

National Report for Lao PDR Executive Summary



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"Trade liberalization will have vast impacts on Lao PDR's natural environment. Some of them may be positive, others negative. These need to be identified, understood and well managed to ensure the best development outcome for the country. Through the RTEA process, we have found the strength in a multi-sectoral, multi-level network that can create working linkages to understand and implement trade and environment policy responses". (RTEA Expert Advisory Panel 2007)

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A full version of the RTEA National Report for Lao PDR can be obtained at www.iisd.org

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Executive Summary

Lao PDR is characterized by an abundance of natural resources and a small population of 5.6 million, the vast majority of whom live in rural areas and are dependent on subsistence agriculture. The country remains amongst the poorest in the region and ranks 133 out of 177 countries on the United Nations Human Development Index. The government has set a goal to graduate from “least-developed country” status by 2020. Lao PDR initiated a gradual shift to a market economy with the introduction of the New Economic Mechanism for economic liberalization in 1986. To a great extent, the strategy for reforming the economy is being situated in the context of Lao PDR’s commitments under the Association of Southeast Asian Nations (ASEAN) Free Trade Area and the process of accession to the World Trade Organization (WTO), as well as increasing bilateral relations and transportation links with neighbouring countries in the Greater Mekong Subregion (GMS). It is, therefore, clear that trade is expected to be the engine of growth and development for Lao PDR.

Trade and investment context

Notwithstanding the rapid growth in the industrial and services sectors since the introduction of the reform process in the mid 1980s, agriculture continues to represent the lion’s share of the national economy, accounting for 45 per cent of GDP in 2005. However, the contribution of the agricultural sector to trade is relatively small. In 2005, this sector contributed only seven per cent to exports while it accounted for nearly 20 per cent of imports. The industrial sector has been driven by gold and copper mining, making it the main contributor to growth over the past five years and accounting for 30 per cent of GDP in 2005. Moreover, timber and garment exports played a significant role in the country’s economic performance throughout the 1990s—with an increasing contribution from electricity and mining—taking advantage of the abundance of unexploited forests, water, minerals and preferential textile and garment quotas prior to the termination of the WTO Agreement on Textiles and Clothing in 2005.

Lao PDR is situated in the centre of the Mekong region, bordered by Cambodia, China, Myanmar, Thailand and Vietnam. Lao PDR has committed itself to becoming a centerpiece for trade in the region—developing infrastructure to facilitate the freer movement of goods throughout the GMS, within ASEAN and between China and its ASEAN trading partners. However, while the country’s geographical location may offer opportunities, it also presents challenges, such as high transportation costs to get its exports to market and difficulty in monitoring trade along the Mekong River borders.

The recent flows of foreign direct investment (FDI) into Lao PDR have been an important source and guiding force for economic growth. Mining and hydroelectric power have attracted significant investment, with FDI reaching an estimated US\$500 million in 2006. The agriculture sector—specifically plantation production—is another key source of investment after mining, representing 15 per cent of FDI in 2004. Economic integration through the ASEAN Investment Area is expected to further promote flows of FDI from both ASEAN and non-ASEAN sources into Lao PDR by progressively streamlining and reducing investment regulations and conditions.

Environmental context

Lao PDR’s path to development has been firmly rooted in developing its abundant natural resources, including water, minerals, wetlands, forests and biodiversity. For example, wood and wood products accounted for over 35 per cent of total export revenues and contributed over 15 per cent of GDP in 2005. However, as evidenced during the recent National Assembly meetings in July 2007, concerns are now being raised over the long-term sustainability of the current resource-dependent development path. For instance, while Lao PDR is still the most forested country in Southeast Asia, forested areas have declined considerably due to deforestation for timber and agricultural production, spill-over effects from hydropower and mining projects, and a lack of enforcement of the export ban on raw logs. Planned infrastructure development will put

further pressure on forests and biodiversity through road construction, increased pollution from transit, and illegal exports (timber, endangered wildlife and plant species).

The Government of Lao PDR is in the process of elaborating a broad environmental policy and has assigned the recently created Water Resources and Environment Agency (WREA) with the responsibility of managing water and environmental resources in order to ensure sustainable development. Previously, the Science, Technology and Environment Agency (STEA) under the Prime Minister’s Office held the main responsibility related to the environment and conservation of natural resources.

