

# BTI 2014 | Laos Country Report

	scale	score	rank	trend
<b>Status Index</b>	1-10	<b>3.89</b>	# 109 of 129	
Political Transformation	1-10	2.95	# 121 of 129	➔
Economic Transformation	1-10	4.82	# 86 of 129	➔
<b>Management Index</b>	1-10	<b>3.88</b>	# 105 of 129	

This report is part of the Bertelsmann Stiftung’s Transformation Index (BTI) 2014. It covers the period from 31 January 2011 to 31 January 2013. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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### Key Indicators

Population	M	6.6	HDI	0.543	GDP p.c.	\$	2925.6
Pop. growth <sup>1</sup>	% p.a.	1.9	HDI rank of 187	138	Gini Index		36.7
Life expectancy	years	67.4	UN Education Index	0.707	Poverty <sup>3</sup>	%	66.0
Urban population	%	35.3	Gender inequality <sup>2</sup>	0.496	Aid per capita	\$	44.0

Sources: The World Bank, World Development Indicators 2013 | UNDP, Human Development Report 2013. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$2 a day.

## Executive Summary

In the past two years the Lao People's Revolutionary Party's (LPRP) has reinforced its determination to pursue economic growth while resisting even the slightest reform of its one-party political system. Economically, the regime has continued to oversee some of Asia's highest GDP growth rates as a result of market reforms commenced in the 1980s. Yet politically, its clampdown on the nascent civil society sector in late 2012 sent the unmistakable message that the LPRP will continue to guard its monopoly of the political landscape.

In 2011, according to a cycle repeated every five years, the LPRP held its 9th Party Congress, conducted National Assembly elections and endorsed a new five-year National Socio-Economic Development Plan (NSEDP). The key LPRP Congress – which elects the party's main decision-making organs, the Politburo and Central Committee – re-elected Choummaly Sayasone as LPRP secretary-general, ensuring the National Assembly would duly re-endorse him as president. Thongsing Thammavong, elevated to prime minister in December 2010 after the resignation of Bouasone Bouphavanh (for reasons that remain unclear), was made number two in the Politburo. Gradualist and generational, changes to the Politburo nevertheless indicated reduced military influence: three relatively youthful figures replaced two retiring revolutionary-era generals and Bouasone, whose fall was confirmed by his demotion from the Politburo and central committee. Despite similar generational turnover in the central committee – where half are under 60 years old – party power remains in the hands of the old guard in the Politburo, where the average age is close to 70. In typical fashion, National Assembly elections were almost wholly restricted to – and totally dominated by – members of the LPRP.

Meanwhile, the 7th NSEDP (for 2011 – 2015) reinforced the party's objective of underwriting high economic growth with foreign investment, foreign aid and exploitation of natural resources – with the ultimate goal of “graduating” from Least Developed Country status by 2020. Since then, ambitious targets of 8% GDP growth per annum have been met and exceeded. Laos advanced its integration into the global economy, symbolically, by hosting the Asia-Europe Meeting (ASEM)

in November 2012 and, substantially, by finally joining the WTO in February 2013, the culmination of a 16-year process.

Meanwhile, problems associated with Laos's development trajectory persisted. For example, economic growth continued to come with significant social and environmental costs, particularly land and compensation disputes emanating from industrial agriculture and other development projects. Such conflicts are frequently related to corruption, a growing problem even though leaders rhetorically condemn it.

Likewise, a series of events in 2012 dashed hopes – triggered by a 2009 decree permitting local NGOs – that a more tolerant political culture was emerging. In fact, authorities have continued to seriously undermine civil liberties. In January, a “talk-back” radio program, in which callers could voice concerns over development issues, was shut down; in May, the director of the Academy of Social Sciences, Khampheuy Phanmalaythong, was dismissed for criticizing the education system in the National Assembly; in October, rural residents were harassed and intimidated for voicing concerns over land issues at the Asia-Europe People's Forum (AEPF), a state-sanctioned civil society meeting that preceded ASEM; and, in December, a Swiss NGO director and co-organizer of AEPF, Anne-Sophie Gindroz, was expelled from Laos after criticizing the lack of free speech and state intimidation in a letter to colleagues. A week later, another AEPF organizer, the respected civil society leader Sombath Somphone, mysteriously disappeared, presumed to have been abducted by Lao security services.

## History and Characteristics of Transformation

The Lao People's Revolutionary Party (LPRP) came to power in 1975 as a Marxist-Leninist regime modeled on that of the Democratic Republic of Vietnam. One of its first acts was to replace multiparty parliamentary system with a system of “democratic centralism.” In theory, each level of the party, from the bottom up, elects delegates to the next level, but in practice those controlling the higher level co-opt the delegates they want. Tightly controlled elections for a National Assembly have been held since the promulgation of a constitution in 1991 (amended in 2003) but all candidates are screened by, and the overwhelming majority are members of, the LPRP. No subsequent transition to democracy has occurred, nor is one likely in the foreseeable future.

Upon coming to power, the LPRP also socialized the economy. They nationalized industry and financial institutions and encouraged the formation of agricultural cooperatives. However, peasant opposition and collapsing production forced the party first to modify its hard line in 1979, then in 1986 to embark on a reform program known as the New Economic Mechanism (NEM), which set in motion the transition from a centrally planned economy to a free-market one. Co-operativization was abandoned, restrictions on internal trade were removed and a free market was introduced for agricultural produce. The government also liberalized international trade and sought foreign investment. As in China and Vietnam, but unlike the Soviet Union, this transition to a market

economy took place without any corresponding political liberalization. The changes in Laos were driven by the party's powerful secretary-general, Kaysone Phomvihane, who, with Vietnamese support, won the party's backing despite pockets of internal opposition.

An array of supporting measures were introduced over the next decade: the elimination of microeconomic constraints limiting private production; legislation to encourage foreign direct investment (FDI), including a legal framework of commercial, trade and labor laws; closer attention to macroeconomic stability (improved budgetary and monetary policy, reduced state subsidies, civil service cuts and a new tax framework); and the privatization of most state-owned enterprises (SOEs), with the exception of about 20 that were designated as "strategic." By the mid-1990s, these measures were producing their desired economic effect of improving resource allocation and spurring economic growth. Growth levels were a misleading indicator, however, as the country was highly dependent on official development assistance (ODA), especially for infrastructure development.

The Asian economic crisis hit Laos in 1998 and 1999. Though the country was initially spared much of the economic fallout observed elsewhere in Southeast Asia, the political decision to dispense with budgetary restraint led to sudden inflation and a slowing of growth that shocked the party leadership. Further reforms toward a market economy were either put on hold or reluctantly agreed to and then not implemented, much to the frustration of international donors pressing for reform.

