing domestic and foreign private sector activity. Also, higher government investment spending is expected to give an immediate boost to the construction sector. Assuming that the May-October monsoons are normal, real growth is projected to recover to about 4 percent in 1989.

The drought has also contributed to additional pressure on prices. To help alleviate supply constraints, the private sector has been authorized, for the first time, to import rice directly. Trade reforms already implemented and the resulting increased supplies of imported consumer goods should also dampen price rises. Nevertheless, inflationary pressures can be expected to remain strong until domestic agricultural production rebounds. A more cautious monetary and fiscal policy stance is needed if inflation is to be contained to the 20 percent targeted.

The external position is expected to remain weak, reflecting the stagnation of electricity export earnings, the effect of a ban on log exports, and higher imports needed to facilitate private sector activity, rehabilitate economic infrastructure, and permit some increase in consumer goods. Even if the log export ban is replaced by a quota in a timely fashion, the current account deficit is projected to widen significantly. Given present aid commitments, a balance of payments gap of about \$14 million is expected to emerge and gross reserves would decline to about 3 1/2 weeks of total imports. Failure to mobilize additional assistance would lead to a curtailment of imports and the Government's investment program, with the attendant adverse consequences for inflation and long-term growth.

b. Fiscal policy

(i) Public enterprises

The authorities remain committed to further liberalization of the state enterprise sector. Enterprises still subject to government intervention are being reviewed to identify those that can be granted autonomy and those that may have to be closed. To improve financial management, a standard accounting framework is being developed with

bilateral technical assistance, and is expected to be adopted by many of the larger public enterprises toward the end of the year. Efforts are being stepped-up to rehabilitate selected industrial enterprises, with bilateral and multilateral foreign assistance, replacing or repairing, where possible, old equipment. The lack of an adequate legal framework remains a major impediment to the eventual privatization of these industries.

The policy of nonintervention in pricing decisions will be continued. To improve the financial position of state enterprises whose prices are still subject to control, consideration should be given to freeing these prices or adjusting them to better reflect costs and market conditions. In the case of electricity, the present domestic price of KN 7/kwh is well below the border price and does not reflect the cost of production of the low-voltage electricity used for domestic consumption.

During the process of granting increased enterprise autonomy, the existence of domestic payment arrears among the public enterprises and between them and the State Bank has come to light. By end-1988, the State Bank had written off about KN 2 billion pertaining to liquidated public enterprises, of which the largest was the Lao Food Corporation. ^{1/} The staff urged that work be initiated to quantify the remaining arrears and that a clearing mechanism and repayment schedules be developed.

(ii) Central government

In early 1989, the authorities initiated a thorough evaluation of the tax system to identify measures that could be taken to raise revenue, reduce the distortions inherent in the new tax system, and to improve administration. Among the revisions being considered for implementation in the last quarter of 1989 are: replacement of the variable profits tax rates with a flat rate; revision of the wage tax, which currently covers only locals working for foreign companies, embassies and agencies, to a progressive scheme covering all formal sector workers, including civil servants; imposing taxes on dividend and interest income; expansion of the turnover tax; introducing excises on alcohol, cigarettes and public utilities; and replacing the export profits tax with taxes on the value of exports. The staff, while supporting most new revisions, expressed reservations about specific measures. Profits from the production of exportables should be subject to the same flat tax proposed for profits accruing from other products; no new ad valorem tax on exports should be imposed. The proposed income tax should include bonuses and tax brackets should be indexed. The proposed turnover taxes should be examined carefully to minimize their cascading effects.

^{1/} For analytical purposes, outstanding bank credit has been adjusted to include these loans.

The staff welcomed the elimination of consumer subsidies, subsidies to civil servants and to autonomous public enterprises. As a result of these actions, however, real wages of civil servants have declined to about one third to one half of those of employees in public enterprises and the private sector. This has caused difficulties in the retention of qualified staff needed to manage the new economic system. The Government plans to raise wages by an average of 30 percent in July 1989 while increasing the proportion to be paid in cash. To limit the impact on the wage bill, civil service employment is to be reduced by a further 20 percent prior to mid-year, continuing the trend of 1988 separations. Allocations for operations and maintenance are being increased and investment spending is being redirected to repair, rehabilitate, and expand social and economic infrastructure.

Taking into account these tax and expenditure proposals and the external assistance available, the staff analysis of the 1989 budgetary outturn indicated that a financing gap is likely to emerge if recourse to bank financing is to be avoided. The staff suggested that selected excises be advanced to the second quarter of the year, and that royalty payments be required from the state-owned electricity company. Further revenues could be obtained from an increased tariff on petroleum imports, whose domestic price is low by international standards since Lao P.D.R. benefits from preferential import prices from the nonconvertible currency area. The incentives provided for new and rehabilitated domestic firms should also be reviewed bearing in mind the twin objectives of encouraging investment without undue loss of revenue. The proposed salary increases and shift to cash payment ^{1/} would need to be carefully handled to avoid exacerbating demand pressures. The reordering of expenditure priorities to increase operations and maintenance and to rehabilitate infrastructure, in line with World Bank recommendations, was welcomed. Project selection, preparation, and design, as well as implementation and monitoring procedures, need to be improved. The size of the proposed investment program, however, would have to reflect overall budgetary considerations, including the limited availability of funds for local investment, the relationship between investment and recurrent cost, and the need to avoid recourse to inflationary sources of finance.

^{1/} The inflationary impact of the shift to cash payments would be limited to the extent that goods now purchased under the purchase book system are released to the market. Moreover, the increased market supplies of rice during the present drought may result in reduced price pressure if the composition of spending changes. Purchase books, however, have permitted the accumulation of wage payments for purchase of more expensive consumer goods. To the extent that these savings are monetized or do not take place once cash payments increase discretion over spending, the shift to cash may contribute to demand pressures.

c. Monetary policy

The authorities have implemented a number of measures to reform the financial system. During this transitional period, the formulation of monetary policy is hampered by the rapid changes that have taken place in the economy and in the financial system. The demand for money is difficult to predict in light of the decontrol of prices, the shift to cash payment for procurement of agricultural products, the increasing payment of public sector salaries in cash, and the recent depreciation of the kip. The inadequacy and small denomination of kip notes ^{1/} have contributed to the increased use of foreign currencies in domestic transactions. Lack of monetary policy instruments has also impeded effective policy implementation. Presently, individual branches and the new commercial banks are free to determine their own level of reserves within a 5-30 percent range specified by the State Bank. Interest rates have not been effectively used to mobilize savings or allocate credit.

Prior to 1988, the role of monetary policy had largely been confined to accommodating the credit needs of the state enterprises, and, indirectly, the budget. Starting in 1988, preferential access to credit by public enterprises was eliminated, and an overall credit ceiling was established by the State Bank. Moral suasion was used extensively to contain the growth of credit. Outlying branches, however, were often pressured by the provincial authorities to grant loans. In October 1988, interest rates were increased; however, most rates remain negative in real terms. Selected long-term loan rates are below short-term rates, in order to encourage priority sectors such as agriculture. While foreign currency deposits are not remunerated, such deposits are maintained because of their greater liquidity.

Noting the authorities' concern about accelerating inflation and the weak external position, the staff urged caution in setting the credit program for 1989. Use of credit by the central government should be strictly limited to ensure adequate availability of funds for the private sector and the state enterprises. To counter political pressure, limits could be placed on loans that can be granted to single borrowers by branches without head office authorization. These limits would be eliminated as the branches are constituted into autonomous commercial banks. Access to State Bank overdrafts should be strictly controlled. Once the financial system becomes more developed, the adoption of reserve requirements was also encouraged.

Willingness to hold kip deposits is undermined by the inability to withdraw funds because of the lack of kip notes and their small denomination. The habit of using checks in transactions has not yet taken hold. The stock of currency notes needs to be replenished and

^{1/} In late March 1989, a new KN 500 bill, equivalent to about \$1.05 was introduced. Prior to that, the largest denomination was KN 100.

notes of higher denomination printed. Appropriate interest rates would also encourage a shift into financial assets. Interest rates on domestic currency accounts should also be raised above the rate of inflation and be kept positive in real terms. To develop the banking tradition, consideration should be given to permitting banks to pay interest on foreign currency accounts at rates approximating those abroad. Lending rates would need to be raised and the negative spread on maturities eliminated. To the extent that the authorities want to subsidize credit to particular sectors, the cost of such subsidies should be borne by the budget. The staff noted that sometimes lengthy procedures were required to obtain approval from the Council of Ministers in order to change interest rates. In an economy where almost all other prices have been freed, the staff urged that consideration should be given to the eventual freeing of interest rates, once adequate instruments have been developed, with the State Bank influencing rates indirectly.

Measures already taken are important first steps in developing a financial system supportive of the shift toward a more market-oriented economy. The decision to open the domestic banking system to foreign competition was welcomed. The present proposal calls for the State Bank to maintain an equity participation in the new joint ventures. As a central bank, however, it would not be appropriate for the State Bank to own part of individual banks as this might conflict with its ability to conduct an independent monetary policy.

d. External policies

The authorities intend to maintain a unified official exchange rate and manage it in a flexible manner, taking into account developments in the parallel market. While this policy would be effective in the short run, over time the parallel market rate is likely to become relevant for only a dwindling number of transactions. The authorities and the staff team agreed, therefore, that the official rate would not be tied explicitly to the parallel rate or adjusted on a daily basis. Sustained deviations in the rates, however, would be a signal to adjust the official rate. The maintenance of a dual market rate, however, should only be viewed as a transitional step toward eventual unification. Over the medium term, additional indicators of exchange rate action need to be developed. The staff described the methodology used in calculating a real effective exchange rate index and suggested that consideration be given to measuring real effective exchange rate movements against a weighted basket of currencies of major trading partners and competitor countries.

With respect to the exchange and trade systems, ^{1/} the authorities noted that they are presently in a transitional period and requested Fund assistance in designing more rational systems. In practice, there are no foreign exchange surrender requirements. Payments for authorized imports and other authorized current account transactions can be made by using retained foreign exchange earnings and--depending on availability--foreign exchange allocated by the Foreign Trade Bank (BCEL). Additional foreign exchange may be obtained from the parallel market. They would prefer a system that channels foreign exchange through the banking system and have prepared draft legislation to this effect. The staff stressed that the role of financial institutions in the foreign exchange market fundamentally depends on the accessibility of banking facilities, appropriate interest and exchange rates, and consistency in policy implementation aimed at promoting stability. Nevertheless, an appropriate legal framework is an adjunct to banking legislation. At the request of the authorities, the staff is planning to review all aspects of banking and foreign exchange legislation.

Although not yet effective, a decision has been taken to reduce the list of strategic goods to three products: logs, minerals, and coffee. The staff welcomed this decision and urged that further liberalization be considered, particularly since strategic minerals are only produced by state enterprises. Moreover, mixed enterprises will continue to be allowed to compete with state enterprises in the procurement and export of coffee; present contracts with the non-convertible currency area allow the Lao Trading Corporation to pay prices slightly above those offered by the private sector. Effective January 1, 1989, log exports, except for trees harvested from the reservoir and those already cut or dead, have been banned. The ban aims at redressing the emerging problems of deforestation, preventing uncontrolled exploitation of forests arising from the imposition of a ban on logging in neighboring Thailand, and developing a domestic wood processing industry. The authorities have already reached agreement with the AsDB to replace the ban by an export quota that would be reduced in line with the expansion of the domestic wood processing industry. Once the global survey of forest resources, now under way, is completed, the size of the quota would be reviewed. Given the weak external payments position and the substantial contribution of log exports to total export earnings, the early introduction of the proposed quota is essential.

Import licenses, which are issued by the Ministry of Commerce taking into account national priorities, are required for all imports and are given mainly to trading corporations, which are also the

^{1/} From the discussions with the authorities, the staff ascertained that the restrictions presently maintained by Lao P.D.R. were introduced or significantly modified subsequent to its becoming a Fund member, and hence do not fall under the provisions of Article XIV.

principal exporters. The composition of trade that can be undertaken by these corporations is also determined by the Ministry of Commerce. At present, exporters are provided with import licenses for twice the value of their planned exports. The BCEL provides foreign exchange on the basis of availability, with the remainder being obtained from the parallel market. The present practice of issuing import licenses only to exporters is unduly restrictive and consideration should be given to giving licenses to all applicants. Permitting more producers to export directly could also encourage exchange transactions through the banking system as firms need kip to meet domestic obligations.

Lao P.D.R. maintains multiple currency practices subject to approval under Article VIII, Sections 2(a) and 3 in the form of a dual exchange rate system, as the spread between the official and parallel market rates exceeds 2 percent, and in the form of margin requirements for opening letters of credit by the BCEL, as yet a branch of the State Bank. The staff noted, however, that once the BCEL becomes an autonomous commercial bank, as expected during 1989, this practice if continued by the BCEL on its own accord would no longer constitute a multiple currency practice.

