



POLICY BRIEF

ADDRESSING THE IMPACTS OF THE PHASING OUT OF TEXTILES AND CLOTHING QUOTAS IN LAO PDR



DIVERSIFICATION AND VALUE ADDITION

The diversification of a country's industry is an important element for a stable and sound economy to absorb a proportion of the growing labor force. The more diversified a country's industry is, the better the opportunities to recover from shocks in the form of competition, price falls due to excess supply, etc. In a combined analysis of the market potential and human development impacts of various sectors, three sectors that meet these criteria are identified: tourism, handicrafts and food processing.

Impacts of tourism on economic and human development

Tourism is making an important contribution to socio-economic development in the Lao PDR. The sector has received significant government attention and promotions such as the "Visit Lao Year" campaign in 1999; tourism development strategies have been identified and carefully developed. The study shows that major contributions of tourism to economic development are visible in the following areas:

- Direct and indirect promotion of domestic investment in tourism facilities;
- Indirect enhancement of infrastructure, such as on roads, airports, harbors, telecommunication systems, electricity, water supply, and so on;
- Direct and indirect employment generation;
- Generation of export revenue;
- Income distribution to local and rural areas.

Tourism is one of the major sectors to have played a significant role in employment creation and economic development in the country. With the increasing number of tourist arrivals, revenue from the tourism industry accounted for approximately 7 percent of the GDP in 2004 and has continued to grow steadily in recent years. The national revenue generated from tourism has soared from US\$2.25 million in 1991 to US\$147 million in 2005. The industry has been able to offer a reliable source of income for many Lao.

Currently, tourism generates approximately 37,000 direct jobs in the hospitality sector (hotels,

restaurants, bars), the retail sector (souvenir and handicraft shops), travel agents and tour operators, and the transport sector.

The domestic inter-sectoral links with the tourism industry are significant, with the tourism sector generating (or supporting) a massive 630,000 indirect jobs through the supply of goods and services needed by tourism-related businesses. The tourism industry has shaped the economy significantly through the development of businesses in various sectors and the improvement of infrastructure and public facilities. Tourism has also assisted in reducing poverty in certain local communities through participation in eco-tourism activities such as home stays, guided tours and selling handicrafts. This type of tourism fosters greater interaction among tourists and local communities.

Contribution to the economy: As the highest revenue generation sector in the country, tourism has caught the interest of various stakeholders. Tourism is a broad-scale economic activity and its stakeholders have become the main players that influence and support the tourism industry. At the central level, the major players of tourism include government departments and ministries. At the provincial level, there are also tourism-related divisions and offices that manage and promote the tourism industry. Furthermore, international aid agencies support, fund and set up tourism projects in cooperation with the corresponding government agencies.

Constraints: The industry faces some constraints from both the demand and supply side. From a demand side point of view, social problems, natural disasters and disease epidemics can act as major

threats towards its growth. Countries that have high-quality tourism attractions, infrastructure and marketing campaigns are better equipped to attract more tourists. Infrastructure such as roads and electricity are still lacking in some areas and many tourist sites are still underdeveloped. Moreover, Lao PDR has limited capacity to build facilities to meet demand from niche consumers who want to receive world-class luxury services such as in neighbouring countries like Thailand and China.

From the supply side, inefficient infrastructure (particularly transportation) and a lack of skilled human resources are identified as current (short-term) obstacles to the development of Lao tourism. Concerns about skills and education were far more apparent amongst tourism firms than amongst firms in the manufacturing sector. An investment climate survey by ADB in 2005 to determine the key constraints faced by private firms in the tourism sector found that about 45 percent of the surveyed firms also perceived infrastructure to be the most important constraint in the tourism sector.

Opportunities: The study finds that there are a number of opportunities presented to Lao tourism. On the demand side, Lao PDR is widely known as the “Jewel of the Mekong” and will attract tourists wishing to visit a peaceful place of natural and cultural beauty in an increasingly industrialized region. Lao PDRs’ cultural and natural tourism assets have attracted particular interest from tourists. In addition, as the country has become part of a number of regional and international associations, it has received a wide range of support and benefits, which are strengthening tourism demand. From the supply side, on the other hand, many of Lao PDRs’ existing cultural and natural tourism assets have attracted more interest from tourists through developing new forms of tourism, such as ecotourism.