These stop-and-go reforms have remained the pattern over the past decade as investment has steadily picked up, especially in hydropower, mining, plantation agriculture and tourism. This period of renewed prosperity has coincided with a growing culture of corruption, encouraged by the example of senior political figures, who have increased their power by building patronage networks oiled by the plunder of state resources. Especially in the provinces, public money has been used for private gain, which has complicated center-province relations. Although anti-corruption legislation has been enacted, no senior political figure has yet been prosecuted.

The global financial crisis of 2008 and 2009 reduced the quantity of FDI originating from the West, but this was soon replaced by increased investment in plantation agriculture, mining and hydropower from China, Vietnam and Thailand. Those Lao still practicing subsistence agriculture (close to half the population), were largely unaffected by the global economic downturn. In urban areas, rising unemployment led increasing numbers of young people to seek work in Thailand, but economic growth soon rebounded strongly. None of these events threatened the ruling party's hold on power.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

Question  
Score

The ruling Lao People's Revolutionary Party (LPRP) has maintained its monopoly on the use of force over the past two years. Hmong insurgents who opposed the regime after 1975 have been all but eliminated; others gave up long ago. There has been no recurrence either of bandit-like attacks on road transport or the series of small bomb blasts in Vientiane and the south of the country that were seen between 2002 and 2005.

Monopoly on the  
use of force  
9

Foreign-owned plantation business interests utilize private security services, some of which are known to be heavy-handed, but they are not thought to threaten the state's monopoly on force.

Laos is the most ethnically diverse country in Southeast Asia. Under the former regime, the population was roughly divided into "Lao of the plains," "Lao of the hillsides" and "Lao of the mountain tops," depending on language, culture and location. After initially adopting the same construction, which aimed to eliminate racist terminology and express that all were citizens of the Lao state, the present regime adopted language as the principal distinguishing criterion. Both the nationality and the "race" (noted on identity papers) of all 49 different ethnic groups officially recognized in the 2005 census is "Lao." Chinese and Vietnamese of Lao nationality are not considered of Lao "race," though they enjoy the same constitutional civic rights and responsibilities possessed by other citizens. Members of the Lao diaspora are of Lao "race," but not nationality. Laos does not recognize dual nationality, but Lao with foreign citizenship may invest and live in Laos.

State identity  
8

The Hmong insurgency that once sought to establish a Hmong homeland, with its implied repudiation of allegiance to the Lao state, has now collapsed. Several Hmong now serve on the LPRP Central Committee, as ministers in the government, and as

governors of provinces. In January 2011, Pany Yathortou, a Hmong member of the Politburo, was named president of the National Assembly.

Other ethnic minorities also accept that they are citizens of Laos. Both the LPRP and the army recruit minority members, though their representation in the bureaucracy at the national level is lower, relative to their population, than for ethnic Lao. Lao officials reportedly still discriminate against rural ethnic minorities, and resentment over minority rights and resettlement still works against full identification of some minorities with the Lao state, but the regime has been relatively effective at integrating minority groups and in promoting inter-ethnic solidarity.

According to the 2005 census, 67% of the Lao population is Buddhist, 2% is Christian and the remaining 31% is animist. The Lao constitution guarantees freedom of religion. However, whereas the Buddhist Sangha (monastic order) has a widespread organizational presence throughout the ethnic Lao areas of the country, Christians from minority groups live in a few towns, where they are kept under surveillance by Lao authorities, and complain of persecution. Certain constitutive practices of animism, like animal sacrifice, are disapproved of by the government, but not forbidden. Animism is tendentiously seen as superstitious by many Lao and only locally and unofficially called a religion. Some members of minority groups turn to Buddhism as a condition for upward social mobility. In addition, the resurgence of Buddhism in official ceremonies in recent years perhaps suggests it is a component of national identity. But while monks enjoy social status and respect, and Buddhism will continue to play a greater public role as nationalism replaces Marxism as the dominant ideology, the Sangha remains completely under the control of the ruling LPRP and has little or no political influence.

The party-state structure extends throughout the country, from national to provincial, district and village levels. Appointments are made, or at least directed, by higher levels in the party-state structure. Given that the two institutions of party and state are largely parallel, almost all officials in positions of authority are members of the LPRP. Regionalism remains strong and provinces assert a degree of autonomy both in their economic relations with neighboring countries and in their relations with the central government (which at times struggles to enforce new policies in the provinces, or to extract tax revenue from them). Law is enforced through a system of courts that reaches to the district level, but minor infringements are often dealt with through conciliation at the village level. New legislation is poorly disseminated and understood by bureaucrats and citizens, but this is slowly improving. Service delivery (health, education) in the rural areas is poor and often dependent on international aid. Though access to improved sanitation and water source has increased markedly over the past decade, access to both remains relatively poor (63% and 67% respectively). Remote rural villages lack transportation and communication links, although this is also improving slowly.

No interference of religious dogmas

10

Basic administration

7

## 2 | Political Participation

Elections for the National Assembly are held every five years, most recently in April 2011, but the Lao constitution defines the LPRP as the “nucleus” of the political system and no other political parties are permitted. Besides a few independents, just one of which was elected in 2011, all candidates are party members and all, including independents, are vetted by the party-controlled Lao Front for National Construction (LFNC). Thus, although all citizens over the age of 18 are eligible and required to vote, there is no democracy. Power remains firmly in the hands of the party, which determines all policy matters and the legislative program. Voters do have a choice of candidates but the number of independent candidates allowed to run is too small to threaten party domination. Perhaps reflecting the strengthening of the National Assembly in recent years, some candidates campaigned quite vigorously on local issues in 2011, but none voiced any but the mildest indirect criticisms of the government. In fact, all but two of the elected deputies were themselves public servants. Nor was there any critical discussion of issues facing the country in any of the entirely party-controlled media outlets. No elections take place at the local level, either for provincial or municipal administrations, or for district or village heads, though village heads may be selected with communal approval.

Free and fair elections

1

Laos is a one-party autocracy. Political decision-makers are not democratically elected and there is not the slightest degree of political openness or “semi-democratic” elements even at the local level.

Effective power to govern

1

Although the right and freedom of speech, press and assembly is guaranteed under Article 44 of the amended Lao constitution (2003), rights of association are extremely limited and tentative steps toward the emergence of a Lao civil society sector have stalled. There are no opposition political parties; public demonstrations are not permitted and, on the rare instances that they occur, participants have received long prison sentences. Although non-governmental Non-Profit Associations (NPAs) are finally permitted to operate under the 2009 Decree on Associations, an important reform in terms of developing civil society, most have little choice but to retain close relations with the state. Most alarmingly, the 2012 Asia-Europe People’s Forum (AEPF), held in Vientiane in association with ASEM, led to intimidation of civil society participants, and was linked to the disappearance and presumed abduction by security forces of Sombath Somphone, a respected civil society leader and AEPF organizer.