Environmental impacts of trade liberalization in key sectors

In considering the linkages between trade and environment, it is helpful to keep in mind that countries that pursue trade liberalization agreements are ultimately seeking economic restructuring, which they anticipate will be beneficial on the whole for their economies and people. Whether trade and trade liberalization will in fact bring net benefits may vary from case to case. What is certain, however, is that whenever there is economic restructuring there are environmental impacts. These impacts may be positive or they may be negative, but there is no disputing the fundamental truth: trade is linked to the environment because economic change has environmental impacts. If we accept that trade can be both good and bad for the environment, the need to analyze environmental impacts becomes obvious. Where trade is liberalized, policy-makers need to be prepared to capture the positive opportunities and avoid any negative outcomes that may result.

The Rapid Trade and Environment Assessment (RTEA) has been developed as a practical tool to help integrate sustainable development considerations into trade and environment policy-making. It aims to provide policy-makers with the kind of information they need to better understand the environmental implications of trade liberalization initiatives. To this end, the RTEA examined 10 key economic sectors in Lao PDR: hydropower, mining, construction materials, wood and wood products, garments, tourism, organic agricultural products, silk handicrafts, medicinal plants and spices, and biofuels.

Rather than focusing on lengthy quantitative assessments (as is the case for most assessment methodologies), the RTEA provides a relatively fast assessment to identify and prioritize those trade policies, negotiations and sectors that have potential to negatively or positively impact the environment, and deliver the associated policy advice. In some cases, this may be sufficient information; in others, it may be the basis for more detailed analyses of policies, institutional capacities and information gaps. Table 1 summarizes the results of the RTEA in Lao PDR.

Overview of the RTEA Methodology

- Step I: Partnership-building with key government and non-governmental actors in the country (establishment of a National Expert Advisory Panel to guide the research);
- Step II: Setting the context through statistical, empirical and economic analyses;
- Step III: Expert input through broad-based stakeholder interviews and a literature review;
- Step IV: Scenario-building to establish the potential impact of liberalization agreements on the regulatory framework and policy coherence;
- Step V: Identification of the potential environmental and social results of the impacts of trade liberalization as per scenario-building; and
- Step VI: Conclusions and strategic policy recommendations, culminating in a National Workshop.

Table 1: Environmental impacts of trade and investment liberalization in Lao PDR

Sector	Trade and investment drivers	Main environmental impacts	Mitigating factors (environmental management framework)
Hydropower	Priority investment and growth sector; industrial development in the GMS; ASEAN Investment Area (AIA)	-ve: flooding of forested areas; impacts on natural water flows; biodiversity loss (including fisheries resources) +ve: increased government revenue to contribute to sustainable development; increased possibility to leap frog outdated approaches to environmentally-sound technologies (ESTs); mitigate climate change	National Growth & Poverty Eradication Strategy (2004) (NGPES); National Policy: Environmental and Social Sustainability of the Hydropower Sector in Lao PDR (2005)
Mining	Priority investment and growth sector; overseas demand, especially from China and India; AIA	-ve: forest clearance; water, land and air pollution; habitat loss +ve: increased government revenue to contribute to sustainable development; leap frog to ESTs	GPES; environmental impact assessment (EIA) required under the Mining Law (1997)
Construction materials	Priority investment and growth sector; AIA	-ve: pollution; impacts from mining raw materials +ve: efficient materials can mitigate resource use; leap frog to ESTs	GPES; Medium-term Strategy and Action Plan for Industrial Development (2003)
Wood and wood products	Prioritized for export in the National Export Strategy (NES); government focus on developing processing industry; various trade agreements and preferences	-ve: deforestation; forest degradation; habitat and biodiversity loss; fewer non-timber forest products (NTFPs); land-use change for plantations +ve: market opportunities for sustainable products enhance forest management	National Export Strategy (2006–2010); Forest Strategy 2020, export ban on raw logs; SFM certification
Garments	Prioritized for export in the National Export Strategy; various trade agreements and preferences	-ve: transport pollution to get to the product to port +ve: leap frog to ESTs	National Export Strategy
Tourism	Prioritized for export in the National Export Strategy; growth of tourism sector overall; AIA	-ve: pollution, habitat loss, unsustainable resource use (waste and water) +ve: value environment as a business asset; increased funds for conservation; local employment; awareness raising, including through CSR	National Tourism Development Strategy 2006–2020; Nation Export Strategy – Tourism; National Ecotourism Strategy and Action Plan 2005–2008; GMS Strategy for Sustainable Tourism
Organic agricultural products	Land-use management, impacts on NTFPs; growing overseas demand, particularly the EU and U.S.; various trade agreements and preferences	-ve: deforestation; forest degradation; shifting cultivation +ve: fewer chemicals; less land degradation; maintain landscapes and agro-biodiversity; increased awareness through high sanitary and phytosanitary measures (SPS) in export markets	NGPES; National Export Strategy – Organic Agricultural Products; organic certification
Silk handicrafts	Prioritized for export in the National Export Strategy; to be integrated in the tourism sector; various trade agreements and preferences	-ve: water discharge and consumption; land-use change for plantations +ve: less pollution from natural dyes; leap frog to ESTs; more sustainable production and processing methods	National Export Strategy – Silk Handicrafts; Industrial and Handicraft Development Strategy toward 2020

