

Lao PDR's Way into the ASEAN Single Market

The ASEAN Economic Community (AEC)

Towards the ASEAN Community: ASEAN has been founded in 1967, the ASEAN Free Trade Area has been established in 1992 and Lao PDR became a member in 1997. The ASEAN integration process intensified since 2003: at the 9th ASEAN Summit, ASEAN Member States (AMS) decided to establish the ASEAN community, which includes the ASEAN Economic Community (AEC), the ASEAN Political-Security Community (ASPSC), and the ASEAN Socio-Cultural Community (ASCC).

The ASEAN Economic Community (AEC): The AEC will be established in 2015. The ASEAN Leaders adopted the AEC Blueprint at the 13th ASEAN Summit in 2007 in Singapore, to serve as a coherent master plan guiding the establishment of the AEC. The AEC Blueprint 2015 envisions four pillars for economic integration:

1. A Single Market and Production Base: the 1st Pillar of the AEC Blueprint foresees five freedoms, namely free flow of goods; free flow of services; free flow of investment; freer flow of capital; and free flow of skilled labour.

2. A Competitive Economic Region: the 2nd Pillar addresses the need to improve ASEAN competitiveness. It envisions a harmonization of policies in the field of competition policy, consumer protection, intellectual property rights, taxation and e-commerce; and better cooperation on infrastructure development (including transportation, energy cooperation and mining cooperation).

3. Equitable Economic Development: The 3rd pillar aims to reduce inequalities between and within ASEAN countries; a key focus is put on SME Development. The Initiative for ASEAN Integration (IAI) supports Cambodia, Laos, Myanmar and Vietnam (CLMV) in catching up with ASEAN-6.

4. Integration into the Global Economy: The 4th pillar seeks to enable ASEAN businesses to compete internationally, participate in global supply chains and attract foreign investment from outside the region; e.g. through 'ASEAN-plus' agreements.



Left to right: Trade in goods at Lao-Thai border; Workshop on AEC Integration in Lao PDR

'AEC 2015' – what does it mean?

The year 2015 marks the formal establishment of the AEC. 'Launching the AEC' is a major milestone that will allow ASEAN to foster a common identity and create momentum for further economic integration, relying on strong regional frameworks. Declaring the AEC operational, however, is not the final culmination of the ASEAN economic integration process: ASEAN integration is an on-going, dynamic process that will continue beyond 2015, as emphasized in the new AEC Blueprint 2025.

Progress and Achievements in the Implementation of the AEC

ASEAN has endorsed 3 main agreements in order to create the Single Market: the ASEAN Trade in Goods Agreement (ATIGA) in 2010, the ASEAN Framework Agreement on Services (AFAS) in 1995, and the ASEAN Comprehensive Investment Agreement (ACIA) in 2012. Under ATIGA, tariffs have been reduced to 0-5% for 96% of products in ASEAN. Under AFAS, ASEAN Member States (AMS) liberalised services trade and allow for up to 70% of foreign equity investment in most services sectors. Finally, with ACIA, ASEAN countries adopted a modern investment agreement, that eases investment restrictions in most sectors, grants investor protection and provides dispute settlement mechanisms.

Progress has also been achieved in the other pillars: A total of 9 AMS – including Lao PDR – have a Competition Law and a Competition Authority in place; 9 AMS also have a Consumer Protection Law. Comprehensive infrastructure agreements have been reached, e.g. to liberalise air transport services in ASEAN, to create an ASEAN highway network and a Singapore-Kunming Railway Link, and to establish an ASEAN joint power grid.

ASEAN concluded 6 Free Trade Agreements (FTAs) with key global trading partners: China, Korea, Japan, India, Australia and New Zealand, and Hong Kong. The Regional Comprehensive Economic Partnership (RCEP) is still under negotiation.

What the AEC means for Lao PDR

Creating economic opportunities: By joining the AEC, Lao PDR will become better integrated into regional value chains. The AEC allows Lao PDR to attract investment to modernize the economy, to gain access to technology and create competitive conditions in the private sector. For Lao companies, the AEC offers the potential to overcome the tightness of the domestic market through exporting and exploiting business opportunities abroad. Trade with perishable goods will be enabled through better transport linkages; access to seaports improves the connection to international markets.

Facing competitive pressure: Benefits from the ASEAN economic integration will not arise automatically for Lao PDR. The economy will face increased competition in almost all sectors. Lao companies will need to adapt, to modernize and to become more efficient and productive in order to compete with stronger producers from the region.

Strengthening domestic institutions, human capacity and the business environment: For the Lao government, the AEC integration process provides a unique opportunity to amend Lao law to comply with ASEAN requirements; and to adopt legislation and regulation that follows regional and global best practices. Taking into account the time and effort needed to create a modern business environment and put in place the necessary infrastructure, CLMV countries have been granted special treatment, technical support and flexibilities within the implementation of the AEC.