Association / assembly rights

1

Media organizations in Laos are controlled by the LPRP through the Ministry of Information and Culture. Although independent lifestyle magazines have appeared in the past decade, a new media law presented to the National Assembly in July 2008 has not reduced government control over political coverage. Opinion cannot be freely expressed in any public forum. Although National Assembly members are now

Freedom of expression

1

encouraged to discuss development issues, their freedom of speech is limited. For example, deputy Khamphuey Phanmalaythong's criticism of the outdated teaching of Marxism in the country's schools resulted in his dismissal as director of the Academy of Social Sciences. Private criticism of the government is tolerated as long as it does not form part of any concerted movement of dissent. While the Internet has the potential for a medium of political expression, it has not been widely utilized for this purpose. Moreover, China has provided the Lao government with technology to censor online communications, which may limit any future benefit of the Internet for the development of Lao civil society.

### 3 | Rule of Law

The Lao constitution outlines a formal separation of powers between the National Assembly (legislature), the government (executive) and the judiciary, but in fact, all function according to the dictates of the ruling LPRP. Separation of powers exists solely on paper and can be overridden at the whim of party leaders. As a result, no checks and balances apply between the three institutions of government. Moreover, there is no constitutional court able to judge the validity of legislation.

Separation of powers

1

The judiciary is institutionally differentiated but is not independent of the ruling party. Most judges and Justice Ministry officials are party members. Bribery is widespread, especially in civil and commercial cases, but political connections usually prove decisive. The government frequently reiterates its commitment to improving the rule of law, and small incremental improvements have been made, including a growing body of laws passed by the National Assembly. However, few are widely known or applied.

Independent judiciary

2

A body of professional lawyers, who may represent clients in court, is slowly being formed and the Lao Bar Association provides legal education, training and advice through its legal aid program. However, as the association works closely with both the Justice Ministry and the Faculty of Law and Political Science at the National University of Laos, it is not an independent body. In fact, the judiciary remains an organ of the LPRP.

Abuse of office is widespread. Virtually anyone holding an official position, whether in the civil service or local administration, uses it for personal gain. A few minor officials have been prosecuted under the existing anti-corruption law, but no senior members of the party, whose example has encouraged the prevailing culture of corruption, have been targeted. Complaints to the police (where the police are not at fault) or to the Office of the Public Prosecutor usually go nowhere. Laos has no ombudsman.

Prosecution of office abuse

3



In recent years, corruption has triggered popular resentment and public discussion. At the only level of administration where the populace actually has a choice, that is, with village headmen, popular disapproval of corruption has been occasionally expressed by dismissing even long-standing office holders. Additionally, the need to combat corruption has been noted in the National Assembly and discussed in the press. However, the press does not investigate corruption and no names are ever mentioned in the media. Indeed, prosecutions are rare, if they occur at all, and never publicized. The worst that has happened to blatantly corrupt officials is that they have been demoted (for example, to a provincial appointment) or removed from office. Moreover, such punishments typically stem more from intra-party politics than from the degree of corruption.

Although civil rights are in principle protected by the Lao constitution, widespread violations occur, for which there is usually no redress. Rights of assembly and the free expression of political beliefs are nonexistent. Religious freedom is granted to Buddhists, but is limited when authorities believe religious differences will exacerbate ethnic divisions. Furthermore, abuses are known to occur at the hands of the security forces and in the prison system. Since there is no likelihood that an appeal against a violation of civil rights will produce a result, few formal complaints are made.

Violations of civil rights disproportionately affect the poor and powerless in rural areas, where foreign companies (particularly from China and Vietnam) have obtained substantial land concessions from central and provincial governments. In an increasing number of documented cases, both ethnic Lao and minority groups have been left with little choice but to make way for plantation forestry and agricultural projects. Concerns over land-use have been voiced in several forums: at local protests, at the AEPF in late 2012, and even by the National Assembly, but authorities have simply cracked down on dissenters. The most widely discussed incident in recent years was the disappearance in late 2012 of Sombath Somphone, presumed to be abducted by elements of the Lao security forces.

#### 4 | Stability of Democratic Institutions

As a single-party Marxist-Leninist state, political power in Laos is monopolized by the LPRP. Although it has become more outspoken in recent years, the National Assembly is not democratically elected and is entirely dominated by the party, as are all levels of government and administration. In practice, the judiciary is also a party instrument. According to the official creed of “democratic centralism,” the views of grassroots party members are supposed to be channeled up the party hierarchy for the central committee to include in policy formulation. In reality, power runs from the top to the bottom, and decisions by the party leadership must be accepted without

Civil rights  
3

Performance of  
democratic  
institutions  
1

question. That said, discussion does occur within the party's upper levels prior to decisions being made by the Politburo.

To the extent that any institution functions "democratically" (through "democratic centralism" as applied within the party itself), it forms an integral part of an authoritarian regime. Attempts by Western governments to urge reforms that would lead to multiparty democracy are vigorously resisted, for they are interpreted as tantamount to creating conditions for regime change. In adopting this position, the LPRP has powerful support from the communist parties of both Vietnam and China, both of which enjoy close relations with the Lao regime.

Commitment to democratic institutions

1

## 5 | Political and Social Integration

There is no party system in the Lao PDR: the sole political party is the LPRP. The ruling party is well institutionalized, stable and deeply rooted in Lao society. Nothing that has happened over the last two years has threatened the stability of the party or its hold on power. In 2011, party membership was estimated at 191,700, or 3% of the population. Membership is attractive to those who are politically ambitious and to those who seek to tap into networks of influence. The party actively recruits members from among the educated elite, and even some businessmen are party members.

Party system

1

Independent organizations were not permitted until recently in Laos, and most interest groups continue to function under, or in close cooperation with, the party and/or state. The party's mass organizations include the Lao Federation of Trade Unions, Lao Women's Union, Lao People's Revolutionary Youth Union and Lao Front for National Construction, which includes representatives of ethnic minorities, religious organizations and professional associations such as the Lao Bar Association and the Lao Chamber of Commerce. Social and economic interest groups (teachers, health workers, business people) are represented at party forums only by virtue of members' party membership, not as interest groups per se.

Interest groups

1

The 2009 Decree on Associations permitted the formation of Lao NPAs. Although NPAs must satisfy onerous regulatory processes and many continue to work closely with the government, this reform was significant since it promised the emergence of a formal non-state sector for the first time since 1975. Yet, despite the registration by late 2012 of over 50 NPAs – and the existence of a similar number that are not registered – the reality remains grim. Harassment and intimidation of those associated with the AEPF confirmed that civil society organizations continue to operate in an extremely restrictive environment, unless they work according to strict parameters set by the government.