Lao P.D.R. has bilateral trading arrangements 1/ with Bulgaria, Czechoslovakia, the German Democratic Republic, Hungary, Democratic Kampuchea, Mongolia, Poland, the U.S.S.R., and Viet Nam. 2/ These arrangements are on a purely countertrade basis with the exception of Hungary and the U.S.S.R. where concessional aid is also provided. Bilateral payments arrangements are maintained with the German Democratic Republic, Democratic Kampuchea, and Viet Nam covering noncommercial transactions related to expenditures of embassies of these countries in Lao P.D.R. and vice versa. The bilateral payments arrangements with the two Fund members give rise to exchange restrictions subject to approval under Article VIII, Section 2(a). At present, Lao P.D.R. maintains a net creditor position with Viet Nam and is in balance with Democratic Kampuchea. Nevertheless, the authorities have indicated their intention to make every effort to eliminate the restrictive features of these arrangements. The requirement of prior authorization of the Ministry of Commerce for invisible payments and the limitations on travel allowances also constitute exchange restrictions subject to approval.

1/ These arrangements and other restrictive features of the exchange and payments systems are described in Annex I.

2/ Lao P.D.R. recently concluded a trade and payments agreement with China. The staff will seek additional information from the authorities regarding this arrangement.

2. Medium-term outlook, 1989-93

The staff has prepared a medium-term balance of payments outlook through 1993 (Table 4). 1/ Strong export growth is projected to reflect the recovery of electricity exports from drought-reduced levels and higher coffee exports as production responds to price and trade liberalization incentives. New hydroelectric generating capacity for export is expected to come on stream in 1991. Over the medium term, processed wood and nontraditional products, such as garments, light assembly items and gemstones, will become important. Tourism and private remittances are also expected to emerge as new sources of foreign exchange earnings. Real import growth is targeted to average 11 percent per annum over the period, compared with an average of less than 2 percent realized in the 1985-88 period. This level of imports is considered necessary in order to meet import requirements for the larger public investment program and to facilitate private sector activity.

The medium-term scenario indicates that Lao P.D.R. will face mounting financing gaps throughout the 1989-93 period. These gaps would increase substantially if the proposed quota on logs is not implemented as envisaged. Moreover, the low level of reserves will leave the economy, which is becoming increasingly open, vulnerable to external shocks. While possible drawings under Fund SAF arrangements and an IDA SAC would close these gaps in 1989-90 and permit some accumulation of reserves, additional foreign assistance would still be needed in the 1991-93 period. Without these funds, the high rate of import growth could not be sustained. This would imply that the Government's rehabilitation program would be slowed and scarcities of imported inputs would not be eased. In these circumstances, economic growth and living standards would not significantly improve.

Lao P.D.R. has accumulated a large outstanding stock of external debt relative to its present level of foreign exchange earnings. Over the medium-term, outstanding external debt would rise from \$826 million at end-1988 to about \$1.5 billion at end-1993. About two thirds of debt

1/ The projections are predicated on: the maintenance of cautious monetary and fiscal policies throughout the period; flexible management of the exchange rate to ensure international competitiveness; the implementation of structural reform measures discussed above; and, from mid-1989, the return of normal weather conditions and the introduction of a log export quota at the 1988 export volume level. Export and import price projections are consistent with those of the most recent World Economic Outlook. Projections of foreign assistance are based on present commitments and do not include additional resources that might become available under the IDA Structural Adjustment Credit (SAC) or the SAF. Scheduled amortization payments take into account the deferment of debt to the U.S.S.R. as well as the debt relief granted by France and the Japanese debt initiatives.

Table 4. Lao P.D.R.: Medium-Term Balance of Payments Scenario, 1988-93 ^{1/}

	1988 Est.	1989	1990	1991	1992	1993
		Projections				
		(In millions of dollars)				
Exports, f.o.b.	57.6	63.8	77.7	88.9	100.4	110.0
Convertible area	36.6	40.8	52.0	61.6	71.5	79.4
Electricity	(11.1)	(11.9)	(18.1)	(21.2)	(22.2)	(21.8)
Wood and wood products	(20.8)	(21.5)	(23.3)	(25.6)	(29.8)	(32.6)
Other	(4.7)	(7.4)	(10.6)	(14.8)	(19.5)	(25.0)
Nonconvertible area	21.0	23.0	25.7	27.3	28.9	30.6
Imports, c.i.f.	-188.0	-232.6	-262.4	-300.6	-343.8	-382.8
Convertible area	-90.4	-133.6	-161.3	-197.1	-238.1	-274.7
Nonconvertible area	-97.6	-99.0	-101.0	-103.5	-105.7	-108.1
Services and private transfers (net)	-0.6	-10.2	-8.0	6.5	7.3	12.0
Current account (excluding grants)	-131.1	-179.0	-192.6	-205.2	-236.1	-260.9
Convertible area	-50.0	-98.0	-111.8	-123.0	-152.8	-176.3
Nonconvertible area	-81.1	-81.0	-80.8	-82.2	-83.3	-84.5
Capital account	139.8	164.5	177.5	189.3	201.6	215.1
Convertible area	58.7	83.5	96.6	107.1	118.3	130.5
Official transfers	(34.0)	(35.7)	(37.5)	(39.4)	(41.3)	(43.4)
Long-term loans (net)	(15.5)	(34.4)	(41.5)	(45.8)	(49.3)	(51.9)
Private capital inflows	(9.2)	(13.4)	(17.6)	(21.9)	(27.7)	(35.2)
Nonconvertible area	81.1	81.0	80.8	82.2	83.3	84.5
Errors and omissions	-13.2	--	--	--	--	--
Overall balance (convertible area)	-4.5	-14.5	-15.2	-16.0	-34.5	-45.7
Financing	4.5	14.5	15.2	16.0	34.5	45.7
Change in net reserves (-increase)	4.5	--	--	--	--	--
Foreign exchange	(4.5)	(--)	(--)	(--)	(--)	(--)
Net Fund credit	(--)	(--)	(--)	(--)	(--)	(--)
Financing gap	--	14.5	15.2	16.0	34.5	45.7
Memorandum items:						
Debt service ratio 2/	15.6	20.3	16.4	14.2	13.1	12.4
Debt outstanding 3/	826	952	1,084	1,223	1,384	1,561
Convertible area	195	245	301	363	447	546
Nonconvertible area	631	707	783	860	937	1,015
Reserves (in weeks)						
Total imports	4.6	3.7	3.3	2.9	2.5	2.3
Convertible area imports	9.6	6.5	5.4	4.4	3.7	3.2

Sources: Data provided by the Lao authorities; and staff estimates and projections.

^{1/} Components may not add to totals owing to rounding.

^{2/} As a percent of exports of goods and services.

^{3/} Includes short-term debt and foreign liabilities of the monetary authorities.

outstanding at end-1993 would be to the nonconvertible currency area and is noninterest bearing. The authorities have indicated their intention not to borrow on commercial terms. Taking into account debt relief already obtained, and assuming that the financing gaps are filled by concessional loans, the ratio of debt service to current receipts is projected to fall from 16 percent at end-1988 to about 12 1/2 percent by end-1993.

Notwithstanding an appropriate policy stance and continued structural reforms, the balance of payments is expected to remain structurally weak in the foreseeable future. Additional debt deferments beyond the year 2000 may be needed if high growth is to be sustained.

IV. Staff Appraisal

Since 1985, Lao P.D.R. has implemented wide-ranging policy reforms that are transforming the economy from a centrally planned to a market oriented one. Measures already implemented include: liberalization of production, distribution, prices and trade; exchange reform, including the unification of the multiple official rates; the introduction of a new tax system; and the initiation of a restructuring of the banking system. The staff strongly supports these initiatives and urges the authorities to maintain the momentum of reforms and redress remaining distortions inherent in the incentive structure.

The authorities are committed to extending autonomy to most viable public enterprises and closing those that cannot be made profitable. The adoption of uniform accounting practices will make possible a more systematic analysis of the financial performance of the enterprises. The staff urges the authorities to review the few prices remaining subject to control and adjust them as needed to reflect market conditions or ensure an adequate return to capital. The staff welcomes the intention to reduce the number of strategic goods and to expand the role of the private sector. The present lack of a legal framework, however, is impeding privatization efforts.

Major progress has been made in reforming the fiscal system, particularly with respect to relations between enterprises and the state budget. A thorough review of the tax system has been undertaken and modifications are being considered. Most of the proposed changes will widen the tax base, improve equity, and ease administration. Distortions would persist, however, if taxes on exports and wage income are implemented as presently envisaged. The staff welcomes the elimination of subsidies and recognizes that some adjustment in civil servant wages is needed if qualified staff are to be retained. To limit the impact on the wage bill, a further reduction in staffing is appropriate. The authorities should review its present policy on granting tax concessions. Increased budgetary allocations are needed to meet recurrent expenditures and to repair and rehabilitate the badly

deteriorated infrastructure. The size of the proposed investment program, however, will have to reflect overall budgetary considerations. Project planning, monitoring and implementation capabilities need to be strengthened.

Financial sector reform is proceeding and the monetary policy capabilities of the State Bank are expected to improve over time. The State Bank should be given the independence needed to conduct monetary policy, including a more active use of interest rate policy. New instruments of monetary policy need to be developed. Consideration should also be given to increasing the note issue and issuing larger denomination currency notes.

The recent acceleration of inflation and further weakening of the external position in 1988 underscore the importance of supporting structural reforms with appropriate macroeconomic policies. The 1989 budget outlook indicates that the implementation of selected tax measures needs to be advanced and that planned wage increases and higher operating, maintenance and rehabilitation expenditures have to be carefully managed so as not to exacerbate demand pressures. Credit policy should be tightened and recourse to bank credit by the Government strictly limited.

The medium-term outlook indicates that the balance of payments will remain weak even if planned reforms are fully implemented and the stance of policy is appropriate. This weakness would be exacerbated to the extent that the proposed quota on log exports is not implemented in a timely fashion. Lao P.D.R. can be expected to remain dependent on foreign aid for the foreseeable future. Because of the large concessional component of its debt and recent debt relief, difficulties in meeting debt service obligations are not expected if the stance of policy remains appropriate. Borrowing on commercial terms, however, should continue to be avoided.

The staff welcomes the authorities' commitment to continuing its flexible management of a unified official exchange rate. Measures to liberalize the exchange rate, trade and current payments systems are welcomed. The multiple official exchange rates were unified in September 1987. The multiple currency practice arising from a greater-than-2 percent-spread between the official buying and selling rates was eliminated. The narrowing of the spread to 2 1/2 percent between the official and parallel market exchange rates in February 1989 is also an encouraging development. This dual exchange rate system still gives rise to a multiple currency practice. The multiple currency practice arising from margin requirements will be eliminated once the BCEL is no longer a branch of the State Bank. Attention should now focus on removing the remaining restrictive features of the exchange, trade and payments regimes including the elimination of multiple currency practices. The staff notes that these systems are in a transitional phase. In view of the intention of the authorities to remove the

multiple currency practice arising from the margin requirements in the near future, the staff recommends the temporary approval of this measure. The staff urges the authorities to cooperate in the establishment of a more realistic representative rate for Fund transactions.

Lao P.D.R. is on the bicyclic procedure and, therefore, the 1990 consultation with Lao P.D.R. will be completed not later than April 1990.

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board.

1. The Fund takes this decision relating to the Lao People's Democratic Republic's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 1989 Article XIV consultation with the Lao People's Democratic Republic, in light of the 1989 Article IV consultation with the Lao People's Democratic Republic conducted under Decision No 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).
2. The Lao People's Democratic Republic imposes restrictions on the making of payments and transfers for current international transactions, subject to approval under Article VIII, Section 2(a), in the form of restrictive features under bilateral payments arrangements with Fund members, requirement of prior authorization for invisible payments and limitations on travel allowances. It also imposes multiple currency practices, subject to approval under Article VIII, Sections 2(a) and 3, arising from a dual exchange rates system and a requirement of margins for the opening of letters of credit. The Fund approves the maintenance of the multiple currency practice arising from the requirement of margins until the completion of the next Article IV consultation with the Lao People's Democratic Republic or until April 30, 1990, whichever is earlier, and urges the authorities to remove the other exchange restrictions and multiple currency practice as soon as possible.

Lao P.D.R.: Exchange and Trade Systems

The currency of the Lao People's Democratic Republic is the kip (KN). On February 21, 1989 the official exchange rates for the U.S. dollar quoted by the State Bank (the central bank) were KN 470 = US\$1 (buying) and KN 475 = US\$1 (selling). The rate in the officially tolerated parallel market was KN 480 = US\$1 (buying) and KN 487 = US\$1 (selling). These rates are used for all transactions except for transactions with the Fund for which a representative rate of KN 10 per dollar applies. The fixing of the official exchange rate is done at the State Bank taking into account developments in the rate prevailing in the parallel market. The Lao Bank for Foreign Trade (BCEL), a subsidiary of the State Bank, handles all official foreign exchange transactions related to foreign trade and services. All other official transactions are handled by the State Bank, which also administers exchange controls.