Completing the AEC Agenda

Challenges in the implementation of the AEC: ASEAN countries are very heterogeneous in their economic structure and level of development. This is linked to imbalances in regulatory and institutional capacity to actively steer and navigate the integration process. There is a need for more political support in some countries, while stronger institutions and more resources are required in other countries. ASEAN also faces the challenge to more effectively engage private sector and civil society stakeholders.

The way forward for ASEAN: ASEAN countries agreed to fast track the implementation of prioritised AEC deliverables in 2015 and 2016. In addition, ASEAN has finalized the AEC's post-2015 agenda for deeper regional economic integration. The AEC Blueprint 2025 builds on previous achievements and experiences and envisions a more highly integrated and cohesive, more competitive and better-connected ASEAN

Key priorities for Lao PDR: Implementation of measures is still a challenge for Lao PDR. Lack of resources, staff and capacity has slowed down the regulatory and legislative process. Communication and outreach is a challenge as in most ASEAN countries: availability and access to information on AEC is suboptimal, key messages to specific audiences on the national and regional level still need to be developed. And finally, the Lao private sector needs to be supported to make use of the opportunities of the AEC.

ASEAN and Lao PDR – An Overview

Indicator	ASEAN	Lao PDR
Population	622 million	6.5 million
GDP	US\$2.57 trillion (2014)	US\$11.7 billion (2014)
GDP Growth	4.6% (2014)	7.5% (2014)
GDP per capita	US\$4,131 (2014)	US\$1,707 (2014)
Total Trade	US\$2.53 trillion (2014)	US\$5.4 billion (2014)
- Intra-ASEAN Trade	US\$608 billion	US\$3.7 billion
- Intra-ASEAN share in total exports, in %	25.51%	54.98%
- Intra-ASEAN share in total imports, in %	22.54%	74.39%
Total FDI	US\$136.2 billion (2014)	US\$0.9 billion (2014)
- Intra-ASEAN share in total FDI, in %	17.9%	15.1%
Tourist Arrivals	105 million (2014)	4.1 million (2014)
- Share of Intra-ASEAN tourists in total tourist arrivals	46.8%	77.5%

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Free Flow of Goods in the ASEAN Single Market

Lao PDR's Way into the ASEAN Economic Community (AEC)

Trade in Goods is the foundation of the AEC

Trade in Goods is a success story in ASEAN. In 2014, ASEAN countries in total exported goods worth US\$1.3 trillion and imported goods for US\$ 1.2 trillion. Intra-ASEAN trade has been growing and accounted for 25% of exports and 22.5% of imports. Lao PDR exported goods worth US\$2.6 billion in 2013 (55% to ASEAN countries) and imported around US\$2.7 billion (74% intra-ASEAN). Main trading partners for Lao PDR are Thailand, China and Vietnam. Main exported goods in 2014 are mining products and industrial products, followed by electricity, agricultural products and wood products. Lao PDR imports mostly construction goods, vehicles, fuel, electricity equipment and industrial inputs.

Free Flow of Goods is a key feature of the 'Single Market and Production Base', the main pillar of the upcoming AEC. Negotiations and implementation towards the Free Flow of Goods are governed by the ASEAN Trade in Goods Agreement (ATIGA), signed by ASEAN Member States (AMS) on 26th February 2009. ATIGA incorporates and unifies previous trade in goods agreements, in particular the Common Effective Preferential Tariff Scheme (CEPT) of the ASEAN Free Trade Area (AFTA), signed in 1992. CEPT focused on tariff elimination, while ATIGA goes beyond tariffs to also cover new elements, including removal of non-tariff barriers and trade facilitation.

The comprehensive agenda of ATIGA: Tariff reduction, elimination of NTBs, trade facilitation and customs integration

Elimination of tariffs: ASEAN-6 countries already eliminated virtually all tariffs (99.2% of tariff lines); CLMV countries reduced 90.85% of tariff lines to 0-5%. Lao PDR has reduced tariffs to 0-5% for 99.09% of total products; for 89.31% of products the tariff is already 0% and only 265 tariff lines remain at 1-5%. Countries may retain a limited number of products on an exclusion list.

Elimination of Non-Tariff Barriers (NTBs): ASEAN adopted a comprehensive Non-Tariff Measures (NTMs) work programme on the national and regional level. NTMs are regulatory policies, procedures or administrative requirements, intended to serve a domestic policy objective (e.g. health protection). Such measures become barriers to trade (NTBs) when they specifically discriminate against imports, or when not applied uniformly. AMS are required to notify their NTMs to the ASEAN Secretariat for review. If NTMs are found to be NTBs, they ought to be eliminated.