Since the LPRP seized power in 1975, few Lao have any memory of a democratic multiparty system of government. For the last 38 years, no Lao has been asked if he or she would prefer a democratic system, as no public opinion surveys addressing this issue have been conducted. In private conversation, many Lao express satisfaction with the present system for the order and stability it imposes, even though almost all are critical of corruption. If freedom of expression were permitted, it is likely that some members of the educated middle class and students would express that they favor a greater measure of democracy.

Approval of  
democracy  
n/a

Although surveys do not exist, there exists a relatively high level of trust at the family, extended family and village level. Trust may also extend to patronage networks, members of the same ethnic group (among ethnic minorities), and people from the same region (among the lowland Lao), but not to the wider society. After the 1975 revolution, non-state social organization was not permitted (except in cases of spontaneous village cooperation), with all formal activities being channeled through the party's mass organizations and state bodies. Even since the 2009 Decree on Associations, conditions for voluntary autonomous organization have been highly restrictive. There is a degree of nascent cooperation among Lao NPAs but a recent crackdown in the wake of the AEPF has created fear and undermined trust.

Social capital  
4

## II. Economic Transformation

### 6 | Level of Socioeconomic Development

Question  
Score

The Lao regime proclaims its support for both ethnic and gender equality but, in both cases, inequality is to a large extent structurally ingrained. Poverty, a lack of infrastructure, and poor government services in remote and mountainous parts of the country still put ethnic minorities at a disadvantage. Backed by the World Bank and Asian Development Bank, the government has thus committed itself to a long-term poverty reduction program aimed at lifting the country out of its least-developed country status by 2020. In 2011, the Lao PDR's Human Development Index score stood at 0.543, ranking Laos 138th out of 187 countries.

Socioeconomic  
barriers  
4

Poverty has fallen but remains widespread in rural areas. Between 2002 and 2008, the latest year for which figures are available, the percentage of the population surviving on less than \$2 a day fell from 76.9% to 66%. Bolstered by increasing foreign aid and burgeoning FDI, per capita GDP rose to \$2,790 in 2011, but most of this increased wealth was concentrated in the national and provincial capitals. Between 2002 and 2008, the Gini coefficient of income distribution worsened from 32.6 to 36.7. Moreover, gross corruption has concentrated wealth in the hands of a

relatively small political elite. Even accounting for remittances from rural migrants seeking employment abroad (especially in Thailand), the rural-urban divide has continued to be the greatest structural barrier to decreasing disparities in wealth and living standards.

Although Laos has a relatively poor Gender Inequality Index score of 0.483 (2012), ranking 100 of 148 countries, the reality of gender exclusion is somewhat mixed. Female labor force participation was 77.7%, almost the same as for men (78.9%), women had a higher life expectancy than men (69 years compared to 66) and in 2011 women won a quarter of the seats in the National Assembly, a relatively high number in the region. Yet, while female participation in education has also improved, the ratio of female to male enrollment remains low – 93.3, 85.3 and 73.6 at primary, secondary and tertiary levels, respectively. Adult female literacy has improved to 70% but remains significantly lower than for men (85%).

Economic indicators		2009	2010	2011	2012
GDP	\$ M	5832.9	7181.4	8226.9	<b>9298.9</b>
GDP growth	%	7.5	8.5	8.0	<b>8.2</b>
Inflation (CPI)	%	0.0	6.0	7.6	<b>4.3</b>
Unemployment	%	-	-	-	-
Foreign direct investment	% of GDP	5.5	3.9	3.7	-
Export growth	%	3.7	24.9	14.5	-
Import growth	%	-2.5	2.6	25.1	-
Current account balance	\$ M	-60.9	29.3	-206.3	-
Public debt	% of GDP	61.9	61.0	54.4	<b>53.1</b>
External debt	\$ M	5736.5	5654.8	6158.3	-
Total debt service	\$ M	220.0	305.5	281.2	-

Economic indicators		2009	2010	2011	2012
Cash surplus or deficit	% of GDP	-1.7	-0.8	-1.0	-
Tax revenue	% of GDP	12.8	12.9	13.7	-
Government consumption	% of GDP	10.7	9.5	9.9	-
Public expnd. on edu.	% of GDP	-	3.3	-	-
Public expnd. on health	% of GDP	1.8	1.2	1.4	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	0.2	0.2	0.2	-

Sources: The World Bank, World Development Indicators 2013 | International Monetary Fund (IMF), World Economic Outlook 2013 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2013.

## 7 | Organization of the Market and Competition

Laos has made progress in moving from a command to a market-based economy. For example, prices are now set by the market, the Lao kip is convertible and profits from foreign investments can be transferred abroad. But competition operates within a relatively weak institutional and regulatory framework. When disputes arise, the legal system fails to provide businesses with protection against those with powerful political connections. In addition, while efforts have been made to provide foreign businesses with certainty, they remain vulnerable to arbitrary decision-making and collusion between local business and political interests. Moreover, the government retains ownership of what it considers to be “strategic” enterprises. The informal sector of the economy is significant.

Market-based  
competition  
5

The Decree on Trade Competition (2004) provides a rudimentary framework for regulating competition and monopolies, but the Trade Competition Commission it envisaged has not yet materialized. Regulations can often be circumvented through political contacts and a number of expanding business groups depend upon political connections. While most state-owned enterprises (SOEs) have been sold off or otherwise privatized, the government still retains control of those it considers “strategic” or essential for national development. These tend to be monopolistic, though this is changing in certain sectors including telecommunications and aviation.

Anti-monopoly  
policy  
3

Laos has moved to liberalize foreign trade since the mid-1980s. Tariffs have been reduced in order to meet the requirements of the ASEAN Free Trade Area (AFTA). Import trade is competitive, but some key exports (such as timber) are controlled. Having applied in 1997, Laos finally joined the WTO in February 2013. In the process, it has implemented a number of important reforms in areas such as taxation, foreign exchange, investment, and import and export procedures. There will be costs

Liberalization of  
foreign trade  
8

as well as benefits from WTO accession, with the former falling disproportionately on the agricultural sector.

Although legislation governing the Lao banking system is oriented toward international standards, and the government frequently reiterates its intention not to be involved in quasi-fiscal activities, a considerable degree of political interference remains, for instance the financing of state-owned enterprises by state-owned commercial banks (SOCB). Having twice been restructured and refinanced because of nonperforming loans, the SOCBs have demonstrated improved performance over the past decade. Yet the overall bank loan to deposit ratio increased from 71% in June 2011 to 85% in June 2012, while the level of nonperforming loans increased from 2.2% to 3.7%. The World Bank attributes these increases to increased credit growth, though continued political interference in determining loan eligibility may also be a factor.