Sector	Trade and investment drivers	Main environmental impacts	Mitigating factors (environmental management framework)
Medicinal plants and spices	Prioritized for export in the National Export Strategy; overseas demand primarily in Asia; various trade agreements and preferences	-ve: unsustainable resource use; land-use change for plantations; pollution; biodiversity loss +ve: value of products coupled with sustainable harvesting can help protect forests; contribution to pro-poor strategies, rise in incomes of local communities; increased environmental awareness	NGPES; Forestry Strategy 2020; National Export Strategy – Medicinal Plants and Spices
Biofuels	Development of domestic energy alternative source considered to be key to supplement expense of petroleum imports	-ve: land-use change for plantations; less land for food crops; monocropping; soil erosion; pesticide use; water consumption +ve: less costly energy source increases government revenue to contribute to sustainable development; mitigate climate change; reduce air pollution; use of biodegradable outputs from other sectors	Strategy for development of alternative biofuels (under development)

Source: Compiled by the authors based on research and stakeholder interviews conducted for the RTEA project.

Conclusions

The following general conclusions are highlighted from the research.

- First, the analysis of the impacts of the economic scenarios on the environment of Lao PDR reveal mixed and variable outcomes for the selected sectors. For the main exports—electricity, minerals and wood products—economic growth is likely to result in a significant expansion of exports and place an increased burden on the natural resource base and the environment in Lao PDR. To a large extent, the framework for managing natural resources is still in the process of being developed. Whether the increasing extraction of natural resources in these main export sectors is sustainable will depend on the development and implementation of effective institutional and regulatory structures in Lao PDR, as well as the use of government revenue to advance socio-environmental objectives.

For those sectors which are environmentally and livelihood sensitive—ecotourism, organic agriculture, silk handicrafts, and medicinal plants and spices—economic growth is likely to result in an increased potential to develop “green” niche exports. Various obstacles will need to be overcome to realize the opportunities of developing these sectors, such as domestic supply-side constraints and non-tariff barriers to trade. Moreover, it needs to be borne in mind that such activities, even if aimed at supporting environmental protection, can have negative environmental impacts, such as land-use change and pressures from increased tourism. Again, the institutional and regulatory setting is an important variable in determining whether the outcome is positive or negative on the economy and the environment. Moreover, whether Lao PDR can harness the competitive advantage in these “green” niche sectors will depend to a great extent on private sector initiatives.

The RTEA puts forward a preliminary analysis of the potential environmental impacts of trade and investment liberalization. There is a need to study in greater detail specific policy linkages and monitor the implementation of liberalization commitments to ensure trade and environment policies are integrated.