Rules of origin (ROO): Rules of origin are necessary to define, whether a product is eligible for ASEAN preferential tariffs (i.e. duty-free in most cases). ASEAN ROOs are fulfilled if at least 40% of a product's value content originates from the ASEAN region. The fulfilment of ROO criteria is determined prior to customs clearance through the ATIGA 'Form D', filled by the exporter. ASEAN ROOs are regularly adjusted to make them as liberal and simple as possible. A new initiative to facilitate dealing with ROOs is the self-certification scheme: it allows exporters, who can demonstrate their track record of ROO compliance, to become "authorized economic operators" and self-certify the originating status of goods without having to apply through ATIGA Form D.

Trade facilitation: Trade facilitation aims at simplifying and harmonising custom procedures, streamlining product standards, ensuring transparency, as well as providing transport and logistics services, in order to reduce trade costs. ASEAN launched a multitude of initiatives in this area, as discussed below.

The **ASEAN Trade Repository (ATR)** will provide information on on preferential tariff rates, ROOs, NTBs, as well as national trade and customs laws and rules and documentary requirements. Lao PDR established the Lao Trade Portal website which will serve as the National Trade Repository, to be linked with the ATR.

Customs integration: Customs integration and modernisation is the heart of trade facilitation reforms in ASEAN. AMS implement-



Trade in Goods at the Lao-Thai Friendship Bridge

ed the ASEAN Harmonized Tariff Nomenclature (AHTN). Customs procedures are step by step harmonized with international conventions and standards and unified within ASEAN, for example through the ASEAN Customs Valuation Guide, the ASEAN Cargo Processing Model and the Customs Post Clearance Audit Manual. Simplifying, harmonising and standardising customs procedures and introducing ICT applications across AMS will facilitate the establishment of the ASEAN Single Window.

ASEAN Single Window (ASW): The ASW is an initiative to provide an integrated platform between government agencies and end-users (economic operators) to expedite cargo clearance and release in the AEC. The ASW seeks to connect and integrate National Single Windows (NSW). NSWs require a single submission of export information and a single decision-making process for customs clearance of cargo – hence accelerate processing times and increase transparency. The ASW will ensure compatibility and transparency of customs clearance in ASEAN and automatic exchange of documents and data. NSWs have been established in ASEAN-6; Lao PDR is in the process of developing its NSW.

Standards and Conformity Assessments: Standards and technical regulations (and their respective conformity assessments) are necessary to ensure quality, safety and transparency for the consumer. However, standards may create barriers to trade if they hinder market access of foreign products or require additional conformity assessments in each country. ASEAN intends to achieve harmonization of standards by aligning its standards and regulations with international standards. AMS concluded framework agreements on single regulatory regimes for cosmetics, electrical and electronic equipment (EEE) and medical devices. Mutual Recognition Arrangements (MRAs) of conformity assessments were completed for pharmaceuticals and EEE.

Implementation of ATIGA is progressing, but more effort from Member States is needed in the fields of NTBs and customs integration

Currently, tariff elimination is one of the biggest success areas of ASEAN. Tariffs have been virtually eliminated for ASEAN-6 countries and CLMV countries will do so by 2018. Some countries still face internal difficulties to eliminate tariffs for e.g. tobacco,

petroleum, alcohol, sugar and rice. Use of preferential tariffs is low in some cases (particularly where the difference between ASEAN and other tariffs is small) due to overly complicated ROO.

Implementation challenges remain, particularly regarding the elimination of NTBs, customs modernisation and the ASEAN Single Window. Lack of common definitions and approaches, institutional capacity and political will slowed down the process to eliminate discriminatory and diverse product standards, regulations and procedures. Customs reform and the introduction of modern ICT will need to be an on-going process at both the national and regional level.

Impact and Implications of the Free Flow of Goods in ASEAN – and Lao PDR

ASEAN Trade in Goods flows in and out of the region have been increasing. Progress with trade liberalisation significantly lowered trade costs in ASEAN and contributed to increased trade flows within ASEAN, but also with third-party countries. Trade within ASEAN is increasingly intra-industry trade in intermediate goods with ASEAN moving towards the “single production base”. ATIGA contributed towards making ASEAN’s manufacturing sectors more efficient and competitive and facilitated the integration of the region in global value chains.

For Lao PDR, there are both opportunities and challenges associated with the Free Flow of Goods. Little rigorous research exists with respect to the impact of Free Flow of Goods on Lao PDR – mostly due to a lack of data. However, tariff elimination means that imports are more readily available and prices have been decreasing. Foreign investment in infrastructure has been increasing in expectation of increased trade flows to and through Lao PDR. Lower overall trade costs also incentivize international manufacturers to establish production plants in Lao PDR, to make use of lower labour and energy costs, while also being able to export products easily to the region. On the other hand, certain un-competitive sectors in Lao PDR stand to lose from the Free Flow of Goods in ASEAN as their products cannot compete with cheaper and higher quality production in other AMS – which can now be cheaply imported into Lao PDR.