The exchange and trade systems of the Lao P.D.R. are in a transition phase. Most of the restrictive foreign exchange and trade regulations, introduced in 1976, have not yet been officially abolished. In practice, however, the systems are liberally implemented. Foreign trade has been decontrolled and state trading companies, mixed companies (joint ventures between public and private domestic enterprises but these can also form joint ventures with foreign investors), cooperatives, and public enterprises can engage in trade. Import licenses, which are issued by the Ministry of Commerce, are required for all imports and are generally given only to exporters. A national import-export plan is a key element of the trading system. This plan is formulated by the Department of Foreign Trade in the Ministry of Commerce and takes into account the plans of individual enterprises and the requests furnished by each ministry and by the provincial governments. Payments for licensed imports are made by using retained export earnings, foreign exchange allocated by the BCEL, and foreign exchange obtained from the parallel market. The restrictive features of the import licensing system tends to put pressure on the parallel market exchange rate. This is aggravated by the fact that even for authorized imports, foreign exchange is not necessarily provided by the BCEL.

Payments for invisibles are subject to prior authorization by the Ministry of Commerce. Up to a limit of \$2,000 foreign exchange can be used for travel purposes; for higher amounts authorization by the Ministry of Commerce is required. Foreign exchange for traveling is provided by the BCEL up to a limit of \$1,000. Persons holding foreign exchange deposits with the BCEL are permitted to withdraw foreign exchange up to \$2,000, or more if adequate authorization was given. In practice, there are no restrictions on profit remittances; profit remittances are freely permitted under the new foreign investment law promulgated in mid-1988.

Although not yet effective, a decision has been taken to reduce the list of strategic goods and, thereby, dismantle the state's monopoly to export these items. According to that decision, only logs, minerals, and coffee will continue to be considered strategic. Notwithstanding this classification, mixed enterprises are also allowed to buy coffee in the domestic market and to export coffee. Reflecting the Government's intention to prevent undue exploitation of forests and to encourage the development of a domestic wood processing industry, log exports, except for trees harvested from the reservoir and those already cut or dead, have been banned effective January 1, 1989. The authorities have agreed with the AsDB to replace the ban by a quota on log exports. The level of the quota would be reviewed when a country-wide forest survey has been completed. The quota would gradually be reduced as the capacity of the domestic wood processing industry increases.

Although foreign exchange surrender requirements have not been abandoned officially, in practice the surrender of foreign exchange earnings is not enforced. Foreign exchange deposits held with the BCEL can be used to make payments for authorized imports of goods and services, to make payments in foreign currency by check for domestic purposes, and for cash withdrawals in kip. No prescription of currency requirement is imposed on receipts or payments, but in principle, the central bank provides and accepts only Deutsche marks, French francs, Japanese yen, pounds sterling, Swiss francs, Thai baht, and U.S. dollars.

Lao P.D.R. maintains bilateral trading arrangements with Bulgaria, Czechoslovakia, the German Democratic Republic, Hungary, Democratic Kampuchea, Mongolia, Poland, the U.S.S.R., and Viet Nam. These are multiyear trading arrangements and are implemented through annual protocols determining imports and exports in volume terms and attaching shadow prices (expressed in rubles) to various transactions. Except for trading arrangements with the U.S.S.R. and Hungary, all other arrangements are on a purely countertrade basis. If balances exist at the end of a year it is required to reach within three months an agreement with the partner country to settle the balance during the year in which the settlement agreement was reached. In principle, balances have to be settled by means of trade transactions. In the case of Hungary, the same regulation applies if the countertrade deficit exceeds a certain line of credit granted by Hungary. Under the trading arrangement with the U.S.S.R., the import value of Lao P.D.R. may exceed its export value by 400 percent. Trade deficits, up to a maximum limit specified at the outset of the year, with the U.S.S.R. are converted into long term loans at the end of each year.

Lao P.D.R. has bilateral payments arrangements with the German Democratic Republic, Democratic Kampuchea, and Viet Nam covering noncommercial transactions related to expenditures of embassies of these countries in Lao P.D.R. and vice versa.

Lao PDR: Summary of Tax System as of 1989

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates																						
1. <u>Taxes on income and profits</u>																									
1.1 Tax on industrial and commercial profits	Annual levy on industrial and commercial profits derived by enterprises (public, private, and mixed) from domestic sales. Collected monthly on profits forecast in annual plan; adjusted quarterly in light of actual outcome.	New and rehabilitated domestic firms are exempt from profits taxes for 2-4 years from the time that profits begin. Foreign and jointly owned firms are eligible for exemption for 1-5 years, as discussed below.	<table><tr><th><u>Industry</u></th><th><u>Tax Rate</u> (In percent)</th></tr><tr><td colspan="2">Different rates apply to different industries.</td></tr><tr><td>Beer, soft drinks, cigarettes</td><td>85</td></tr><tr><td>Alcohol, slippers, and other foam rubber products</td><td>80</td></tr><tr><td>Plastic products, electrical cords, batteries, tin, gypsum, coal, precious stones, chemical products such as oxygen, acetylene</td><td>70</td></tr><tr><td>Timber and processed wood: logs, sawn wood, parquet, sliced veneer, furniture, wooden products, fuel wood, charcoal; textiles, cloth, paper, printing, soap, medicine, tooth-paste, insecticides, trade in foreign currency and precious metals</td><td>60</td></tr><tr><td>Electrical power for local consumption, water, bottled water, ice</td><td>50</td></tr><tr><td>Foreign-owned enterprises, regardless of industry</td><td>50</td></tr><tr><td>Cement, gravel, sand, lime, detergent</td><td>40</td></tr><tr><td>Agricultural tools, corrugated iron, bricks, tents, nails, barbed wire, animal feed, sugar, fish sauce, biscuits, cakes, noodles, abattoirs, products made out of bones or vegetables</td><td>30</td></tr><tr><td>Rice milling, salt</td><td>20</td></tr></table>	<u>Industry</u>	<u>Tax Rate</u> (In percent)	Different rates apply to different industries.		Beer, soft drinks, cigarettes	85	Alcohol, slippers, and other foam rubber products	80	Plastic products, electrical cords, batteries, tin, gypsum, coal, precious stones, chemical products such as oxygen, acetylene	70	Timber and processed wood: logs, sawn wood, parquet, sliced veneer, furniture, wooden products, fuel wood, charcoal; textiles, cloth, paper, printing, soap, medicine, tooth-paste, insecticides, trade in foreign currency and precious metals	60	Electrical power for local consumption, water, bottled water, ice	50	Foreign-owned enterprises, regardless of industry	50	Cement, gravel, sand, lime, detergent	40	Agricultural tools, corrugated iron, bricks, tents, nails, barbed wire, animal feed, sugar, fish sauce, biscuits, cakes, noodles, abattoirs, products made out of bones or vegetables	30	Rice milling, salt	20
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Lao PDR: Summary of Tax System as of 1989 (Continued)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates	
1.2 Taxes on wages and salaries of Lao citizens employed by foreign embassies and companies and international organizations	Levied on wages, salaries, bonuses, and other benefits derived from employment. Withheld at source by the employer on a monthly basis.	All public, private, and mixed enterprise sector employees.	<u>Monthly Wage</u> (In kip)	<u>Tax Rate 1/</u> (In percent)
			0-15,000	0
			15,000 and above	5
1.3 Rental income tax	Assessed on all rental income. Paid by the lessor when rent is paid.	None.	40 percent.	
1.4 Agricultural income and profits taxes	Tax on paddy collected in kind, while cash payments are made for all other products.	Dry season paddy crop. Output from farms where average yield is less than 100 kg/ha and output of disabled farmers. Output in newly terraced mountainous land and in the plain exempt for five and three years, respectively. Two years exemption for rice farming on fallow land abandoned 2-4 years ago and on a case by case basis on land fallow less than 2 years. Rice farming on land that is turned to permanent crop cultivation is exempt for five years.	<u>Paddy Tax</u>	<u>Tax (kg/ha)</u>
			<u>Lowlands</u>	
			Yield of 0-2,500 kg/ha	100
			Yield of 2,501-3,000 kg/ha	120
			Yield of 3,001-3,500 kg/ha	140
			Yield of 3,501 kg/ha or more	160
			<u>Uplands</u>	
			Slash and burn	70
			Terraced farming	40
			<u>Other Products</u>	
			Six percent of selling price or annual income.	
2. <u>Taxes on property</u>			<u>Real Estate</u>	
2.1 Death, gift, and transfer taxes	Applied to the market value of real property transferred through inheritance, sale, or gifts.		Transfers between direct descendants: 2 percent Transfers between second degree relatives: 4 percent Transfers between third degree relatives: 7 percent Transfers between nonrelated persons: 10 percent Other property: 3 percent	

Lao PDR: Summary of Tax System as of 1989 (Continued)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates																																												
<hr/>																																															
3. <u>Taxes on goods and services</u>																																															
3.1 Turnover taxes	Levied on turnover of enterprises. Collected monthly based on turnover forecast on the basis of annual plan; revised quarterly in light of actual outcome.		<table><tr><th><u>Category</u></th><th><u>Tax Rate</u> (In percent)</th></tr><tr><td>Handicrafts</td><td></td></tr><tr><td> Blacksmiths</td><td>2</td></tr><tr><td> Weavers, tailors</td><td>3</td></tr><tr><td> Goldsmiths, painters, sculptors</td><td>4</td></tr><tr><td>Construction (on value)</td><td>4</td></tr><tr><td>Transport and mail</td><td></td></tr><tr><td> Road transport</td><td>5</td></tr><tr><td> River transport</td><td>4</td></tr><tr><td> Air transport</td><td>4</td></tr><tr><td> Mail</td><td>5</td></tr><tr><td>Repair services</td><td></td></tr><tr><td> Road and irrigation infrastructure repairs</td><td>1</td></tr><tr><td> Equipment, transport, and building repair</td><td>4</td></tr><tr><td> Other repairs</td><td>5</td></tr><tr><td>Hotels, restaurants, and other services</td><td></td></tr><tr><td> Laundry, shoemaking, hairdressing, photo- graphy, movies, and theater</td><td>5</td></tr><tr><td> Hotels and tourism</td><td>10</td></tr><tr><td> Restaurants and nightclubs</td><td>15</td></tr><tr><td>Retail trade</td><td></td></tr><tr><td> Mountain regions</td><td>2</td></tr><tr><td> Retail of agricultural and forestry products not subject to agricultural tax</td><td>6</td></tr></table>	<u>Category</u>	<u>Tax Rate</u> (In percent)	Handicrafts		Blacksmiths	2	Weavers, tailors	3	Goldsmiths, painters, sculptors	4	Construction (on value)	4	Transport and mail		Road transport	5	River transport	4	Air transport	4	Mail	5	Repair services		Road and irrigation infrastructure repairs	1	Equipment, transport, and building repair	4	Other repairs	5	Hotels, restaurants, and other services		Laundry, shoemaking, hairdressing, photo- graphy, movies, and theater	5	Hotels and tourism	10	Restaurants and nightclubs	15	Retail trade		Mountain regions	2	Retail of agricultural and forestry products not subject to agricultural tax	6
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Lao PDR: Summary of Tax System as of 1989 (Continued)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates	
3.2 Business and professional licenses	Levied annually on enterprises, based on turnover. Payable during the first three months of the year on a current basis.		Different rates apply to industrial commercial and import-export enterprises as follows:	
			Enterprise Rates	
			Turnover (In kip)	Indus- trial (In kip)
			0- 100,000	150
			100,001- 250,000	400
			250,001- 500,000	700
			500,001- 800,000	1,500
			800,001-1,300,000	3,000
			1,300,001-2,000,000	6,000
			2,000,001 and above	10,000
			Enterprise Rates	
			Turnover (In kip)	Import-export commercial (In kip)
			0- 200,000	3,000
			200,001- 400,000	10,000
			400,001- 600,000	15,000
			600,001- 800,000	20,000
			800,001-1,000,000	25,000
			1,000,001 and above	30,000
3.3 Taxes on vehicles	Levied annually.	Public vehicles and river boats with less than 500 kg carrying capacity are exempt.	Tricycles: KN 30 Motor vehicles: KN 50-200 depending on horsepower River boats (pirogs): KN 100-300 boarding tax	