Regarding employment levels in 2008, the LNTA estimates national revenue from tourism will total US\$290, million. In 2004, it was estimated that 23 international tourist arrivals creates one full time job. If this same ratio applies in the future, there will be 666,000 job opportunities in 2008 (37,000 directly and 639,000 indirectly employed). By 2010, with the forecasted number of tourist arrivals, the direct employment in the tourism industry will reach 89,000, approximately 22 percent of the potential new labor force that year, which will compensate for losses of employment in the garment sector.

Possible Actions: Infrastructure improvements are needed on rural roads to tourist attraction areas. There will also need to be improved maintenance of current sites, as well as new sites discovered and developed. For the transport system, action should be taken to expand public transport at the provincial level; policies on its costs should be improved with fixed price standards, as well as improved maintenance of transport vehicles.

In the case of tourism services and facilities, the study team recommends actions to obtain more diversification of products and services, e.g. tourist walking zones, home stays and community-based tourism. It also recommends further promotion of Lao products, visa waivers for non-reciprocal countries and improved efficiency when granting visas on arrival.

In terms of skills and education, the establishment of vocational training schools in tourism, language training necessary for tourism-related service workers, refreshment courses for tour guides and building professional integrity and skills in hospitality among service providers are crucial.

Impacts of handicrafts on economic and human development

The handicraft sector is a pro-poor industry that creates a high level of employment and generates income for local people, particularly those in rural areas. Handicraft production is often carried out alongside farming activities, which means that up to 85 percent of the Lao population could potentially be engaged in some forms of handicraft making.

If the current trend continues, the handicraft industry could potentially provide employment to a larger number of people - both formally and informally. Considering formal employment alone, it was estimated that 20,000 artisans were involved in this industry. Coupled with relatively low required investment costs, it is estimated that export revenues from handicrafts will increase from US\$13 million in 2004 to US\$40 million by 2010. This would mean the handicraft share of total exports would increase from 1.7 percent in 2004 to 2 percent by 2010, and employment would be doubled. This increase in employment is estimated to account for about 10 percent of the potential labour force by 2010 (including both new labour and possibly displaced workers from the garment industry).

Contribution to the economy: Lao PDR is slowly gaining an international reputation for its handicrafts. Traditional woven textiles, jewellery and wood products are attracting the interest of many foreign customers, especially those with traditional and contemporary designs using ethnic patterns. The major exported handicraft products are woven cotton and silk, woodcarvings, silver and gold ornaments, and bamboo and rattan items.

There is no official data on how much handicrafts contribute to the national economy, due to the informal nature of the trade, but based on employment data, the contribution is believed to be high. Handicrafts are particularly important for households in the rural sector, and provide additional income for families. There are also large informal exports to neighbouring countries, and “suitcase” trading to foreign countries.

It has been estimated that the number of handicraft producers in 2003 numbered no less than 120,000. Both direct and indirect employment in the handicraft sector have accounted for approximately 4 percent of the total labour force in the past few years. However, those who can make products that meet necessary quality standards for export are relatively scarce. It is therefore very important to conduct further studies on how to increase productivity and quality in this sector.

Constraints: The Lao handicraft sector faces a number of constraints in enhancing its value addition. The major factors contributing to low value addition in the handicraft sector, as with the garment industry, mainly come from the lack of the supporting industries that provide intermediate goods; irregular or insufficient supply of raw materials from local suppliers; a shortage of skilled labour, particularly for higher-end goods; inadequate investment in technology and efficient machineries; lack of effective marketing strategies and designs; and limited access to information about the market.