Banking system

5

Several foreign banks have had branches in Vientiane, the nation's capital, for some time. More recently, there has been a pronounced expansion in the sector, with the establishment of new Lao-foreign joint ventures and Lao private banks. Coupled with rapid expansion in credit and limited supervision capacity, this has prompted the World Bank to caution Laos over the need to manage domestic demand. Tentatively, Laos is also developing a capital market. In 2009, Laos issued its first international bonds (denominated in Thai baht). In January 2011, a stock exchange opened for business in Vientiane, though only two companies – both SOEs – were listed as of February 2013. This model of partial privatization seems set to continue.

## 8 | Currency and Price Stability

Lao monetary policy over the past decade indicates the government is aware of the importance of keeping inflation under control. After annual inflation hit 110% in 1998-1999 – when the government, for political reasons, attempted to spend its way out of the Asian economic crisis – the government embarked upon a macroeconomic stabilization program. Inflation was reduced to an average of 15% between 2000 and 2003 and has remained under 10% since 2007. Since falling to zero in 2009 in the wake of the global financial crisis, inflation has fluctuated between 5.5% and 7.6%.

Anti-inflation /  
forex policy

7

The central bank of the Lao PDR is controlled by the state. The bank oversees a managed floating exchange rate regime. The official exchange rate tracks the free-market rate. Party policy is to maintain this system.

Lao authorities are aware of the need for macroeconomic stability, but in the Laos, politics takes priority. This means that ultimate decisions are taken not by the central bank, or even by the Ministry of Finance, but by the Politburo, most members of which have little understanding of macroeconomics. The party is not populist in its

Macrostability

6

response to macroeconomic challenges, however, and decision makers do take note of expert advice. As a result, the government has been prudent in limiting the deficit in order not to stoke inflation.

Since 2010, growing hydropower and mining receipts have boosted government revenue from 16.4% to 19.7% of GDP. With expenditure increasing only marginally, from 21.3 to 22% of GDP, the fiscal deficit has fallen from 4.9% to 2.3% of GDP. However, planned increases to public wages threaten to reverse this performance in 2013. Public debt fell to 44.4% of GDP in 2011. The corresponding net present value of debt (29.8%) convinced the IMF and World Bank to reclassify Laos's risk of debt distress from high to moderate. However, the prospect of heavy borrowing to fund large-scale projects, including the Laos-China railway, has raised concerns over future debt sustainability. Gross foreign-exchange reserves fell to \$608 million in June 2012, prompting World Bank caution over the need to manage domestic demand.

## 9 | Private Property

Although the Lao constitution theoretically protects property rights, all land is formally owned by the state and can be expropriated for state purposes. A land-titling program has been underway in some larger towns, and is slowly being extended into the countryside. False and disputed claims can in theory be resolved in a court of arbitration, but are more often settled through payment of bribes to relevant officials.

In rural areas, families possess user rights to agricultural land, which are transferable and heritable. Communities may also exercise traditional rights to non-agricultural land, including those ethnic minorities who practice shifting slash-and-burn farming. As the demand by foreign companies for land concessions for industrial agriculture has increased, authorities have often disregarded these traditional rights. As a result, land issues remain one of the principal areas of injustice and contestation in Laos today. The matter has been raised increasingly in the National Assembly, as well as by the nascent and still weak civil society sector.

Laos permits both domestic and foreign-owned private companies to operate, but state interference trumps market principles and the playing field is not level. Most state-owned enterprises have been privatized, but others still dominate their respective sectors. These sectors include electricity and water, which the government considers to be of "strategic" importance. In addition, the state (or state leaders) often retains a substantial degree of informal control over enterprises that are formally privatized. In other cases, government contracts are often awarded to private companies that have political relationships with high-ranking party members. In other words, there remain close links between business and the party, even where the two are ostensibly separate. Indeed, commercial projects sometimes have difficulty

Property rights  
3

Private enterprise  
5

getting off the ground without such political support, not least due to the difficulty of accessing formal credit. Foreign companies sometimes pay substantial sums for such patronage.

## 10 | Welfare Regime

Laos has no comprehensive social security system to alleviate poverty and health insurance schemes cover only a small fraction of the population. The only aged or invalidity pensions are those provided by the Ministry of Labor and Social Welfare to veterans who fought on the revolutionary side in the civil war. Eradicating poverty is the primary objective of both the National Growth and Poverty Eradication Strategy (2004) and the latest NSEDP (2011-2015). Although poverty is certainly falling, implementation of these strategies has been patchy. Revenue from hydropower and mining are providing increased funding for social programs, but an effective social safety net is still a long way off.

Social safety nets

3

The Lao government recognizes that some segments of the population, notably geographically remote ethnic minorities, face significant disadvantages. It has thus introduced some measures to alleviate poverty in mountainous parts of the country, including a controversial resettlement program. Additional programs designed to improve living conditions for ethnic minorities are inadequate in scope and open to abuse by local officials. Only the small-scale networks of kinship, village, ethnicity, and patronage work effectively for providing any social safety.

Although, in principle, all Lao – including women and ethnic minorities – have equal opportunity to access education, public office and employment, the reality is mixed. While women make up 25% of the current National Assembly and the Lao Women’s Union remains well organized and influential, women constitute less than 10% of the all-important LPRP Politburo (1 of 11 members) and central committee (5 of 61). Despite great improvements since the 1990s, female access to education remains significantly lower than for men, as does female literacy (70% compared to 85%). On the other hand, the female labor force participation rate (77.7% compared to 78.9% for men) is one of the highest in the region.

Equal opportunity

4

Ethnic minority populations also have poorer access to education than the ethnic Lao-Tai majority, a problem that is multiplied for girls from ethnic minorities. However, the party and the army both target ethnic minorities for recruitment. Indeed, almost half (5 of 11) of the Politburo falls into this category. Still, the prevailing political culture puts ethnic minorities at a disadvantage. Powerful party members build patronage networks of loyal followers who benefit accordingly. Scholarships, jobs in the public service and promotions all depend on whether support can be obtained



from a powerful patron. Those without such connections are at a disadvantage, no matter how talented they may be.

## 11 | Economic Performance

Strong economic growth, averaging almost 8% since 2007, has more than doubled per capita income in the past decade to \$2,790 (2011, PPP). Most growth over this period has occurred in the industrial sector (notably hydropower and mining), though the resource sectors' share of GDP growth has decreased since peaking in 2010. The service and construction sectors – boosted by a series of international events in Vientiane – have also been performing well. However, the agricultural sector, which continues to employ close to 80% of the population, accounts for less than 40% of GDP and agricultural growth remains slow. Although inflation has hovered between 5% and 7% over the last two years, inflation on food was a concern in 2010.