Lao PDR: Summary of Tax System as of 1989 (Continued)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates														
4. <u>Taxes on international trade</u>																	
4.1 Import duties	Imposed on c.i.f. value of imports; not based on any standard nomenclature.	Goods imported as grants and under investment projects; goods for sample are also exempted.	Ranging from 1 percent to 70 percent as follows:														
			<table><tr><th><u>Category</u></th><th><u>(In percent)</u></th></tr><tr><td>Machinery, transport equipment and spare parts for heavy industry, agriculture, forestry, irrigation, construction, telecommunications; salt production, electricity generation, seeds and animals for reproduction, insecticides, pesticides, animal feed</td><td>1</td></tr><tr><td>Medical, school and sport equipment, toys, printing equipment, photocopying machines, seafood</td><td>3</td></tr><tr><td>Machinery, equipment and spare parts for light industry and handicrafts; kerosene, jet fuel, natural gas, rice, flour, live animals, raw materials, and construction materials which are not produced locally</td><td>5</td></tr><tr><td>Buses, spare parts, electrical equipment, and industrial goods for consumption; textiles, office materials and equipment, fishing and household appliances, dyeing liquids, paints, barbed wire, diesel oil, gasoils and oils</td><td>10</td></tr><tr><td>Four-wheel trucks, electrical utensils, movie cameras, health care products, kitchenware, watches, eye glasses, cassettes, movie projectors and related spare parts</td><td>15</td></tr><tr><td>Raw materials and construction materials which can be produced locally; jeeps, motorcycles, spare parts, gasoline, cloth, umbrellas, shoes, hats, belts, cameras, radios, video machines, tape recorders, amplifiers, loudspeakers, musical instruments, air conditioners, basic products not made of plastic, finished chemical products for consumption</td><td>20</td></tr></table>	<u>Category</u>	<u>(In percent)</u>	Machinery, transport equipment and spare parts for heavy industry, agriculture, forestry, irrigation, construction, telecommunications; salt production, electricity generation, seeds and animals for reproduction, insecticides, pesticides, animal feed	1	Medical, school and sport equipment, toys, printing equipment, photocopying machines, seafood	3	Machinery, equipment and spare parts for light industry and handicrafts; kerosene, jet fuel, natural gas, rice, flour, live animals, raw materials, and construction materials which are not produced locally	5	Buses, spare parts, electrical equipment, and industrial goods for consumption; textiles, office materials and equipment, fishing and household appliances, dyeing liquids, paints, barbed wire, diesel oil, gasoils and oils	10	Four-wheel trucks, electrical utensils, movie cameras, health care products, kitchenware, watches, eye glasses, cassettes, movie projectors and related spare parts	15	Raw materials and construction materials which can be produced locally; jeeps, motorcycles, spare parts, gasoline, cloth, umbrellas, shoes, hats, belts, cameras, radios, video machines, tape recorders, amplifiers, loudspeakers, musical instruments, air conditioners, basic products not made of plastic, finished chemical products for consumption	20
<u>Category</u>	<u>(In percent)</u>																
Machinery, transport equipment and spare parts for heavy industry, agriculture, forestry, irrigation, construction, telecommunications; salt production, electricity generation, seeds and animals for reproduction, insecticides, pesticides, animal feed	1																
Medical, school and sport equipment, toys, printing equipment, photocopying machines, seafood	3																
Machinery, equipment and spare parts for light industry and handicrafts; kerosene, jet fuel, natural gas, rice, flour, live animals, raw materials, and construction materials which are not produced locally	5																
Buses, spare parts, electrical equipment, and industrial goods for consumption; textiles, office materials and equipment, fishing and household appliances, dyeing liquids, paints, barbed wire, diesel oil, gasoils and oils	10																
Four-wheel trucks, electrical utensils, movie cameras, health care products, kitchenware, watches, eye glasses, cassettes, movie projectors and related spare parts	15																
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Lao PDR: Summary of Tax System as of 1989 (Continued)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates																																										
			<table><tr><th>Category</th><th>(In percent)</th></tr><tr><td>Fresh vegetables, dried</td><td></td></tr><tr><td>vegetables, fruits, fresh</td><td></td></tr><tr><td>meat, dried meat, seasonal</td><td></td></tr><tr><td>products, vegetable oil,</td><td></td></tr><tr><td>juice, syrup, biscuits, cakes</td><td>25</td></tr><tr><td>Wood and wood products, fresh</td><td></td></tr><tr><td>flowers, brooms, brushes,</td><td></td></tr><tr><td>jewelry, electrical cords,</td><td></td></tr><tr><td>cosmetics, handbags, bags</td><td></td></tr><tr><td>made of cloth</td><td>30</td></tr><tr><td>Cigarette paper, plastic bags,</td><td></td></tr><tr><td>perfumes, soft drinks, sodas,</td><td></td></tr><tr><td>white alcohol, detergent,</td><td></td></tr><tr><td>toothpaste, hunting guns,</td><td></td></tr><tr><td>shotguns, bullets, tobacco</td><td>40</td></tr><tr><td>Coffee, tea, plywood, parquet</td><td>50</td></tr><tr><td>Cars, beer, alcohol, soap</td><td>60</td></tr><tr><td>Packed cigarettes, cigars,</td><td></td></tr><tr><td>concentrated sugar, gambling</td><td></td></tr><tr><td>equipment</td><td>70</td></tr></table>	Category	(In percent)	Fresh vegetables, dried		vegetables, fruits, fresh		meat, dried meat, seasonal		products, vegetable oil,		juice, syrup, biscuits, cakes	25	Wood and wood products, fresh		flowers, brooms, brushes,		jewelry, electrical cords,		cosmetics, handbags, bags		made of cloth	30	Cigarette paper, plastic bags,		perfumes, soft drinks, sodas,		white alcohol, detergent,		toothpaste, hunting guns,		shotguns, bullets, tobacco	40	Coffee, tea, plywood, parquet	50	Cars, beer, alcohol, soap	60	Packed cigarettes, cigars,		concentrated sugar, gambling		equipment	70
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concentrated sugar, gambling																																													
equipment	70																																												
4.2 Export duties	Levied on profits derived from exports.	Goods imported and reexported are exempt, as well as goods exported to pay debts to the nonconvertible area.	<table><tr><th>Category</th><th>(In percent)</th></tr><tr><td>Strategic goods which</td><td></td></tr><tr><td>are not processed ^{2/}</td><td>80</td></tr><tr><td>Strategic goods which</td><td></td></tr><tr><td>are processed</td><td>60</td></tr><tr><td>Of which: electricity</td><td></td></tr><tr><td>for export</td><td>80</td></tr><tr><td>Nonstrategic goods which</td><td></td></tr><tr><td>are not processed</td><td>70</td></tr><tr><td>Nonstrategic goods which</td><td></td></tr><tr><td>are processed</td><td>50</td></tr><tr><td>Goods made from imported</td><td></td></tr><tr><td>raw materials</td><td>50</td></tr><tr><td>Goods produced locally and</td><td></td></tr><tr><td>carried by passengers abroad</td><td></td></tr><tr><td>(percent of value</td><td></td></tr><tr><td>over KN 5,000)</td><td>5</td></tr><tr><td>Goods produced locally</td><td></td></tr><tr><td>and sent by mail</td><td></td></tr><tr><td>(percent of value)</td><td>2</td></tr></table>	Category	(In percent)	Strategic goods which		are not processed ^{2/}	80	Strategic goods which		are processed	60	Of which: electricity		for export	80	Nonstrategic goods which		are not processed	70	Nonstrategic goods which		are processed	50	Goods made from imported		raw materials	50	Goods produced locally and		carried by passengers abroad		(percent of value		over KN 5,000)	5	Goods produced locally		and sent by mail		(percent of value)	2		
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Lao PDR: Summary of Tax System as of 1989 (Concluded)

(All amounts in kip)

Tax	Nature of Tax	Exemptions and Deductions	Rates
5. <u>Tax incentives</u>			
	<p>New and rehabilitated domestic enterprises are exempt from profits taxes for 1-5 years, as determined on a case by case basis. New joint ventures and private enterprises with foreign invested capital are exempt from profits taxes for 2-4 years, beginning with the first profit-making year. Thereafter, a 50 percent reduction of profits tax for the first two succeeding years of tax collection may be allowed, depending on the branches or size of the investment, the volume of exported goods, and the duration and limits of operations. Moreover, losses may be carried forward and reinvested profits are not taxable.</p>		
<u>1/</u>	A flat 2 percent fee is also assessed on all earnings and paid to the Department of Diplomatic Services.		
<u>2/</u>	At the time of formulation of the new tax system, strategic goods included electricity, coffee, tobacco, cardamom, benzoin, sticklac, logs, processed wood, rattan, cattle, wild animals, minerals, and other special goods.		

Lao P.D.R.: New Monetary Reporting Format

This appendix summarizes the improvements to the monetary accounts following a STA technical assistance in November 1988. During this mission, a team member assisted the authorities in compiling the data from the fourth quarter of 1987 through the fourth quarter of 1988 on the basis of recommendations made by the technical assistance mission. The new classification emphasizes a consistent separation of financial institutions' accounts by economic sectors and by liquidity. While almost all recommendations have been implemented, the accounting systems of the banks will need to be improved in order to allow further refinement of the sectorization of the accounts.

Banking system and sectorization

In line with the NSEM, the authorities initiated a reform of the banking system, separating the central and commercial banking functions of the State Bank. In recognition of this change, a new monetary accounts system was developed. The new classification framework is based on a division of the banking system into two subsectors: the monetary authorities (MAs) and the other banking institutions (OBIs). The MAs' accounts consist of the accounts of the State Bank and those relating to operations and transactions with the IMF, which are now maintained by the BCEL. The OBIs comprise the BCEL and the two newly constituted commercial banks--the Nakhonluong Bank, and the Sethathilath Bank. In the future, any new institution that accepts deposits and/or deposit substitutes will be added to the OBIs group. Annex IV Tables 17 and 18 contain summaries of the new presentation of the accounts of the MAs and OBIs, respectively.

The banking system's assets and liabilities are separated into claims on and liabilities to the following sectors: (1) the Government, which includes the central government (including the Supreme People's Assembly, Council of Ministers, and ministries) and the 17 provincial governments (this definition of the Government is consistent with available government finance statistics); (2) the nonfinancial public enterprises (NFPEs), which, however, only includes the state enterprises; 1/ (3) the private sector, which includes private enterprises, mixed enterprises, cooperatives, social associations, and

1/ These state enterprises may include some units that may be more appropriately classified in the central government sector; although further work would be needed to improve the definition of the components of the public sector, it is important to separate at present the NFPEs from other domestic sectors, because most state enterprises have become, under the NSEM, important autonomous productive units.

individuals; and (4) the external sector, which is defined on the basis of the balance of payments residency criteria.

Data compilation

Previously, the monetary accounts were derived from aggregate data provided by the authorities; however, these data only covered part of the accounts maintained by the State Bank and the BCEL. The new framework is based on complete balance sheet data. Previously, foreign assets and liabilities were based on a currency criteria; now they are based on a residency criteria. As a result, some accounts were reclassified; for example, margin deposits, which are required by banks from resident importers for opening letters of credit, were shifted from foreign liabilities to quasi-money. In addition, foreign currency accounts used to be valued at a constant rate of KN 10 per U.S. dollar, even when the kip counterpart transactions were recorded at market rates; at present, all foreign currency accounts are valued at market rates.

Data on domestic credit obtained from the new classification for end-1987 are twice those reported previously, because part of domestic credit is denominated in foreign currency and because some loans were previously excluded from the old accounts. The main component of domestic credit is credit to state enterprises. Claims on the Government were not reported previously; however, a close review of the accounts indicated that credit had been extended. These claims were included in the new monetary accounts. Government deposits consist mainly of operating funds of the Government kept in the State Bank (in kip) and the BCEL (in foreign currency). Government deposits also include other special accounts, possibly government lending funds, which still have to be identified separately. Separate identification of valuation effects on credit flows still needs to be undertaken.

The main component of banks' liquid liabilities is the state enterprises' deposits (demand deposits in local and foreign currency). In the new classification, the foreign currency component of the deposits has been identified separately and is one of the most important liability categories of the banking system.

Other categories of accounts that have been distinguished in the new classification include reserve money, banks' reserves, capital accounts, and valuation adjustments. Detailed data on deposits and banks' reserves would facilitate the monitoring of the reserve requirements, once these are in place.

Data reporting

A new format to report data to the Fund has been established, as well as a cable report form to obtain essential financial data in a timely fashion. A call report form to collect data from the commercial

banks is being introduced to facilitate the consolidation of the OBI sector. Compilation problems remain because of communication difficulties with outlying branches of the State Bank. The staff recommended that data from the five provinces around Vientiane, accounting for about three-fourths of banking transactions, be used as a proxy for the entire banking system. These branches and banks can be reached by telephone. As data become available from the remote regions, the accounts would be updated accordingly. Timely data are available on foreign exchange holdings of the State Bank and the BCEL, and on currency issued by the State Bank. The definitions of the economic sectors (Government, NFPEs, and private sector) are to be distributed to all the banks and branches in order to obtain consistent data on the accounts relating to these sectors.