Opportunities: There are a number of opportunities to further develop the Lao handicraft industry. From the demand side, preferential trade agreements, access to fair trade labels and networks, development of niche products, and a continuous increase in tourism are favorable to its development and growth. In addition, the effective and efficient use of the country’s natural resources combined with the already available skilled producers and low labor

costs places the handicraft sector in a competitive position. The problems of insufficient raw materials for woodcrafters and furniture-makers can be met by using plantation wood. And to the benefit of silk producers, sericulture has the comparative advantage of land abundance; growing mulberry trees for silkworm breeding seems to be a potential segment to exploit in agriculture.

Possible Actions: There are a number of possible responses to improve the sector’s performance. When it comes to market access and information, actions range from organising trade fairs and exhibitions and night markets for selling handicrafts where tourists are concentrated to integrating handicrafts into community-based tourism with the possibility of direct sales. In terms of access to finance, proposals cover capacity building in managing micro-finance, promotion of short-term credit with reasonable conditions and village funds contributed by producers or villagers.

Further protection of intellectual property rights initiatives like competition among producers or the adoption of “geographical indicators” could be considered.

In terms of skills training, the government, in cooperation with the private sector, could strengthen existing training centres with an adapted curriculum. There is a need to raise awareness of the importance of vocational training in handicrafts to potential students, as well as providing skills testing and certification to producers and service-related training in management and advertising. Responses on quality issues refer to standards required by importing countries and the capacity of Lao producers to meet these standards. On value addition, the industry could adopt proper packaging with labels on content explanation, origins of the product and trademarks with the unique features of each province or region.

Impacts of food processing industry on economic and human development

The agriculture sector accounts for a significant 77 percent of the total labour force in the Lao PDR and contributes approximately 47 percent of the GDP. In early 2006, there were two major companies that produced processed fruit and vegetables for export, but the opportunities for additional firms and for more exports are significant. Processed fruit and vegetable products from those two companies include

jam, fruit juice, canned baby corn, bamboo shoots, mangoes and pineapples. More than 90 percent of those processed products are exported to the EU. Processed fruits and vegetables have increased by 118 percent in value and 94 percent in volume over the past five years.

Contribution to the economy: Two important products in the food processing sector are coffee and tea. Although the Lao coffee industry is relatively young, it has been one of the major export products and sources of foreign revenue in Laos since 1990. In fact, coffee was the sixth largest export commodity in 2004, with a total value of US\$13.02 million and US\$9.6 million in 2004 and 2005 respectively. The main export market is the EU. While the domestic market for tea is small, international demand is dynamic. Lao tea production was 160 tons in 2001 and reached 180 tons in 2004. Currently there are a number of local companies producing tea for both local supply and for export. The export performance of tea from Lao PDR has been impressive, with export earnings increasing by over 90 percent a year between 1999 and 2003.

The available statistics indicate that the number of production workers in the food processing sector increased by 23 percent from 2,800 in 2003 to 3,400 in 2004. It is estimated that at least 90,000 agricultural jobs are directly associated with the food processing industry. Available data reveals that at least 12,000 farmers are involved in supplying fruit and vegetables to the food-processing factories. Key players are farmers and middle traders who buy and resell crops from farmers.

Constraints: The constraints on the supply side are similar as in other sectors, e.g. shortage of raw materials, lack of access to market information, credits, skills and education, and lack of supporting industries. The food processing industry faces challenges to meet international standards to receive organic certification.

On the demand side, Lao producers are discriminated against, as their products receive variable tariff rates from international markets especially from EU and ASEAN countries, even though certain trade preferential agreements are in place.

Opportunities: Food processing products have the potential to break into the EU market, and the importance given to healthy food can play well into

the hands of domestic producers once organic certification is obtained. The country's abundance of natural resources is also an advantage. Through expansion of the food processing sector, farmers will be provided with assured markets for crops, regular income and permanent employment. As a result, farmers will move from subsistent to commercial farming, the country will benefit from increased exports and decreased imports of agricultural produce, and, most importantly, the food processing industry will contribute to reducing poverty and expanding opportunities and choice for rural families.

The food processing sector in Lao PDR is still in its early stages, but its potential for export and employment growth is large. In recognition of this, the Government has identified the food and beverage processing industry as the highest priority sector to develop. Currently, the exports of food processing products are concentrated within a few major companies. However, the number of smaller exporters is likely to increase.