A major driver of GDP growth has been foreign direct investment, particularly from Vietnam, Thailand and China, and particularly in the hydropower and mining industries. Total annual FDI almost doubled from approximately \$800 million in 2010 to \$1.6 billion in 2012, though this was offset by deterioration in the current account balance.

Meanwhile, the budget deficit decreased to 2.3% of GDP in 2012 while public debt fell to 44.4% of GDP, encouraging the IMF and World Bank to revise Laos's policy performance from weak to medium and to reclassify its risk of debt distress from high to moderate. No reliable statistics are available for unemployment, but current estimates of 2.5% would appear to be conservative.

## 12 | Sustainability

Despite paying lip service, the Lao government takes little heed of environmental concerns. It has set aside 17 National Biodiversity Conservation Areas (covering just over 10% of the national territory), where both flora and fauna are nominally protected, but logging controls are only enforced sporadically, especially where the military is involved. Typifying the priority placed on growth, construction is proceeding on the Xayabury Dam, the first on the lower Mekong River, despite the deep reservations of downstream countries and international environmental groups. Criticism of the dam and other major projects cannot be voiced in the state-controlled Lao media, however. The government expresses most environmental concern over the swidden agriculture practices of primarily ethnic minorities, and has a policy in place of resettling them in locations where their livelihoods can be controlled more closely. But this effort has served more as a means to integrate minorities into the state, rather than to protect Laos's dwindling forests.

Output strength  
7

Environmental  
policy  
4

Although progress has been made, the government has failed to make education a national priority and the quality of education at all three levels remains low in Laos. Public education spending rose to 3.3% of GDP in 2010, compared to 3% in 2006 and only 2.3% in 2008. As a percentage of the budget, expenditure has increased slightly from 12.2% in 2008 to 13.2% in 2010, though it remains less than in 2006 (15.8%). With the growth of the economy, these increases are not insubstantial, but much more is required. Teachers remain poorly paid, textbooks in short supply, and schools still have minimal facilities. Education attracts significant funds from foreign donors. A few private schools operate, especially in the capital, Vientiane, where they predominantly offer courses in language (mainly English), business (management, accounting) and information technology. Investment in research and development is nonexistent.

Education policy /  
R&D

3

## Transformation Management

### I. Level of Difficulty

Historically, the greatest structural constraint on effective governance in Laos has been geography. Not only landlocked, the country is mountainous in the north and east while waterfalls on the frontier make navigation down the Mekong River to Cambodia impossible. Infrastructure has been poorly developed, making communication difficult with neighboring countries, except with Thailand.

Structural  
constraints

6

In the past two decades, however, the Asian Development Bank's Greater Mekong Subregion scheme, within which Laos is strategically situated, has greatly helped to improve regional integration. Laos now promotes itself as "land-linked" rather than landlocked. Major roads cross the country linking Thailand and Vietnam in an east-west direction and China and Thailand along a north-south corridor. Five bridges span the Mekong and two more are planned or under construction. Navigation on the river itself has been improved and the Lao government has committed to building a railway from Vientiane to the Chinese border.

Another significant constraint is the low level of development of the country's human resources. Educational levels are below ASEAN averages, as are levels of literacy. Poverty rates remain high, especially in rural areas, with 33.9% of the population below the U.N. income poverty level of PPP \$1.25 per day. HIV/AIDS, though low by international standards, is a continuing concern, while malaria and tuberculosis continue to take their toll.

Ethnically, linguistically and culturally divided, Laos does not enjoy strong civil society traditions. During the "revolutionary struggle", solidarity and cooperation – which previously existed mainly at the village level – was strengthened among different groups, but promises to ethnic groups that supported the revolution have not been fulfilled. The promise represented by the 2009 Decree on Associations, which permitted the formation of independent NPAs, has been dashed in the past year due to state intimidation and harassment.

Civil society  
traditions

10

There are no obvious ethnic, religious or social conflicts in Laos, but this is partly because of the draconian control exercised by the ruling party. The longest-running ethnic conflict was between a relatively small group of Hmong and the Lao

Conflict intensity

3

government. The insurgents originally believed that the United States would support the establishment of an independent Hmong homeland, but the insurgency has collapsed in recent years, despite ongoing instances of isolated violence. It should be noted that several pro-government Hmong hold positions of authority in both the LPRP and the government. The Hmong president of the National Assembly, Pany Yathotou, for instance, is also a member of the Politburo.

The government bans all Christian and other religious missionary activity in Laos, but supports Buddhism as central to Lao cultural identity. The small Christian community is equally divided between Catholics (ethnic Lao) and Evangelical Protestants (ethnic minorities), and both keep a low profile. What little social conflict exists is mediated by the Lao Front for National Construction at the direction of the party.

## II. Management Performance

### 14 | Steering Capability

The long-term aims of the political leadership (the central committee of the LPRP) are two-fold. The first is to retain a monopoly on power, which means preserving the current one-party, “Marxist-Leninist” system. This objective has been reiterated at every party congress, at which warnings are issued against any “evolution” toward democracy. The second aim, subordinate to the first, is to develop the economy and raise living standards. To this end, the LPRP outlines and endorses a new five-year NSEDP at each congress, most recently the plan for 2011-2015.

The government is genuine in wanting to develop the economy and reduce poverty, a key part of its strategic long-term priority of “graduating” from least-developed country status by 2020. But political survival is paramount for the party, which enjoys the strong backing of both Vietnam and China. Economic development certainly strengthens the position of the party but, if party leaders believe these priorities to be in conflict, politics takes priority. At the same time, the effective lack of democracy enables the leadership to pursue unpopular development strategies that boost the economy. But the lack of democratic accountability means the resulting policies – such as “turning land into capital” – can have disastrous consequences for rural livelihoods.

Because political survival takes precedence, the political leadership is reluctant to embark on reforms that it believes might undermine its political interests. There is thus a great degree of variation in implementation. On the one hand, “mega-projects,” often funded with Chinese or Vietnamese assistance, are implemented with the full

Question  
Score

Prioritization  
4

Implementation  
3

support of the state. On the other, reforms agreed upon with international donors (to ensure the flow of aid), often aimed at improving the functioning of the market economy or supporting civil society, are subsequently left unimplemented for fear they will weaken the party, or rather the political position of powerful individuals or groups within the party. For the ruling party, no necessary link exists between the market economy and democracy. This is frustrating for international donors, who are convinced that the Lao economy would be stronger if both economic and political reforms were enacted together.

In addition, the effective implementation of endorsed policies, such as poverty reduction and improved bureaucratic efficiency, has been undermined by increased levels of corruption and poor law enforcement. Another problem is that powerful provincial governors do not always implement laws and regulations put in place by the central government. Rising corruption levels have reinforced the government's reluctance to introduce measures increasing transparency (despite regular commitments to do so), thus further limiting the efficiency of policy implementation.