Table 5. Lao P.D.R.: Estimates of Net Material Product and GDP,
1984-88 1/ 2/

(In billions of kip)

	1984	1985	1986	1987 Est.	1988 Est.
Net material product at 1987 prices	87.5	95.6	102.7	97.9	98.9
Agriculture and forestry	67.1	72.7	77.9	74.5	73.8
Industry	5.9	7.0	8.3	8.6	8.5
Construction	1.6	2.3	2.1	2.3	2.6
Transport and communications	2.5	2.7	2.7	1.6	1.8
Commerce <u>3/</u>	8.9	9.3	9.7	8.8	9.6
Other	1.4	1.7	2.0	2.1	2.6
Depreciation <u>4/</u>	5.3	5.7	6.2	6.1	6.2
Nonmaterial services <u>5/</u>	10.6	11.4	11.9	13.7	15.1
GDP at 1987 prices	103.4	112.8	120.7	117.7	120.1
GDP deflator	30.1	55.6	79.4	100.0	167.9
GDP at current prices	31.1	62.7	95.9	117.7	201.7
(Percentage changes)					
Net material product, 1987 prices	7.2	9.3	7.4	-4.6	1.0
GDP at 1987 prices	6.4	9.1	7.1	-2.5	2.0
GDP deflator	11.1	84.8	42.8	26.1	67.9
GDP at current prices	32.0	101.7	52.9	22.9	71.4

Source: Staff estimates based on data provided by the Lao authorities.

1/ The national accounts are established according to the Material Product System (MPS), which differs from the U.N. System of National Accounts (SNA). In particular, the value of depreciation and nonmaterial services is excluded from the MPS and must be estimated to obtain GDP figures. However, the official estimate of NMP covers only public sector activity in all sectors. In addition, the quality of price data used to compute value added is weak. Hence, both NMP and real and nominal GDP are believed to be substantially understated.

2/ Components may not add to totals owing to rounding.

3/ The data for commerce refer to the state sector and exclude the private sector.

4/ Estimated as 6 percent of net material product.

5/ Nonmaterial services include private sector commerce and are estimated as a percent of net material product.

Table 6. Lao P.D.R.: Gross Domestic Product: Sector Shares and Growth Rates, 1984-88

	1984	1985	1986	1987 Est.	1988 Est.
	(Percentage share)				
GDP at constant prices	100.0	100.0	100.0	100.0	100.0
Agriculture and forestry	64.3	63.5	63.6	62.2	60.9
Industry	7.0	7.6	8.4	8.3	8.7
Construction	3.0	3.8	3.3	3.8	3.9
Transport and communications	1.3	1.2	1.2	1.4	1.5
Commerce <u>1/</u>	8.3	7.9	7.7	7.7	7.8
Other	0.7	0.8	0.8	0.8	0.8
Amortization	5.1	5.1	5.1	5.1	5.0
Nonmaterial services	10.3	10.1	9.9	10.7	11.3
	(Percentage change from the previous year)				
GDP at constant prices	6.4	9.1	7.1	-2.5	2.0
Agriculture and forestry	7.3	8.3	7.2	-4.3	-1.0
Industry	6.1	18.8	18.4	4.2	-1.0
Construction	17.1	41.0	-9.4	12.4	10.0
Transport and communications	7.0	6.2	2.1	-41.9	10.0
Commerce <u>1/</u>	4.3	4.1	4.3	-9.4	10.0
Other	5.9	19.0	18.4	4.3	25.0

Source: Staff estimates based on data provided by the Lao authorities.

1/ The data for commerce refer to the state sector and exclude the private sector.

Table 7. Lao P.D.R.: Agricultural Output Index, 1984-88

	Weights	1984	1985	1986	1987	1988 Est.
(1982 = 100)						
Gross agricultural output	<u>1.000</u>	<u>116.1</u>	<u>124.6</u>	<u>123.8</u>	<u>114.5</u>	<u>112.7</u>
Crops	<u>0.720</u>	<u>117.6</u>	<u>126.9</u>	<u>127.3</u>	<u>111.1</u>	<u>107.8</u>
Paddy	0.549	120.9	130.8	132.7	110.5	91.8
Roots and tubers	0.048	100.8	104.4	68.4	108.0	229.9
Coffee	0.027	111.5	113.5	96.2	132.7	150.0
Vegetables	0.023	100.2	101.6	92.9	124.5	129.2
Maize	0.017	97.7	103.5	119.6	103.5	146.7
Groundnuts	0.016	96.7	103.3	122.8	63.0	48.9
Soybeans	0.011	85.7	126.2	173.8	81.0	104.8
Tobacco leaves	0.011	83.8	111.7	184.8	115.2	151.3
Fruits	0.008	100.6	100.6	100.6	100.6	113.2
Cotton	0.007	98.1	90.4	50.0	57.7	82.7
Animal husbandry	<u>0.280</u>	<u>112.2</u>	<u>118.8</u>	<u>114.9</u>	<u>123.4</u>	<u>125.4</u>
(Percentage changes)						
Gross agricultural output		14.3	7.3	-0.6	-7.5	-1.5
Of which: Paddy		20.0	8.1	1.5	-16.7	-16.9
Roots and tubers		-3.5	3.5	22.5	22.0	112.9
Coffee		9.4	1.7	13.6	16.4	13.0
Animal husbandry		6.0	5.9	-3.3	7.4	1.6

Source: Staff estimates based on data provided by the Lao authorities.

Table 8. Lao P.D.R.: Selected Agricultural Statistics, 1984-88

(In hectares, metric tons per hectares, metric tons, and head, as indicated)

	1984	1985	1986	1987 Est.	1988 Plan
Production ('000 metric tons)					
Paddy	1,321.1	1,428.5	1,449.2	1,207.1	1,003.3
Rainfed lowland	(919.3)	(1,019.9)	(1,081.9)	(950.7)	(686.1)
Irrigated area <u>1/</u>	(21.4)	(27.2)	(27.3)	(28.7)	(34.5)
Upland	(380.4)	(381.4)	(340.0)	(227.7)	(282.7)
Vegetables	45.0	45.6	41.7	...	...
Maize	33.9	35.9	41.5	35.9	50.9
Cotton	5.1	4.7	2.6	3.0	4.3
Coffee	5.8	5.9	5.0	6.9	7.8
Tobacco	16.5	22.0	36.4	22.7	29.8
Root crops	96.6	100.0	65.5	103.5	220.2
Groundnuts	8.9	9.5	11.3	5.8	4.5
Mung beans	1.8	2.2	2.6	1.8	2.2
Soybeans	3.6	5.3	7.3	3.4	4.4
Tea	0.61	0.68	0.6	1.0	1.4
Sugarcane	54.5	83.1	112.0	81.8	107.1
Area ('000 hectares)					
Paddy	655.1	689.8	651.6	551.6	536.2
Rainfed lowland	(360.3)	(396.3)	(385.0)	(356.7)	(311.3)
Irrigated area <u>1/</u>	(8.6)	(10.1)	(10.1)	(9.6)	(11.4)
Upland	(286.2)	(283.4)	(256.5)	(185.3)	(213.5)
Vegetables	5.5	5.6	6.5	...	...
Maize	28.6	30.4	29.6	28.8	37.8
Cotton	7.2	7.5	4.2	4.9	6.6
Coffee	11.1	12.8	13.1	14.5	15.5
Tobacco	3.9	5.1	8.0	5.5	7.1
Root crops	11.9	12.4	8.7	14.7	27.8
Groundnuts	11.6	12.2	14.0	4.7	5.4
Mung beans	3.1	3.7	4.3	3.3	3.5
Soybeans	5.2	7.0	9.5	4.6	5.9
Tea	0.2	0.2	0.2	0.2	0.3
Sugarcane	2.0	3.0	4.0	2.9	3.9
Yield (MT/hectare)					
Paddy	2.00	2.10	2.22	2.19	1.87
Rainfed lowland	(2.55)	(2.57)	(2.81)	(2.66)	(2.20)
Irrigated area <u>1/</u>	(2.49)	(2.70)	(2.70)	(2.97)	(3.02)
Upland	(1.32)	(1.35)	(1.32)	(1.23)	(1.32)
Vegetables	8.1	8.2	8.3	...	...
Maize	1.2	1.2	1.4	1.2	1.4
Cotton	0.7	0.6	0.6	0.6	0.6
Coffee	0.5	0.5	0.4	0.4	0.5
Tobacco	4.2	4.4	4.6	4.1	4.4
Root crops	8.1	8.1	7.5	7.0	7.9
Groundnuts	0.8	0.8	0.8	1.2	0.8
Mung beans	0.6	0.6	0.6	0.5	0.6
Soybeans	0.7	0.8	0.8	0.7	0.7
Tea	3.8	3.8	4.1	4.2	4.3
Sugarcane	27.6	27.7	28.0	27.7	27.0
(In thousands of head)					
Livestock					
Buffalo	936.8	974.4	980.1	1,011.1	1,040.7
Cattle	544.0	576.0	646.1	716.3	851.7
Sheep and goats	63.0	66.6	74.4	76.0	89.2
Pigs	1,360.0	1,433.0	1,280.6	1,321.7	1,267.9
Poultry	7,203.0	7,834.0	6,797.8	7,780.0	6,868.5

Source: Data provided by the Lao authorities.

1/ Area cultivated both during the rainy and dry seasons.

Table 9. Lao P.D.R.: Industrial Output Index, 1984-88

	Weights	1984	1985	1986	1987	1988 Est.
(1985 = 100)						
Gross industrial output	<u>1,000</u>	<u>83.5</u>	<u>100.0</u>	<u>100.5</u>	<u>85.9</u>	<u>82.4</u>
Manufacturing	0.385	64.1	100.0	108.4	121.9	122.0
Of which:						
Food and agro-industries <u>1/</u>	0.069	90.0	100.0	120.3	149.0	169.5
Construction materials	0.011	41.5	100.0	104.7	129.3	141.6
Mining	0.063	82.6	100.0	103.8	77.7	64.6
Energy	0.552	97.3	100.0	94.7	61.8	56.8
(Percentage change)						
Gross industrial output		-1.4	19.7	0.5	-14.5	-4.1
Manufacturing		-13.7	56.1	8.4	12.5	0.1
Mining		25.6	21.1	3.8	-25.2	-16.9
Energy		3.2	2.8	-5.3	-34.7	-8.0
Memorandum items:						
Gross industrial output						
Excluding mining (percent change)		-5.8	18.7	3.0	-18.8	...
Excluding energy (percent change)		-22.3	69.5	18.8	10.6	...
Tin production (metric tons)		430	520	559	201.2	245.9
Gypsum production ('000 metric tons)		82	100	100	59	80
Salt production ('000 metric tons)		7.8	9.1	8.6	13.8	...

Source: Staff estimates based on data provided by the Lao authorities.

1/ Excluding rice milling and the processing of cash crops.

Table 10. Lao P.D.R.: Consumer Prices in Vientiane, 1984-89

	Est. CPI	Free market prices						Official prices
		Total	Food	<u>1/</u> Rice	Clothing	Energy	Other	
Historical index <u>2/</u>								
Weights	1.000	0.500	0.239	0.067	0.027	0.046	0.188	0.500
(Percentage change over 12 months; end of period)								
1984	28.2	40.3	28.6	-13.3	105.8	63.5	40.6	7.7
1985	136.8	30.3	58.6	93.7	-0.8	35.9	13.0	371.3
1986	15.0	23.1	23.7	48.9	-10.2	51.4	21.8	10.0
1987	9.8	11.5	20.7	36.0	128.8	-4.1	-5.5	8.7
1988 I	22.3	16.8	25.5	31.3	109.4	36.5	-6.5	26.0
II	23.9	11.3	15.1	11.1	108.4	1.1	-2.8	32.8
III	28.2	27.0	3.4	-4.2	146.2	13.7	48.2	29.0
IV	52.9	39.7	20.1	17.7	135.7	-3.3	54.2	62.2
(Average percentage change over previous period)								
1984	27.2	43.4	19.6	-16.5	89.4	43.9	61.7	3.1
1985	114.7	29.2	46.7	59.8	29.5	43.1	14.9	290.8
1986	35.0	34.0	59.8	71.6	9.0	55.9	10.4	35.7
1987	6.6	9.0	7.8	23.3	16.8	-0.3	11.7	5.0
1988	32.6	25.0	15.4	12.2	127.3	11.6	22.9	38.0
New index <u>3/</u>								
Weights		1.000	0.588	0.113	0.026	0.145	0.241	...
(Percentage change over 12 months; end of period)								
1988 IV		18.4	18.0	7.8	125.5	-1.2	46.6	...
(Percentage change over preceding period)								
1988 Nov.		1.7	3.3	6.2	3.3	0.0	0.5	...
Dec.		2.7	1.1	-8.3	38.3	0.0	3.4	...
1989 Jan.		3.5	6.5	0.0	0.3	-0.1	3.0	...
Feb.		1.1	2.1	0.0	0.0	0.0	0.5	...

Source: Staff estimates based on data provided by the Lao authorities.

1/ Excludes rice.

2/ This index uses weights established to approximate the consumption basket of an average wage earner in Vientiane. Both official and free market consumption are included with each market being given a weight of 50 percent.