- Second, Lao PDR is committed to putting in place a solid institutional and regulatory framework for managing natural resources and maintaining environmental sustainability. The evidence indicates that implementation and enforcement of environmental rules and regulations is crucial and will likely prove to be a challenging issue in Lao PDR as trade-led growth accelerates. In order to meet this challenge, increased knowledge and capacity both in the public and importantly, private sector are vital to ensuring positive outcomes.
- Third, openness to foreign direct investment is emerging as a key driver of development and export growth. The fact that a large share of FDI has been concentrated in the extraction of raw materials in the mining, hydropower and forestry sectors indicates the importance of ensuring that social and environmental considerations are taken into account in order to manage the natural resource base sustainably. This is an aspect that the government can build on to encourage sustainable investment in Lao PDR and stimulate transfer and use of environmentally-sound technologies, particularly in the mining and hydropower sectors.
- Fourth, the path forward charted by the government’s recent National Export Strategy emphasizes value addition in many of the sectors examined in this report. An important factor for penetrating market access in many export sectors is emerging non-tariff measures and industry standards. These measures and standards may influence governmental regulations and private sector practices towards sustainable development. These measures cover certification and labelling for products as diverse as wood products, garments, agricultural products, silk handicrafts, medicinal plants and spices, and are relevant to the burgeoning tourism sector. The Lao private sector, thus, is a key stakeholder and plays a significant role in ensuring that exports can meet these increasingly strict standards. The government has a clear role to play in helping equip exporters with the necessary information and institutional support to help them meet these standards.

Strategic policy recommendations

A number of general recommendations emerged from the research on how environmental impacts of trade and investment liberalization could be addressed:

- Continue to raise awareness of the linkages between trade and environment in diverse constituencies from the local to the national levels.
- Enhance policy coordination and coherence on trade and environment among the relevant policy-makers in government by assessing gaps in institutional capacities and strengthening institutional ability to meet changing priorities in Lao PDR.
- Recognize that economic growth based solely on natural resources is not a panacea for development. The extent to which the natural resource base is sustainably managed will determine longer term growth potential.
- Enable an inclusive domestic trade policy-making framework and explore options for institutionalizing a trade and environment body, as piloted during the RTEA process, in order to allow input from the key stakeholders—related government ministries, private sector representatives and non-governmental organizations such as research and academic institutions.
- Strengthen the role of the private sector in addressing environmental challenges in key sectors and facilitate a domestic environment that attracts responsible business and encourage international best practice.
- Strike the right balance between large environmental “footprint” and environmentally/people sensitive sectors to cushion the potential social and environmental impacts of export-led growth. Finding this balance will require solid coordination and effective policy-making among ministries. It will also need to strike a balance between FDI into those sectors which entail immediate benefit

to the government and those activities which may take longer to foster but result in sustained gains for the people of Lao PDR.

- Ensure the appropriate institutional and regulatory frameworks are solidly in place and enforced in each sector. Enact and ensure compliance with regulations and policies for environmental management in order to provide an environmentally optimal enabling framework for trade liberalization to take place.
- Undertake strategic impact assessment of new policies, regulations, investments and projects in all sectors and raise awareness among stakeholders of the environmental and social impacts and possible mitigation measures.
- Strengthen regional cooperation to address the environmental impacts of economic integration. Of particular importance is managing the growing demand for natural resources in the GMS in pace with the development of infrastructure to facilitate the freer movement of goods, services and investment.
- Enhance monitoring and assessment of the environmental impacts of trade liberalization in order to ensure that investment and economic development priorities do not cause undue or avoidable social and environmental damage.
- Continue to collect data on the current state of the environment, trade flows and potential environmental impacts to aid in the policy-making and environmental management process.

In addition, *sector-specific* recommendations were identified in the background research papers and national workshop, including:

- Improve environmental governance at the same pace as current trends in FDI in the mining, hydropower and construction materials sectors, by encouraging companies to commit to a high standard of socio-environmental performance and ensuring clear investment laws and coordination mechanisms related to environment impact assessments.
- Encourage value-addition in the wood and processed wood sector to stimulate processing industries and obtain greater economic returns while ensuring sustainable resource use, including the promotion of forest certification and chain-of-custody verification.
- To enhance sustainability in the tourism sector, strengthen the Lao National Tourism Administration’s ability to engage with the private sector and investment decision-makers to encourage the development of successful ecotourism models.
- Promote quality assurance in the organic agricultural products sector through the creation of certification bodies or by strengthening existing systems that fully take into account environmental and social considerations to help “green” exports meet international standards.
- Implement the National Export Strategy for the silk handicraft sector and work with the Lao Handicraft Association and the Lao National Chamber of Commerce and Industry through the creation of a silk handicraft fund to promote value-addition and foster diversification of the sector.
- Develop and enforce laws and regulations related to the forestry sector as a whole, and especially to non-timber forest products, such as medicinal plants and spices.
- Draft a national biofuels policy that clearly outlines environmental and social policies and is integrated with, and included in, a national energy production and management plan.

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