Possible actions: On the inadequate supply of raw materials, the study proposes contract farming on terms that benefit both, farmers and food processing firms, as well as technical assistance to farmers to ensure crops are being planted in both seasons. A Farmers' Association should be established to boost farmers' power in negotiations and to encourage more planting, research and development. Land concessions should be provided to food processing companies.

On access to market information, the initiatives proposed by the team refer to strengthening cooperation between line ministries and groups of producers in sharing market information, widening the Lao Agricultural Product Processing Group network with more food processing companies, improvements in telecommunication and more participation of producers at national and international fairs. On access to formal credit loans for agriculture, these could be given lower interest rates than commercial investments and micro-finance projects implemented throughout the country.

In terms of skills and education, the study has found that the current vocational schools provide courses related only to cooking, while training in hygiene at factories should be encouraged. The factories should also set up their own training. On lack of supporting industries, it is mentioned that production of

intermediate products such as cans, bottles, bags, boxes, and labels should be increased with support to existing factories to improve the quality of products, and the Government should encourage more investment in this area.

Further infrastructure investments in transport, irrigation and water management systems are necessary and on mitigating high transportation costs the team proposes alternative transport routes for exports, such as through Vietnam, and further research on trade facilitation, the promotion of an attractive investment climate for investors in the shipping and transportation industry, and increasing opening hours at checkpoints.

On quality standards, measures proposed include the establishment of Grading System Centres as a reference point for pricing standards, and a division under the MAF responsible for quality control. Finally, under local consumer confidence, based on the observation that Lao processed food products are not popular among Lao consumers, awareness could be enhanced and with similar effect Consumer Groups could take on the responsibility to protect the right of consumers and ensure the safety of products.

Summary

Tourism has played a significant role in the economic development and employment creation in the Lao PDR. The tourism industry has affected the economy and local communities, particularly in terms of poverty reduction and participation of local communities through ecotourism. However, the future benefits of tourism depend on the mechanisms for benefit distributions, such as (i) the ability to cater for various types of tourists, (ii) the development of tourist sites and (iii) the development of other supporting industries. In addition, the tourism sector still needs a lot of human resources - particularly female staff. In order to have a sufficient labour supply to this sector, there needs to be more cooperation and support from the involved parties. However, it should be noted that developing the tourism industry is a vast investment and has implications for numerous manufacturing industries. The handicraft sector has been embedded into the way of life for many Lao people. The empowerment of, and choices for, many women also increase, despite the somewhat long hours they spend in making the handicrafts. It has created considerable export revenue, employment and income for local

producers and sellers. The potential growth in exports and revenue can be realised if actions are taken to overcome supply bottlenecks. Other problems include insufficient supporting industries (particularly insufficient supplies of raw materials), limited access to market and information, need for further skills training and education, inadequate capacity and quality standards, restricted access to finance, and an absence of intellectual property rights.

The food processing industry in Lao PDR is still in its early stages, with few large companies. The potential for export and employment growth is estimated to be large and small companies are likely to increase. Some products (e.g. coffee) are vulnerable to external shocks but these tend to hit mass producers rather than smaller ones that rely on niche demand.

In conclusion, the development trends and future outlooks of each of the three industries send a clear message that these selected industries show economic and human development potential. To realise these potentials, appropriate actions and measures from the involved parties are necessary.

The study “Addressing the Impacts of the Phasing out of Textiles and Clothing Quotas in Lao PDR” comprises findings published in four volumes:

- 1. Human Development Assessment in Post-Agreement on Textile and Clothing in Lao PDR**
- 2. Diversification and Value Addition,**
- 3. Assessment of the Trade and Industrial Policy Environment in Lao PDR**
- 4. Trade Negotiation Strategy**



For more information, please contact the National Statistics Centre (NSC), Luang Prabang Road, Vientiane Capital, Lao PDR: +856-21-214740, 242022, nscp@etllao.com www.nsc.gov.la