3/ The new index is based only on the evolution of free market prices and reflects the fact that in 1988 retail prices of most commodities (except electricity, water, domestic air transport, post and telecommunications and minerals) were decontrolled by October 1988. The weights have been adjusted to reflect this change.

Table 11. Lao P.D.R.: Free Market Prices in Vientiane, 1984-88

(In kip per unit; end of period)

	Unit	1984	1985	1986	1987	1988			
						Mar.	June	Sept.	Dec.
Food and beverages									
Rice	kg	26	50.4	75	102	105	100	120	120
Pork	kg	300	575	550	550	530	550	600	680
Chicken	kg	300	625	665	550	580	650	620	780
Cooking oil	liter	130	130	270	330	300	300	340	410
Vegetables	kg	60	49.5	60	100	120	160	140	90
Sugar	kg	190	181.3	145	175	160	160	185	195
Condensed milk	can	170	249.7	190	170	170	150	200	220
Eggs	item	15	20	28	28	30	30	33	35
Fish	kg	300	644.7	820	970	1,140	1,250	950	1,250
Salt	kg	5	19.0	40	35	36	50	50	50
Beer	bottle	60	100	130	150	150	150	150	165
Clothing									
Shoes	pair	450	507	450	2,500	2,500	2,500	3,000	7,830
Pants	pair	...	2,000	3,500	...	...	...	...	...
Shirt	item	600	450	650	1,000	1,500	1,500	2,930	3,000
Skirt	item	700	917	875	1,000	1,170	1,130	1,100	1,580
Fabric	meter	450	370	265	400	400	400	300	280
Energy									
Gasoline <u>1/</u>	liter	60	89.5	150	140	200	110	110	100
Charcoal	kg	17	20	35	35	35	40	50	50
Battery	item	120	157	158	155	155	155	155	160
Other									
Rent	month	1,800	1,800	3,000	3,000	3,000	3,000	5,000	5,000
Bicycle	item	24,000	34,000	25,000	22,000	22,000	22,000	22,000	22,000
Cigarettes	pack	250	313	200	140	130	140	140	180
Pencil	item	15	30	30	35	25	30	35	35
Soap	item	120	176	170	160	150	110	110	140
Detergent	kg	130	213	200	210	180	170	250	290
Electric bulb	item	110	150	170	165	160	160	180	160

Source: Data provided by the Lao authorities.

1/ Variability in recorded gasoline prices reflects trends in world market prices adjusted for the subsidization of imports from the nonconvertible currency area, as well as disruptions to supplies stemming from temporary border disputes.

Table 12. Lao P.D.R.: Official Retail Prices in Vientiane, 1984-88

(In kip per unit)

	Unit	1984	1985	1986	1987				1988 1/			
		Dec.	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.
Rice 2/ Civil servants	kg	3)										
Public enterprise employees		) 6.2)	27	27	27	27	27	27	27	27	27	...
Sugar 2/	kg	8	144	144	144	144)						
Sugar 3/	kg	110	160	160	180	180)	160	160	...	...	...	...
Pork	kg	80	280	300	300	300	300	300	...	...	...	...
Beef	kg	120	350	450	500	500	600	600	...	...	...	...
Fish	kg	30	160	280	285	285	300	300	...	...	...	...
Condensed milk	can	50	126	144	144	144	150	180	180	...	...	...
Salt	kg	4	9	9	9	9	...	...	...	...	...	...
Eggs	item	4.5	22	22	22	22	22	22	22	22	27	...
Detergent 2/	kg	16	210)									
Detergent 3/	kg	90	220)	200	200	200	200	200	200	200	...	...
Cloth	item	...	350	350	350	350	350	350	...	...	...	...
Gasoline 4/	liter	12.5	50	50	50	100	50	50	115	...	...	...
Electricity	kwh	0.4	7	7	7	7	7	7	7	7	7	7
Bus tickets	item	8	30	30	30	30	35	35	50	50	50	...

Source: Data provided by the Lao authorities.

1/ Starting in March 1988, official prices were gradually decontrolled; by October 1988, only electricity, domestic airfares, post and telecommunications and mineral products were still set by the Government.

2/ Subsidized price.

3/ Price of sales in excess of ration limit.

4/ For motorcycle owners. Twenty liters are distributed to automobile owners.

Table 13. Lao P.D.R.: General Government Revenue, 1984-88

(In millions of kip)

	1984	1985	1986	1987	1988
Tax revenue	<u>1,669</u>	<u>1,398</u>	<u>1,755</u>	<u>1,970</u>	<u>21,409</u>
Tax on industrial and commercial profits	250	170	195	210	6,223
Tax on wages and salaries	15	11	14	18	22
Agricultural tax	228	250	450	400	1,213
Business licenses	10	8	10	12	30
Turnover tax	960	786	870	930	7,352
Of which:					
Public enterprises	(453)	(424)	(530)	(580)	(5,730)
Tax on foreign trade	181	160	197	380	6,463
Import duties	150	124	146	320	4,846
Of which:					
Public enterprises	(70)	(66)	(111)	(300)	(4,701)
Export duties	31	36	51	60	1,617
Of which:					
Public enterprises	(24)	(30)	(45)	(55)	(1,596)
Other	25	13	19	20	106
Nontax revenue	<u>3,279</u>	<u>8,902</u>	<u>16,748</u>	<u>18,138</u>	<u>6,801</u>
Surpluses of public enterprises	<u>2,489</u>	<u>6,677</u>	<u>13,890</u>	<u>15,548</u>	<u>517</u>
Depreciation allowances transferred by public enterprises	473	1,084	1,050	950	2,411
Other	317	1,141	1,808	1,640	3,873
Total	<u>4,948</u>	<u>10,300</u>	<u>18,503</u>	<u>20,108</u>	<u>28,210</u>

Source: Data provided by the Lao authorities.

Table 14. Lao P.D.R.: Economic Classification of
General Government Expenditure, 1984-88

(In millions of kip)

	1984	1985	1986	1987	1988	
					Budget	Est.
Current expenditure	4,121	9,542	14,813	16,025	20,029	26,722
Wages and salaries	580	2,520	4,760	5,135	6,420	11,250
Materials and supplies	3,419	6,809	9,875	10,640	13,302	14,238
Pensions	10	27	45	60	73	250
Debt service	112	186	133	190	234	984
Capital expenditure	4,259	10,184	11,732	13,480	16,152	52,628
Education	90	265	780	1,139	1,000	1,920
Health	170	601	714	805	820	1,257
Agriculture and forestry	1,010	1,549	1,993	2,086	3,048	6,710
Industry, mining and energy	1,366	1,556	1,208	1,276	2,700	8,510
Transportation and communi- cations	551	3,717	4,491	4,886	5,370	15,187
Trade and cooperatives	171	489	442	808	780	1,420
Public works	706	496	654	720	620	1,300
Other	195	1,511	1,450	1,760	1,814	4,198
Additional valuation revisions	...	...	...	...	...	5,786
Unallocated expenditures	...	...	...	...	...	6,340
Total	8,380	19,726	26,545	29,505	36,181	79,350

Sources: Data provided by the Lao authorities; and staff estimates.

Table 15. Lao P.D.R.: Functional Classification of
General Government Expenditure, 1984-88

(In millions of kip)

	1984	1985	1986	1987	1988	
					Budget	Est.
General public services <u>1/</u>	<u>2,696</u>	<u>6,732</u>	<u>11,070</u>	<u>12,544</u>	<u>15,229</u>	<u>20,728</u>
Economic services	<u>4,448</u>	<u>9,154</u>	<u>9,938</u>	<u>10,727</u>	<u>13,768</u>	<u>35,428</u>
Agriculture	<u>1,293</u>	<u>1,950</u>	<u>2,393</u>	<u>2,515</u>	<u>3,558</u>	<u>7,828</u>
Forestry,)						
Industry, mining,)	1,509	1,910	1,518	1,530	3,080	9,039
and energy)						
Transport and communications)	689	4,070	4,611	4,984	5,520	15,628
Cooperatives)						
Public works)	754	621	834	901	890	1,412
Other)	203	603	582	797	720	1,521
Social services	<u>1,123</u>	<u>3,653</u>	<u>5,404</u>	<u>6,044</u>	<u>6,950</u>	<u>10,084</u>
Education	<u>698</u>	<u>1,825</u>	<u>2,430</u>	<u>2,891</u>	<u>3,161</u>	<u>4,653</u>
Public health	<u>394</u>	<u>1,499</u>	<u>2,104</u>	<u>2,462</u>	<u>2,878</u>	<u>3,621</u>
Pensions	<u>10</u>	<u>27</u>	<u>45</u>	<u>60</u>	<u>115</u>	<u>250</u>
Other	<u>21</u>	<u>312</u>	<u>825</u>	<u>631</u>	<u>796</u>	<u>1,560</u>
Additional valuation revisions	...	...	...	...	...	5,786
Unallocated expenditures	...	...	...	...	...	6,340
Public debt service	<u>112</u>	<u>186</u>	<u>133</u>	<u>190</u>	<u>234</u>	<u>984</u>
Total expenditure	<u>8,380</u>	<u>19,726</u>	<u>26,545</u>	<u>29,505</u>	<u>36,181</u>	<u>79,350</u>

Sources: Data provided by the Lao authorities; and staff estimates.

1/ Including general administration and national security.

Table 16. Lao P.D.R.: Interest Rates, 1979-89
(In percent per annum, unless otherwise indicated)

	Prior to June 1979	June 1979	July 1985	October 1988	January 1989
Deposit rates					
Private sector					
Savings deposits	1.2	3.6	5.4	7.2	7.2
Time deposits					
Three-month	3.6	5.0	...		
Six-month	3.6	4.0	7.8	10.0	10.0
One-year	3.6	7.2	9.6	14.0	14.0
Two-year	...	...	12.0	18.0	18.8
Three-year	...	...	15.0	18.0	18.0
Public enterprises	--	--	1.0-3.0	... <u>1/</u>	... <u>1/</u>
Foreign currency deposits	--	--	--	--	--
Certificates of deposit (per month) <u>2/</u>	...	...	...	...	3.0
Lending rates					
For agriculture, industry and transportation					
Short-term	6.0	4.8	4.2-8.4	10.0-15.0	10.0-15.0
Long-term	3.0	3.0	3.0-4.2	6.0-10.0	6.0-10.0
For trade					
Private	...	12.0	15.0	15.0	15.0
Public	12.0	7.2	6.1-7.8	15.0	15.0
Loans from certificates of deposit (per month) <u>2/</u>	...	...	...	...	6.0

Source: Data provided by the Lao authorities.

1/ Interest rates for public sector deposits were eliminated. Enterprises continue to hold most of their funds in non-interest bearing demand accounts.

2/ These instruments can only be offered by commercial banks. The rates presented are those presently paid by the commercial banks on these instruments; ceiling deposit and loan rates have been set at 12.5 percent per month and 15 percent per month, respectively.

Table 17. Lao P.D.R.: Monetary Authorities, 1987-88 ^{1/}

(In millions of kip; end of period)

	1987	1988			
	Q4	Q1	Q2	Q3	Q4
Assets					
Foreign assets	6	307	202	473	296
Gold	6	6	6	6	6
Foreign exchange holdings	--	301	196	467	290
Reserve position in the Fund	--	--	--	--	--
SDR holdings	--	--	--	--	--
Claims on Government	2,193	2,451	1,903	1,949	1,257
Loans, advances, and overdrafts	--	624	378	573	120
Treasury -IMF	2,193	1,827	1,525	1,376	1,137
Securities	183	183	183	183	183
Less: Subscriptions	-307	-307	-307	-307	-307
SDRs used by Government	117	117	117	117	117
Trust Fund loans	2,200	1,834	1,532	1,383	1,144
Claims on nonfinancial enterprises	8,732	12,888	11,260	12,004	9,712
Loans, advances, and overdrafts	6,772	10,729	9,210	9,953	9,712
Doubtful claims	1,960	2,159	2,050	2,051	--
Claims on private sector	110	194	657	1,072	678
Claims on other banking institutions	227	227	227	227	593
Liabilities					
Reserve money	6,830	9,177	7,232	9,650	10,318
Of which:					
Currency outside banks	2,091	3,252	3,802	3,754	3,486
Private sector deposits	785	674	673	556	780
Public enterprises deposits	3,826	4,799	1,894	2,606	5,200
Savings and special deposits	112	432	737	541	520
Foreign liabilities	2,200	1,834	1,532	1,383	1,144
Use of Fund credit	--	--	--	--	--
Trust Fund loans	2,200	1,834	1,532	1,383	1,144
Government deposits	706	480	1,573	1,011	1,400
Other items (net)	1,532	4,576	3,913	3,681	-326
Of which:					
Capital and reserves		2,139	2,529	3,089	993
Interbank transactions (net)	765	1,574	-381	372	894
Transfers to branches	--	--	--	--	-2,134

Source: Data provided by the Lao authorities.

^{1/} Comprise the accounts of the State Bank and the accounts relating to operations and transactions with the IMF.