Despite a gradual change in the makeup of the party Politburo and central committee, the leadership is committed to maintaining the political status quo above all else. Not surprisingly, this remains the greatest barrier to policy learning. The leadership is not inflexible, however, as the relative success of the country's market economy over the last two decades indicates. As it has been replenished, the leadership has naturally developed a better understanding of the workings of a market economy, the impact of global economic forces and the motives of international organizations pressing for reform. But what it understands best is Lao politics, especially the politics of party power and patronage. Many decisions are made (or not made) for intra-party political reasons that are usually obscure to observers.

Many hoped that former Prime Minister Bouasone Bouphavanh, appointed after the 8th party congress in 2006, would represent not just a younger generation but also a new approach to reform, including better transparency of governance and enforcing the rule of law. The irony, however, was that he was only able to introduce reforms by building his own patronage network of reformist supporters in the time-honored Lao way. This he tried to do, but apparently without success, as he resigned at the end of December 2010. His replacement, party stalwart Thongsing Thammavong, has abided more by the status quo, including the LPRP's continued monopoly on power. International outcries, for example, over the disappearance of Sombath Somphone, may increase pressure on the regime. But, so far, this incident has resulted in familiar stonewalling rather than policy learning.

As for economic policy, the government in Laos reluctantly accepts some advice from international institutions (the IMF, World Bank, ADB, etc.) as a condition for

Policy learning  
4

receiving aid. But whatever impetus there is for economic reform comes mainly from Vietnam and China, whose state-supervised economic model Laos has adopted.

## 15 | Resource Efficiency

The government fails to make full use of the human, financial and organizational resources available to it. Lao political culture revolves around the competitive interests of powerful individuals, their families and their networks of political clients. At its core lies the benefits and opportunities a powerful individual can provide, by way of employment and other economic advantages. Thus, personnel are most often appointed not because they are the most qualified and capable for the job, but because of their political contacts.

Efficient use of assets

4

Laos has a slowly increasing pool of foreign-educated, technically competent administrative personnel, but they are all too often without political influence and reluctant to make any decision that might jeopardize their careers. There are no competitive recruiting procedures and the public service is highly politicized. When some decentralization took place, corruption increased at the provincial level. Centrally appointed civil servants (teachers, health workers) were unpaid, and revenue was not remitted to the central government. Subsequent re-centralization of financial matters (including payments of public servants, taxation and customs) did little to increase revenue, however, for corruption permeates the bureaucracy.

Policy coordination is weak, largely because of competing interests between ministries, and between the central and provincial administrative levels. The staffing of ministries is highly politicized, as ministers often make appointments designed to strengthen their patronage networks. Ministries essentially function as fiefdoms to be protected from outside interference, which limits coordination and cooperation. Moreover, policy is often ad hoc, driven by the desire to take advantage of donor projects. Horizontal coordination is almost nonexistent. Furthermore, decision-making is centralized and hierarchical, and is a prerogative senior officials guard jealously. Even the most minor technical matters get passed up the hierarchy where decisions are made.

Policy coordination

3

Corruption is ubiquitous in Laos, a chronic and growing problem that has been exacerbated by the example provided by senior party leaders, and by foreign investors' willingness to buy political support and pay off officials. It is fair to say that a culture of corruption has taken hold, encouraged by the political culture of patronage that operates within the LPRP.

Anti-corruption policy

2

A presidential Anti-Corruption Commission did virtually nothing to improve matters, and even the passage of an Anti-Corruption Law in 2005 has had minimal effect. The party-controlled media frequently runs articles condemning corruption, but without

naming names. A State Inspection Law passed in June 2007 was supposed to strengthen the State Inspection Authority, which is charged with policing the public service to ensure officials are not using their positions for personal gain (which almost all do). The government has also established an audit office, but it sits within the Ministry of Finance and does not function independently. Thus, the government does have integrity mechanisms in place but they are not independent and do not perform their function. Although low-level officials have faced criminal charges for corruption, there have been no high-profile prosecutions of senior officials (unlike in Vietnam and China).

Corruption is encouraged not just because of the politics of patronage, but also because of the secrecy of the party, its structure, and the extraordinary overlap between party membership, government, the bureaucracy and the judiciary. Party finances are never published, officeholders are not accountable, and if the Central Committee does anything at all, it is never publicized. The problem of corruption has come up in the National Assembly, but again, no one has named names. Anecdotal evidence suggests that the rising levels of corruption are translating into diminishing popular support for the party.

The principal interest groups and economic actors urging anti-corruption reforms on the Lao government are international lending agencies (IMF, World Bank, ADB), foreign governments with substantial aid programs, and foreign NGOs. Of these, the first have been most insistent in urging reform, and have had some success by attaching conditions to large loans. Japan is by far the largest aid donor but is reluctant to put pressure on the Lao government. Vietnam and China have much greater influence, but dealings with them are the least transparent of all.

## 16 | Consensus-Building

Given that all political dissent is stifled, it is impossible to know if consensus exists in Laos regarding the direction of either political or economic reform. Local NPAs have not yet been allowed to play a meaningful role as consensus partners. Anecdotally, many urban people seem to subscribe to market-based economic development but there are no forums to express dissent or pose alternatives. Everything is decided within the party where, by contrast, discussion and old-fashioned political horse-trading can be intense.

Though it is impossible to penetrate internal party dynamics, the LPRP appears (despite occasional cracks) to be in broad agreement that it should retain a monopoly on political power, and that the best way to develop the economy is by permitting a free market to function. There is also broad support, in principle, for a strategy that would enable Laos to graduate from LDC status by 2020. Beyond that, there is little consensus on the purpose of economic development. Several senior party members

Consensus on goals

4

seem to believe the purpose is to make themselves and their families rich, rather than to develop the country's human resources and eradicate poverty.

There is no opposition or dissident movement in Laos urging the government to speed up reform. Likewise, those elements within the party and bureaucracy who accept the logic of reform (at least regarding the economy), and would like to see corruption reduced, represent a small minority. The majority of party members oppose any move toward democracy. Those opposed to reform also include senior military officers, who probably have veto powers sufficient to torpedo any democratic reforms.

Anti-democratic  
actors

1

Political cleavages in Laos are rarely ideological. Rather, cleavages arise from a competition for resources between powerful patrons and their clients, between provincial and regional interests, and between the dominant lowland Lao and ethnic minorities who believe they are not being equitably treated. The party cannot eliminate these divisions, but it has been relatively effective in preventing them from escalating. Compromise is common among the Lao, who prefer to avoid face-to-face conflict. The “democratic centralism” that operates within the LPRP also helps build consensus. There are reports of tensions in the party between military and civilian factions, old-guard revolutionaries and new-generation technocrats, and those who lean toward China rather than Vietnam, but these are difficult to confirm since differences are never aired publicly.

