LAO PDR

Table 1	2020
Population, million	7.3
GDP, current US$ billion	18.1
GDP per capita, current US$	2479.5
National Official Poverty Rate[a]	18.3
International poverty rate ($1.9)[a]	10.0
Lower middle-income poverty rate ($3.2)[a]	37.4
Upper middle-income poverty rate ($5.5)[a]	38.8
School enrollment, primary (% gross)[b]	100.0
Life expectancy at birth, years[b]	67.9
Total GHG Emissions (mtCO2e)	39.8

Source: WDI, Macro Poverty Outlook, and official data.
(a) National Statistics Office. Most recent value (2018).
(b) Most recent WDI value (2019).

A new wave of COVID-19 cases is jeopardizing the economic recovery. GDP growth is forecast to reach 2.2 percent in 2021, as containment measures disrupt business activities. Income losses and rising inflation are negatively affecting living standards, while limited fiscal space has constrained the capacity to respond to shocks. Macroeconomic instability, fueled by a growing public debt burden, is also a key risk to the outlook. Structural reforms are needed to support a more inclusive growth pattern.

Key conditions and challenges

Over the past two decades, economic growth has been predominantly driven by large-scale investments in capital-intensive sectors – particularly mining and hydropower. However, these investments have failed to support sufficient job creation and have entailed considerable environmental costs. Moreover, public investment in the power sector has been mostly financed by external debt – often on commercial terms – gradually jeopardizing macroeconomic stability. The weak financial position of the power utility SOE compounds these concerns through its contingent liabilities. Meanwhile, revenue collection has been deteriorating – exacerbated by the pandemic. Despite reform efforts, fiscal and current account imbalances persist, partly due to growing public debt service. Coupled with limited reserve buffers, these imbalances are increasing depreciation pressures on the kip and widening the spread in the parallel market. Nonetheless, the country can leverage its strategic location and abundant natural capital to build back better. In order to sustainably accelerate economic growth, new greener and more inclusive sources of growth need to be found.

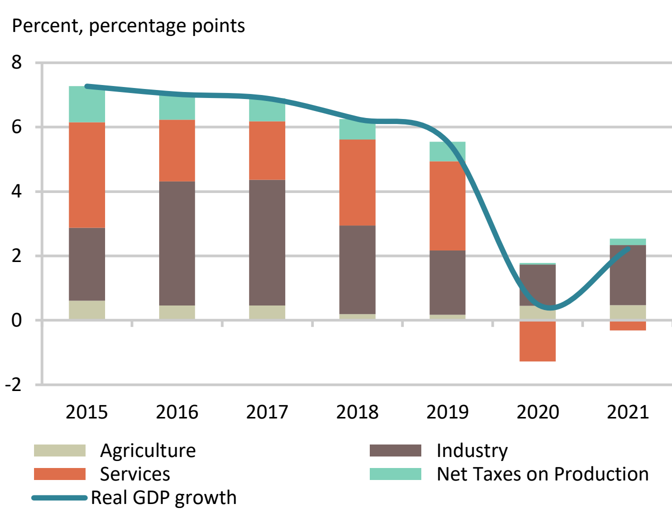
The COVID-19 pandemic and macroeconomic instability are the main risks to the outlook. A prolonged wave of COVID-19 infections will likely require extended containment measures to avert a significant loss of lives. These measures could then result in further job and livelihood losses, especially if not complemented by adequate policy responses to support households and businesses. In turn, this would amplify existing structural vulnerabilities. Low revenue collection, a growing debt service, heightened financial risks, and insufficient foreign exchange earnings will test the resilience of the economy.

Recent developments

Reported cases of COVID-19 increased in April-May 2021, triggering the implementation of strict containment measures. However, cases have risen considerably since July. Recent evidence of community transmission led the authorities to reintroduce some public health measures. While the vaccination rate has risen steadily – with 40 percent of adults fully vaccinated as of September 2021 – it remains significantly below the levels needed to avoid significant local outbreaks.

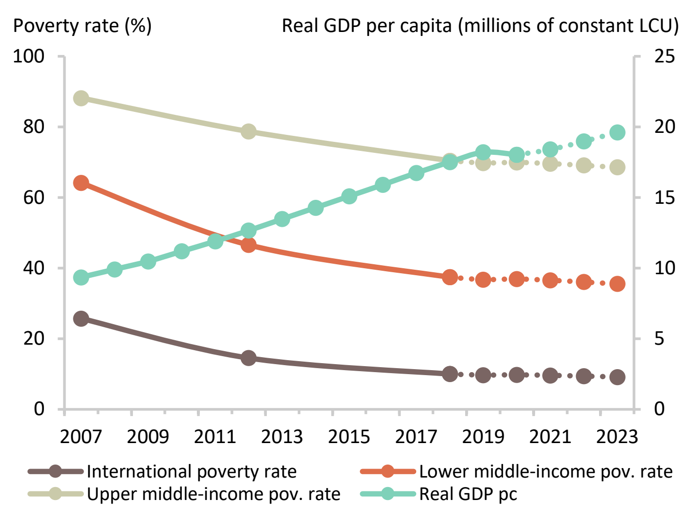
Fiscal revenue performance showed some signs of recovery in the first half of 2021, while public spending was broadly stable when compared to the same period in 2020. However, fiscal space remains limited, which restricts the ability to provide relief to affected businesses and households. Efforts to increase revenue collection and curtail non-essential spending are essential. Total public and publicly guaranteed (PPG) debt has reached critical levels – at about 72 percent of GDP in 2020. The share of non-concessional debt

FIGURE 1 Lao PDR / Real GDP growth and contributions to real GDP growth



Sources: Lao Statistics Bureau and World Bank staff estimates.