Table 18. Lao P.D.R.: Other Banking Institutions, 1987-88 1/

(In millions of kip; end of period)

	1987	1988			
	Q4	Q1	Q2	Q3	Q4
Assets					
Reserves	16	20	125	866	961
Foreign assets	10,942	11,354	12,022	14,630	12,985
Foreign currency holdings	3,506	1,984	2,298	2,295	2,936
Foreign bills	325	349	383	421	509
Accounts with foreign banks	6,141	8,051	8,276	10,841	8,467
Bilateral arrangements	970	970	1,065	1,073	1,073
Claims on Government	3,593	4,152	5,225	7,471	4,852
Claims on nonfinancial public enterprises	6,599	6,508	10,639	10,984	13,143
Claims on private sector	--	--	183	188	192
Liabilities					
Demand deposits	186	280	2,867	2,478	2,638
Of which: Public enterprises	51	58	2,636	2,296	2,308
Time and savings deposits	--	--	77	371	564
Of which: Public enterprises	--	--	--	--	--
Foreign currency deposits (residents)	8,894	7,811	10,986	8,875	9,475
Of which: Public enterprises	(8,894)	(7,811)	(10,986)	(8,790)	(9,278)
Restricted deposits	1,603	3,566	2,723	1,929	1,458
Special deposits	1,043	3,009	2,171	1,372	913
Blocked deposits	560	557	552	557	545
Government deposits	357	144	679	4,359	2,438
Foreign liabilities	10,662	10,647	9,012	11,492	11,751
Short-term liabilities	--	--	--	745	667
Bilateral arrangements <u>2/</u>	7,959	7,944	6,519	7,861	7,991
Long-term debt	2,703	2,703	2,493	2,886	3,093
Nonconvertible currency area	...	...	...	438	453
Convertible currency area	...	...	...	1,759	1,890
Multilateral organizations	...	...	...	689	750
Other items (net) <u>3/</u>	-556	-414	1,850	4,634	3,808

Source: Data provided by the Lao authorities.

1/ Comprises the accounts of the BCEL (excluding the accounts relating to operations and transactions with the IMF), the Nakhonluong Bank, and the Sethathilath Bank. Foreign currency accounts are valued at end-of-period market rates.

2/ Included in this account are the bilateral payments arrangements with the nonconvertible currency area as well as the registry of trade flows with these countries.

Table 19. Lao P.D.R.: Composition of Exports 1984-88 ^{1/}

	1984	1985	1986	1987	1988 Est.
(In millions of U.S. dollars)					
Total exports	43.9	53.6	55.0	62.1	57.6
Convertible area	30.1	34.6	39.4	33.0	36.6
Coffee	0.6	0.3	2.1	0.9	0.5
Hydroelectric power	25.2	25.7	29.8	11.6	11.1
Logs	3.3	3.8	4.9	17.9	18.2
Wood products	0.4	1.8	0.6	1.6	2.6
Other	0.6	3.0	2.0	1.0	4.2
Nonconvertible area	13.8	19.0	15.6	29.1	21.0
Coffee	8.1	8.2	7.1	8.5	6.8
Logs and wood products	1.3	5.6	2.3	13.3	9.3
Tin	1.3	1.1	2.8	1.9	2.1
Gypsum	1.0	1.4	2.2	2.3	1.1
Other	2.1	2.7	1.2	3.1	1.8
(In percent of total exports)					
Total exports	100	100	100	100	100
Convertible area	68.5	64.6	71.6	53.1	63.5
Coffee	1.4	0.5	3.8	1.4	0.9
Hydroelectric power	57.4	47.9	54.2	18.7	19.2
Logs	7.5	7.1	9.0	28.8	31.6
Wood products	0.8	3.4	1.0	2.6	4.4
Other	1.3	5.7	3.6	1.6	7.3
Nonconvertible area	31.5	35.4	28.4	46.9	36.5
Coffee	18.5	15.3	12.9	13.7	11.7
Logs and wood products	3.0	10.4	4.1	21.4	16.1
Tin	3.0	2.1	5.1	3.1	3.6
Gypsum	2.3	2.6	4.0	3.7	1.9
Other	4.8	5.0	2.3	5.0	3.1

Sources: Data provided by the Lao authorities; and staff estimates.

^{1/} Components may not add to totals owing to rounding.

Table 20. Lao P.D.R.: Composition of Imports, 1984-88

(In millions of U.S. dollars) 1/

	1984	1985	1986	1987	1988 Est.
(In millions of U.S. dollars)					
Nonaid imports					
Convertible area	35.4	38.3	41.1	55.6	54.1
Rice and other food	4.0	1.7	3.0	7.7	5.7
Petroleum products	10.8	10.6	7.8	6.4	5.3
Machinery and raw materials	10.3	11.1	12.3	14.8	8.9
Other official imports	5.3	7.7	9.4	17.2	15.8
Private imports	4.9	2.2	3.6	4.5	9.2
Provincial imports	--	5.0	5.0	5.0	9.2
Nonconvertible area	62.0	66.6	71.5	82.4	53.4
Imports under aid programs	64.5	88.3	73.1	78.2	80.5
Convertible area	23.9	39.3	37.3	26.1	36.3
Nonconvertible area	40.6	49.0	35.8	52.1	44.2
Total imports	161.9	193.2	185.7	216.2	188.0
Convertible area	59.3	77.6	78.4	81.7	90.4
Nonconvertible area	102.6	115.6	107.3	134.5	97.6
(In percent of total imports)					
Nonaid imports	60.2	54.3	60.6	63.8	57.2
Convertible area	21.9	19.8	22.1	25.7	28.8
Nonconvertible area	38.3	34.5	38.5	38.1	28.4
Imports under aid programs	39.8	45.7	39.4	36.2	42.8
Convertible area	14.8	20.3	20.1	12.1	19.3
Nonconvertible area	25.0	25.4	19.3	24.1	23.5
Total imports	100.0	100.0	100.0	100.0	100.0
Convertible area	36.6	40.2	42.2	37.8	48.1
Nonconvertible area	63.4	59.8	57.8	62.2	51.9

Sources: Data provided by the Lao authorities; and staff estimates.

1/ Components may not add to totals owing to rounding.

Table 21. Lao P.D.R.: External Debt Disbursed and Outstanding, 1984-88

(In millions of U.S. dollars; end-of-period) 1/

	1984	1985	1986	1987 Est.	1988 Proj.
Convertible area	124.7	160.9	171.9	178.8	195.2
Suppliers' credits	2.8	3.0	3.0	3.0	4.7
Bilateral creditors	46.1	77.4	74.3	70.1	69.4
France	(4.8)	(6.6)	(6.6)	(6.6)	(6.6)
Germany, Fed. Rep.	(19.5)	(33.0)	(31.5)	(29.8)	(28.9)
Indonesia	(1.0)	(1.0)	(1.0)	(1.0)	(0.8)
Japan	(20.7)	(36.7)	(35.1)	(32.6)	(33.0)
Other 2/	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Multilateral creditors	66.7	77.4	93.6	104.7	120.1
AsDB	(20.5)	(24.9)	(34.2)	(35.5)	(41.9)
EC	(0.7)	(1.4)	(1.4)	(1.8)	(2.2)
IDA	(25.7)	(31.8)	(39.8)	(48.3)	(57.2)
IFAD	(--)	(0.5)	(0.7)	(3.4)	(6.5)
OPEC	(8.5)	(8.5)	(9.0)	(9.5)	(9.7)
Trust Fund, IMF	(11.3)	(10.3)	(8.5)	(6.2)	(2.6)
Foreign liabilities of the monetary authorities	9.1	3.1	1.0	1.0	1.0
IMF	(8.1)	(2.1)	(0.0)	(0.0)	(0.0)
Other	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)
Nonconvertible area	318.7	341.7	432.3	535.8	631.0
Bulgaria	2.5	4.4	4.9	4.7	5.5
China	20.0	20.0	20.0	20.0	19.3
Czechoslovakia	2.0	3.6	5.0	5.9	8.7
Germany, Dem. Rep.	1.8	3.5	3.8	6.8	6.1
Hungary	1.1	1.9	3.3	5.3	7.4
Poland	0.9	1.0	1.2	1.4	3.4
U.S.S.R.	288.0	298.7	384.4	481.7	569.2
Viet Nam	2.4	8.6	9.7	10.0	11.4
Total debt	443.4	502.6	604.1	714.5	826.1
Short-term					
(convertible area)	2.8	3.0	3.0	3.0	4.7
Medium- and long-term					
nonmonetary	431.5	496.5	600.1	710.5	820.4
Convertible area	(112.8)	(154.8)	(167.8)	(174.7)	(189.4)
Nonconvertible area	(318.7)	(341.7)	(432.3)	(535.8)	(631.0)
Monetary debt					
(convertible area)	9.1	3.1	1.0	1.0	1.0

Sources: Data provided by the Lao authorities, IBRD, Fund accounts, and staff estimates.

1/ Components may not add to totals owing to rounding.

2/ The United Kingdom and the United States.

Table 22. Lao P.D.R.: External Aid Disbursements, 1984-88

(In millions of U.S. dollars)

	1984	1985	1986	1987	1988 Est.
Use of disbursements					
Aid in kind	8.2	10.3	6.0	11.0	14.9
Convertible zone	1.5	6.1	4.0	5.2	6.6
Nonconvertible zone	6.7	4.2	2.0	5.8	8.3
Project aid	56.3	78.0	67.1	67.2	65.6
Convertible zone	22.4	33.2	33.3	20.9	29.7
Nonconvertible zone	33.9	44.8	33.8	46.3	35.9
Technical assistance	17.9	23.4	13.1	14.3	25.9
Convertible zone	12.9	18.2	9.5	10.3	21.4
Nonconvertible zone	5.0	5.2	3.6	4.0	4.5
Total	<u>82.4</u>	<u>111.7</u>	<u>86.2</u>	<u>92.5</u>	<u>106.4</u>
Sources of disbursements					
Official transfers	42.1	49.6	30.5	27.0	38.5
Convertible zone	26.7	45.4	26.0	23.0	34.0
Nonconvertible zone	15.4	4.2	4.5	4.0	4.5
Loans	40.3	62.1	55.7	65.5	67.9
Convertible zone	10.1	12.1	20.8	13.4	23.7
Nonconvertible zone <u>1/</u>	30.2	50.0	34.9	52.1	44.2
Total	<u>82.4</u>	<u>111.7</u>	<u>86.2</u>	<u>92.5</u>	<u>106.4</u>

Sources: Data provided by the Lao authorities; and staff estimates.

1/ Excluding loan disbursements related to deficits under bilateral trade arrangements.

Table 23. Lao P.D.R.: External Debt Service, 1984-88 1/

(In millions of U.S. dollars)

	1984	1985	1986	1987	1988 Est.
Convertible area	11.3	13.5	10.8	12.1	10.8
Principal	8.1	11.0	8.7	9.4	8.2
Interest	3.2	2.5	2.1	2.7	2.6
Bilateral creditors	1.9	2.1	2.9	5.5	4.0
Principal	1.2	1.4	2.2	4.4	3.1
Interest	0.7	0.7	0.7	1.1	0.9
Multilateral creditors	9.4	11.4	7.9	6.6	6.8
Principal	6.9	9.6	6.5	5.0	5.1
Of which: IMF <u>2/</u>	(5.9)	(8.6)	(5.2)	(3.3)	(3.4)
Interest	2.5	1.8	1.4	1.6	1.7
Of which: IMF <u>2/</u>	(2.0)	(1.2)	(0.9)	(0.8)	(0.8)
Nonconvertible area	1.9	3.3	1.8	1.8	1.8
Principal	1.9	3.3	1.8	1.8	1.8
Interest	--	--	--	--	--
Total debt service	13.2	16.8	12.6	13.9	12.6
Principal	10.0	14.3	10.5	11.2	10.0
Interest	3.2	2.5	2.1	2.7	2.6
Memorandum items:					
Debt service ratio <u>3/</u>	22.4	22.3	15.9	15.8	15.6
Convertible area	19.2	18.0	13.6	13.7	13.4
Nonconvertible area	3.2	4.4	2.3	2.0	2.2

Sources: Data provided by the Lao authorities, IBRD, Fund accounts; and staff estimates.

1/ Components may not add to totals owing to rounding.

2/ Includes operations under the Trust Fund.

3/ In percent of total exports of goods and services.