Cleavage /  
conflict  
management

6

Despite its decree allowing local Lao NPAs to be established in 2009, the LPRP does not encourage civic engagement or solidarity among Lao citizens, unless it is in support of the party and its policies. NPAs have to apply for registration, so the government can reject applications, and those who do not quietly submit to the official line – for instance over land disputes – have been intimidated. In fact, the disappearance of senior civil society leader, Sombath Somphone in late 2012 was presumably linked to his advocacy of victims of such intimidation. Some professional associations exist (such as the Lao Bar Association and the Lao National Chamber of Commerce and Industry) but, like the party's mass organizations, only under the close supervision of the party. No political debate is permitted, except within the party itself.

Civil society  
participation

2

The ruling party appears to be making some efforts to reconcile with overseas Lao communities, who fled the country after the 1975 revolution, by inviting delegations to national events such as the Southeast Asian Games in 2009. However, reconciliation takes place purely on the terms of the regime, which continues to legitimize its rule by celebrating the history of revolutionary struggle. Overseas Lao may visit and invest in Laos, provided they do not involve themselves in politics. Some have returned to live permanently in the land of their birth, but as foreign nationals since the government refuses to allow dual citizenship.

Reconciliation

4



The government did make an effort to bring about reconciliation with those Hmong and other members of ethnic minorities who fought on the Royal Lao side during the “30-year struggle” (1945-1975), by offering amnesty to all who surrendered. Those who did not accept this offer were subject to continuing military repression. The treatment of Hmong who have surrendered over the last few years has not been transparent, and the government has prevented international observers from making contact with those who have been resettled.

## 17 | International Cooperation

Laos has been remarkably successful in attracting foreign aid from across the ideological spectrum. In order to do so, it includes development partners in an annual roundtable process that helps to develop and monitor its 5-yearly NSEDPs. Nevertheless, while the government presents itself as willing to consider economic reforms in order to bring about greater administrative efficiency and transparency, and agrees to make just enough progress (at least on paper) to ensure that economic assistance continues, it resists any international pressure for democratic reform. This is a fine line but one the government has walked nimbly. However, authorities have been slow to implement agreed-upon reform programs, and many in the international community have become frustrated and suspicious of affable Lao promises. Increasing Chinese and Vietnamese assistance – which comes with fewer strings attached – has provided an appealing alternative and many more opportunities for rent-seeking.

Effective use of support

6

The Lao government is generally considered to be a reliable partner by international organizations, NGOs and bilateral partners. Foreign investors are much more wary. In 2012, a Macau-based casino investor alleged the government had broken international treaties and launched proceedings against it in the World Bank’s International Centre for the Settlement of Investment Disputes. Despite slight improvement in recent years, the World Bank ranks Laos 163rd out of 185 countries (2013) in terms of the difficulty of doing business.

Credibility

6

Laos takes its membership of ASEAN, which it joined in 1997, extremely seriously. Having always understood the need to cooperate with its larger neighbors, and appreciating the ASEAN principle of non-interference, Laos is more comfortable cooperating with other ASEAN states than with Western countries. Laos is also an enthusiastic member of the ADB’s Greater Mekong Subregion (GMS) scheme, which includes the Chinese province of Yunnan as well as the mainland ASEAN states. It has enthusiastically embraced an extensive communications network among GMS members to turn disadvantage into advantage by making landlocked Laos “land-linked.” Still, the country retains its closest relations with its “fraternal” communist ally, Vietnam, and has become progressively closer to China. On the other hand, by pressing ahead with plans to develop the Xayabury Dam on the

Regional cooperation

8

Mekong River, despite protests from Vietnam and Cambodia that it is contravening the 1995 Mekong Agreement, Laos has demonstrated a willingness to act unilaterally in the face of regional criticism.

## Strategic Outlook

The Lao PDR has made no progress toward democracy during the past three years. In fact, the recent clampdown on political expression suggests a shift backwards. Likewise, although the ruling regime will continue to introduce reforms required of AFTA and WTO membership, it will continue to resist those that would provide greater transparency and accountability in the areas of revenue collection and expenditure.

In spite of this reality, Laos enjoys good relations with its neighbors, fellow ASEAN members and Western powers, both for security reasons and to ensure the continued flow of official development assistance (ODA) and foreign direct investment (FDI). Most ODA has come from Japan and multilateral lenders such as the World Bank and the ADB, while, until recently, most FDI has come from Thailand and the West. Over the last few years, though, there has been growing investment and influence from China, which has caused some concern in the region, and even in Laos itself. Investment is also flooding the country from Vietnam, Laos's erstwhile political ally. As a result, Laos no longer relies to the extent it once did on Western and Japanese ODA.

Those who provide economic assistance to the Lao PDR must do so, therefore, with a clear understanding of what this is likely to achieve. Well-targeted economic and human resource development may benefit some of the poorest among the Lao population, and infrastructure projects will have a long-term impact. But economic development will not result automatically in political change, for the tiny wealthy and educated elite has been co-opted by the party and knows better than to advocate for democracy. The business elite too has been co-opted. While the LPRP remains in power, it will continue to operate as it has always done, balancing competing interests within the party and dispensing benefits to its members and other vested interests in ways that are opaque to most outside observers.

The outlook is for more of the same in the years ahead: just enough promise of economic reform to keep the ODA flowing with no practical effect that might threaten the party's hold on power. This is hardly an optimal outcome, but it is one with which Western powers, aid agencies and NGOs must work. While recognizing that significant political change remains extremely unlikely in the foreseeable future, international actors should continue to pursue the following strategies:

- Keep economic reform on the agenda in two ways: by stressing the attractiveness of transparent processes for foreign investors; and by demonstrating benefits for development and economic growth where reforms have been introduced.
- Strengthen the rule of law by providing programs to support the National Assembly (workshops, exchange visits), disseminate laws that have been passed (by helping with printing costs, conducting regional workshops), and encourage implementation by stressing the benefits for Lao society.

- Promote education as a national priority through support for the Ministry of Education (curriculum workshops, producing and printing textbooks, teacher training, etc.), by stressing economic benefits, and by making comparisons with ASEAN states and other Asian countries.

As the past two years have demonstrated, however, such efforts will not suffice to develop civil society or to lay foundations for a more democratic system. Therefore, international actors should raise concerns over the recent clampdown on civil society with government counterparts, voice these concerns publicly and internationally, and urge the government to uphold its own constitution. If international actors face continued stonewalling, as seems likely, they should consider applying appropriate forms of pressure and reassessing their goals in working with the Lao government. At the same time, international actors should try to convince the government of the benefits of cooperating with democratic countries, particularly when compared with the negative consequences of poorly regulated natural resource-based development underwritten by unscrupulous foreign investors.