FIGURE 2 Lao PDR / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

has increased to almost 40 percent of total external PPG debt, with a considerable impact on debt service – due to higher interest rates and shorter maturities. Debt rescheduling has eased immediate debt service pressures, but further measures are required to secure debt sustainability.

Trade performance was relatively solid in January-July 2021. Merchandise exports grew by 38 percent, supported by agricultural and industrial output. Imports rose by 27 percent in the same period, driven by electrical machinery and equipment. Despite an improved merchandise trade performance, service exports lagged due to international travel restrictions. Current account imbalances remain a concern, partly owing to rising debt service payments and lower workers' remittances. Net foreign reserves are low, covering only 2 months of imports. High demand for foreign exchange – especially to service external debt – coupled with limited reserve buffers has contributed to widen the spread between the official and parallel exchange rates – currently at about 20 percent for the US dollar. This is the highest level on record.

A second and larger wave of COVID-19 cases has had a significant impact on employment levels. After rebounding to pre-pandemic levels in the first quarter of 2021, employment dropped by almost half in May 2021 amid lockdown measures. About 50 percent of households experienced a reduction in incomes when compared to the same period last year. Gradually increasing food prices are eroding consumer purchasing power, threatening food security – especially of the poor. Lower employment levels and rising consumer prices – partly owing to a weaker local currency – have weighed negatively on poverty reduction.

Outlook

GDP growth is projected to rebound to 2.2 percent in 2021, from 0.5 percent in 2020. This forecast has been revised downwards from the 4 percent growth projected in March 2021 due to the recent outbreak. The agriculture and industry sectors are expected to drive growth, supported by external demand – as key trading partners gradually recover. However, the sluggish recovery of services is expected to weigh on growth. The economy is expected to gradually recover in the medium-term, but growth will remain below pre-pandemic levels in 2022 reflecting the impact of both cyclical and structural factors on the economic outlook.

Total public external debt payments due are projected to average $1.3 billion a year over 2022-25, which is about half of expected domestic revenues. Hence, meeting debt service obligations will become increasingly challenging, and may lead to debt distress in the absence of significant debt restructuring and limits on new commercial borrowing. Financing options are limited, both domestically and abroad. Sovereign credit downgrades in 2020-21 and several unsuccessful attempts to issue bonds in international markets are a case in point. Foreign currency reserves are expected to remain inadequate in the absence of structural reforms to boost export performance.

Compared to a non-COVID-19 scenario, poverty is expected to increase by 2.5 percentage points in 2021 – as measured by the $3.2-a-day international poverty line. Extended lockdown measures may result in permanent job and livelihood losses, especially when response measures have been limited and do not target the most vulnerable population. Rising food prices further undermine recent achievements in poverty reduction.

The main risks to the outlook include a prolonged wave of COVID-19 cases, a deterioration of fiscal deficits and debt levels, growing current account imbalances, and a slower-than-projected recovery in key trading partners. It is key to accelerate COVID-19 vaccination rates to stem community transmission, and thus avoid the need for extended lockdown measures that undermine economic activity. Debt discussions with the largest creditors (namely, China) are vital to alleviate debt service pressures. Moreover, accelerating reforms in key state-owned enterprises – in the electricity, aviation and banking sectors – is crucial to reduce contingent liabilities and safeguard fiscal and debt sustainability. Improving bank surveillance is important to address financial sector vulnerabilities. An improved business environment and trade facilitation reforms would be key to enhance the benefits from better regional connectivity, such as the Lao-China railway.

TABLE 2 Lao PDR / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020	2021 e	2022 f	2023 f
Real GDP growth, at constant market prices	6.3	5.5	0.5	2.2	4.5	4.8
Real GDP growth, at constant factor prices	6.3	5.5	0.5	2.2	4.5	4.8
Agriculture	1.3	1.2	3.2	3.3	4.0	4.2
Industry	7.8	5.6	3.6	5.1	4.3	4.3
Services	6.8	7.0	-3.2	-0.8	4.8	5.6
Inflation (Consumer Price Index)	2.0	3.3	5.1	5.0	5.3	5.5
Current Account Balance (% of GDP)	-11.5	-7.7	-2.4	-4.0	-5.7	-6.0
Fiscal Balance (% of GDP)	-4.7	-3.2	-5.2	-4.7	-4.2	-3.8
Debt (% of GDP)	57.2	58.4	64.4	65.1	65.4	65.0
Primary Balance (% of GDP)	-3.0	-1.5	-3.5	-2.6	-2.2	-1.9
International poverty rate ($1.9 in 2011 PPP)[a,b]	10.0	9.7	9.8	9.7	9.5	9.2
Lower middle-income poverty rate ($3.2 in 2011 PPP)[a,b]	37.4	36.8	36.9	36.8	36.3	35.7
Upper middle-income poverty rate ($5.5 in 2011 PPP)[a,b]	70.4	69.8	70.0	69.8	69.3	68.8
GHG emissions growth (mtCO2e)	-0.4	2.7	0.2	1.3	2.4	2.6
Energy related GHG emissions (% of total)	47.6	48.5	48.2	48.5	49.3	50.2

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.
Notes: e = estimate. f = forecast.

(a) Calculations based on EAPPOV harmonization, using 2012-LECS and 2018-LECS.Actual data: 2018. Nowcast: 2019-2020. Forecast are from 2021 to 2023.

(b) Projection using annualized elasticity (2012-2018) with pass-through = 0.7 based on GDP per capita in constant LCU.