Table 24. Lao P.D.R.: International Reserves, 1984-88

(In millions of U.S. dollars; end of period)

	1984	1985	1986	1987	1988 Est.
Gold	0.60	0.60	0.60	0.60	0.60
Foreign exchange	10.60	25.33	31.79	20.60	16.13
SDRs	0.01	0.01	0.16	0.01	--
Fund reserve position	--	--	--	--	--
Gross reserves	11.21	25.94	32.55	21.21	16.73
Foreign liabilities	-9.10	-3.10	-1.00	-1.00	-1.00
IMF credit	-8.10	-2.10	--	--	--
Other foreign liabilities ^{1/}	-1.00	-1.00	-1.00	-1.00	-1.00
Net official reserves	<u>2.11</u>	<u>22.84</u>	<u>31.55</u>	<u>20.21</u>	<u>15.73</u>
Memorandum items:					
Gross reserves					
In weeks of total imports	3.6	7.0	9.1	5.1	4.6
In weeks of imports from convertible area	9.8	17.4	21.6	13.5	9.6
Change in net official reserves	-6.00	20.80	8.71	-11.34	-4.48

Sources: Data provided by the Lao authorities; and Fund accounts.

^{1/} In comparison with previous staff reports, the treatment of letters of credit with the Bank for Foreign Trade (BCEL) has been changed. As a result of the improved classification of the monetary accounts, these letters of credit, in fact, represent domestic claims on the BCEL and not, as previously indicated, foreign claims.

Table 25. Lao, P.D.R.: Exchange Rates, 1984-89

(In kip per U.S. dollar)

	1984 Dec.	1985 Dec.	1986 Dec.	1987		1988				1989 Feb.
				Sept.	Dec.	Mar.	June	Sept.	Dec.	
Representative rate ^{1/}	10	10	10	10	10	10	10	10	10	10
Exchange rate for local expenses of embassies	35	35	35	--	--	--	--	--	--	--
Commercial exchange rate	35	95	95	--	--	--	--	--	--	--
Exchange rate for tourist receipts and inward remittances to non-Lao nationals	108	108	108	--	--	--	--	--	--	--
Exchange rate for remit- tances to Lao nationals	108	270	270	--	--	--	--	--	--	--
Exchange for exports/ imports of mixed corporations	--	300	380	--	--	---	--	--	--	--
Exchange rate for the Prefecture of Vientiane	--	--	390	--	--	--	--	--	--	--
Unified official exchange rate ^{2/}										
Buying	--	--	--	350	350	350	360	435	450	470
Selling	--	--	--	385	385	355	380	440	455	475
Memorandum item:										
Exchange rate in the parallel market										
Buying	253	424	400	395	390	390	390	454	483	480
Selling	...	...	...	...	...	...	...	...	...	487

Source: Data provided by the Lao authorities.

^{1/} The representative rate used to value foreign transactions with multilateral agencies.
From December 1988, this rate was only maintained with the IMF.

^{2/} All exchange rates, except for the representative rate, were unified in September 1987.

Table 26. Lao P.D.R.: Social and Demographic Indicators

<u>GDP per capita (1988)</u>		US\$120 ^{1/}	
<u>Area</u>	<u>Population (1988)</u>	<u>Density</u>	
236,800 sq. km	3.9 million	16.5 per sq. km	
	Rate of growth	200 per sq. km of	
	2.5 percent	agricultural land	
<u>Population characteristics (1987)</u>		<u>Health and nutrition (1987)</u>	
Life expectancy at birth	50	Physicians and nurses (per thousand)	3.0
Infant mortality rate (per thousand)	117	Per capita daily calorie intake	1,842
Crude birth rate (per thousand)	46	Calorie intake (% of requirement)	97
Crude death rate (per thousand)	17		
<u>Labor force (1985)</u>		<u>Education (1985)</u>	
Participation rate (%)	49	Primary enrollment rate (percent)	81
Male	53	Secondary enrollment rate (percent)	13
Female	45	Adult literacy rate (percent)	45

Source: United Nations Development Program: Report on the Economic and Social Situation, Development Strategy, and Assistance Needs of Lao P.D.R..

^{1/} GDP in 1988 was converted at the unified, market-related exchange rate of K¹ 400 per U.S. dollar.

Fund Relations with the Lao People's Democratic Republic
(As of March 31, 1989)

I. Membership status

- (a) Date of membership: 1961
- (b) Status: Article XIV

A. Financial Relations

II. General Department

- (a) Quota: SDR 29.3 million
- (b) Total Fund holdings of kip: SDR 29.3 million
(100 percent of quota)
- (c) Fund credit: None
- (d) Reserve tranche position: Nil
- (e) Current operational budget: Not included
- (f) Lending to the Fund: None

III. Current stand-by or extended arrangement and special facilities

- (a) Current arrangement: None
- (b) Previous stand-by and extended arrangements during the last 10 years: Stand-by arrangement, June 1980-May 1981 for SDR 14 million, or 87.5 percent of quota. The amount was fully repurchased.
- (c) Special facilities during the past two years: None

IV. SDR Department

- (a) Net cumulative allocation: SDR 9.41 million
- (b) Holdings: Nil
- (c) Current designation plan: Not included

V. Administered accounts

- (a) Trust Fund loans
 - (i) Disbursed: SDR 12.7 million
 - (ii) Outstanding: SDR 1.7 million
- (b) SFF subsidy account: None

VI. Overdue obligations to the Fund: None.

B. Nonfinancial Relations

VII. Exchange rate

In September 1987, Lao P.D.R. unified all rates, except the representative rate of KN 10 per U.S. dollar used to value foreign transactions, at KN 350 (buying) and KN 385 (selling) per U.S. dollar. The exchange rate subsequently has been adjusted in line with movements in the parallel market rate. On February 21, 1989 the official exchange rate was devalued to KN 470 (buying) and KN 475 (selling) per U.S. dollar; the parallel market rate was KN 480 per dollar. The representative rate of KN 10 per U.S. dollar continues to be used in transactions with the Fund.

VIII. Last Article IV consultation discussions

The last Article IV consultation discussions were held in Vientiane during November 2-13, 1987. The Executive Board discussed the staff report (SM/88/23) on February 10, 1988. The decision was the following:

1. The Fund takes this decision relating to exchange measures of the Lao People's Democratic Republic subject to Article VIII, Sections 2(a) and 3, and in concluding the 1987 Article XIV consultation with the Lao People's Democratic Republic in the light of the 1987 Article IV consultation with the Lao People's Democratic Republic conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).
2. The Lao People's Democratic Republic continues to maintain restrictions on the making of payments and transfers for current international transactions in accordance with Article XIV, as described in SM/88/23, except for the multiple currency practices and the exchange restrictions arising from bilateral payments agreements with Fund members, which are subject to Fund approval under Article VIII, Sections 2(a) and 3. The Fund encourages the authorities of the Lao People's Democratic Republic to simplify the exchange system, and in particular to eliminate the multiple currency practices as well as the restrictive features of the bilateral payments arrangements with Fund members.

IX. Technical assistance:

Staff members of the Bureau of Statistics visited Vientiane from October 25 to November 5, 1988, to provide technical assistance in the field of money and banking statistics and during November 14 to 26, 1988 to assist in the compilation of balance of payments data and to review the progress that has been made since the March-April 1985 technical assistance mission. The IMF Institute conducted a seminar on Financial Analysis and Policy in Vientiane on June 12-25, 1987.

X. Resident Representative/Advisor: None.

XI. Present consultation cycle: Bicyclic procedure.

Lao P.D.R.: Relations with the World Bank Group

The World Bank supports the development priorities of the Second Five-Year Plan (1986-90). Provided existing bottlenecks in absorption can be reduced, IDA disbursements are expected to increase during the Plan period. All projects are financed with IDA credits. A credit for a road rehabilitation project (amount: \$14.1 million) was signed in December 1987. An industrial credit project (amount: \$10 million) was approved in July 1988 and the establishment of a National Polytechnic Institute (amount: \$3 million) was appraised in July 1988. The Bank is currently negotiating an IDA structural adjustment credit for about \$40 million. Negotiations for their credit are expected to be finalized by midyear.

As requested by the Government, the Bank intends to place increased emphasis on structural lending in its new commitments. Since 1978, the amount of IDA credits committed and disbursed has been as follows:

IDA: Commitments and Disbursements to Lao P.D.R., 1978-88

(In millions of U.S. dollars)

	Committed	Disbursed	Repayments
1978	8.2	0.1	--
1979	10.4	0.2	--
1980	13.4	5.3	--
1981	15.0	5.4	--
1982	14.5	3.1	--
1983	--	4.6	--
1984	5.9	7.3	--
1985	--	--	--
1986	4.1	7.0	--
1987	14.3	5.0	--
1988	<u>36.6</u>	<u>10.1</u>	<u>0.1</u>
Total	122.4	48.1	0.1

Source: IBRD.

The last Country Economic Memorandum, Report No. 7188-LA, was published on September 21, 1988.

Lao P.D.R.: Relations with the Asian Development Bank

The AsDB's operational strategy in Lao P.D.R. supports the development objectives of the Government's Second Five-Year Plan. Thus far, AsDB assistance has been concentrated in the forestry and the hydroelectric power subsectors and in the development of the road network and of skilled manpower. A credit for the Xeset hydropower project (amount: \$15.5 million) was approved in October 1987. In December 1988, a credit for \$11.0 million for the Nam Ngum-Luang Prabang Power Transmission project was approved. In addition, the Bank has provided technical assistance in conjunction with specific projects and through formal and specialized education. The Bank, in close collaboration with the IMF, is providing technical assistance to assist the Government in restructuring the banking system. The Bank is currently negotiating an agricultural program loan; negotiations are expected to be finalized in May 1989.

AsDB: Commitments and Disbursements to Lao P.D.R., 1983-88

(In millions of U.S. dollars)

	1983	1984	1985	1986	1987	1988
Commitments	14.4	1.0	8.8	11.7	49.2	11.4
Disbursements	3.4	2.6	6.0	5.7	4.7	5.8

Source: AsDB.

Lao P.D.R.--Statistical Issues

The statistical base remains very weak, notwithstanding recent efforts to improve it. Problems include the collection and classification of data as well as in the consistency between different sets of data. Statistical information publicly available is limited to production trends, transport, commerce, education, and health. Lao P.D.R. does not report data to the Fund for inclusion in International Financial Statistics, the Balance of Payments Yearbook, the Government Finance Statistics Yearbook, or Direction of Trade Statistics.

The Government has received Fund technical assistance to improve monetary accounts and balance of payments statistics. The World Bank debt notification system has been introduced. The Government is receiving bilateral technical assistance to improve national income accounts and prices. Interest has also been indicated in receiving technical assistance from the Fund and bilateral sources to improve government finance statistics. Effective March 21, 1989, the Government has begun reporting selected financial data to the Fund.

National Accounts

The National Accounts are compiled according to the Material Product System (MPS), which differs from the concept of GDP in that it excludes the value of nonmaterial services and depreciation. Net material product is considered to be substantially understated as subsistence agriculture and most private sector activities are not adequately covered. The accounts are compiled at constant prices. The series on agriculture and industry have been adjusted by the staff on the basis of estimates of gross agricultural and industrial output, respectively. The GDP deflator is estimated by the staff on the basis of price series for consumer goods, investment goods, the exchange rate, and import and export prices.

Production

In agriculture, crop estimates are subject to wide margins of error. In industry, data cover only the output of major public enterprises located in the Vientiane plain. They exclude rice milling, the processing of agricultural products, and output of provincial industries.

Prices and wages

No price indices are currently published, although prices for a large number of items in the city of Vientiane are collected on a monthly basis. The staff uses those price series to establish a consumer price index by making assumptions on the consumption pattern of a middle-income household in Vientiane. Sub-indices were estimated for free market prices and official retail prices prior to 1989, as well as

for the main categories of goods and services. With price decontrol from October 1988, the weights used in calculating the overall index have been adjusted. Pending an updated consumer expenditure survey expected to be available during 1989, the Government is using the 1982 expenditure weights and the staff methodology to compute the CPI.

Government sector

The breakdown of the consolidated budget between the central government and the provinces is not available and budget transfers to public enterprises are not shown separately. In the absence of statistics on consumer subsidies, the staff prepared estimates based on fragmentary price and volume data. The accounts of public enterprises have not been provided to the staff. The data on foreign loans and grants in the budget are not reconcilable with those in the balance of payments; some foreign technical assistance was not included in historical data. In addition, foreign aid was valued prior to 1988 at an overvalued accounting rate. Finally, commodity credit received from the nonconvertible currency area did not yield the revenues, when sold domestically that would have been expected from the balance of payments data. The Government is receiving bilateral foreign technical assistance on the presentation of the budget.

Money and banking

A recent Bureau of Statistics technical assistance mission established a monetary survey consolidating the accounts of the monetary authorities and the other banking institutions, valuing foreign current accounts at the prevailing official exchange rate, and improving the classification and coverage of the accounts. The delay in compiling monetary data has been reduced from 14 to 2 months. The Government is prepared to report data regularly on this basis. Additional work remains to be done on the sectorization of accounts and on the call report form to collect data from the banks.

Balance of payments

The Bureau of Statistics provided technical assistance in 1985 and again in 1988 in the area of balance of payments and the authorities have begun compiling such data on the basis of the report's recommendations. From 1988, trade data is compiled on the basis of customs data. Residency criteria are being strictly applied to trade and payments transactions. Additional work is needed to revise historical data. Re-exports are not yet included in total exports.