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Free Flow of Services in the ASEAN Single Market

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Liberalisation of Trade in Services in ASEAN is a potential engine of growth.

In ASEAN Member States (AMS), services account for 40% to 75% of GDP and the sector keeps growing. In Lao PDR, the services sector makes up 40% of GDP and employs around 22% of the workforce (2013). Services include transport, distribution and tourism sectors, but also smaller segments such as business or health services. In all AMS, services contribute more to GDP growth than manufacturing – which underlines the importance of the services sector as an engine for economic diversification and development in ASEAN and in Lao PDR. A well-developed services sector can shield the economy from global recessions that rapidly affect manufacturing and resource exploitation activities.

ASEAN countries are increasingly specialising in services exports. Singapore exports financial services, Cambodia tourism, and Malaysia education services. ASEAN services exports amount to US\$305 billion in 2014. Intra-ASEAN services exports expanded by 17% per year in the past decade (reaching US\$54 billion or 18% of total ASEAN services exports in 2014). ASEAN services trade will continue to expand with the removal of barriers to the various modes of supply (see Box 1). Lao PDR's services exports have been growing by on average 33% per year since 2005; Lao PDR exported commercial services worth US\$764 million in 2014 (travel services alone accounted for three quarters of it).

Opportunities for Lao PDR associated with the liberalisation of trade in services include:

- Increased investment in services sectors due to the removal of foreign ownership limitations (Mode 3 of service supply);
- Higher competitiveness of Lao manufacturing and agricultural enterprises due to access to high-quality services, e.g. in the areas of logistics, legal, accountancy, or ICT services;
- Economic opportunities to specialize in intermediate services, and export services such as electricity, transportation, or business services to production facilities in other AMS.

'Free Flow of Services' is negotiated under the ASEAN Framework Agreement on Services.

The ASEAN Economic Community (AEC) will create a Single Market and Production Base by the end of 2015. Free Flow of Services is one of the key features of the Single Market. Services liberalisation is negotiated under the ASEAN Framework Agreement on Services (AFAS). AFAS has been concluded in 1995 to reduce or eliminate restrictions on providing services and establishing a commercial presence for service suppliers across the region. AMS have been progressively enhancing Market Access and guaranteeing National Treatment for services suppliers from other ASEAN countries in the four modes of supply.

Box 1. How to trade in services in the AEC ?

Modes of supply

Mode 1: Cross-border supply via telecommunications infrastructure, mail, transport services, call centres, among others.

Mode 2: Consumption abroad through citizens travelling abroad to consume for example tourism, healthcare, or education services, provided by foreign suppliers.

Mode 3: Commercial presence of the foreign services provider, through which it supplies services (foreign investment).

Mode 4: Temporary physical movement of natural persons across borders to supply a service in the other country.

What will be liberalised ?

ASEAN countries will gradually allow foreign services providers to supply services through Mode 1, 2 and 3. At the moment, liberalisation of Mode 4 is modest and mostly takes place through Mutual Recognition Arrangements (see below).

Market Access and National Treatment

For each Mode of Supply in each sector, ASEAN countries will remove restrictions to Market Access and National Treatment.

Market Access (MA): allowing foreign providers to enter and supply services in the domestic market.

National Treatment (NT): promising to regulate, tax, license, (etc.) foreign providers the same way as domestic suppliers.



Financial and legal services companies in Vientiane, Lao PDR

The AEC Blueprint 2015 sets clear targets, milestones and timelines, as well as pre-agreed flexibilities to achieve the Free Flow of Services. Within these flexibilities, Mode 1, 2 and 3 of services supply will be fully liberalised. For Mode 3, limitations to foreign equity investment will raise to a minimum of 70%. Mutual Recognition Arrangements (MRAs) have been concluded for 8 professions. They constitute an important step towards free movement of skilled labour and liberalisation of Mode 4 (see Box 2).

Achievements and challenges: Negotiations delivered promising results, but implementation of liberalisation commitments is slow.

AMS have recognized the important role that Trade in Services will play in future economic development. Until today, ASEAN countries concluded 9 rounds of services liberalisation negotiations and 8 MRAs, as well as 4 packages of commitments on financial services and 5 packages on air transport services. Lao PDR currently has commitments in place for 92 out of 128 services sectors, just slightly behind schedule. Implementation of commitments and some of the MRAs are underway in most AMS.

Liberalisation of Trade in Services in ASEAN is only at the beginning. Most AMS are currently struggling to make more commitments even within the limited scope of liberalisation envisioned by the AEC Blueprint 2015 (e.g. 70% foreign equity limit, as opposed to 100% for investment in manufacturing or agriculture, under the ASEAN Comprehensive Investment Agreement). The

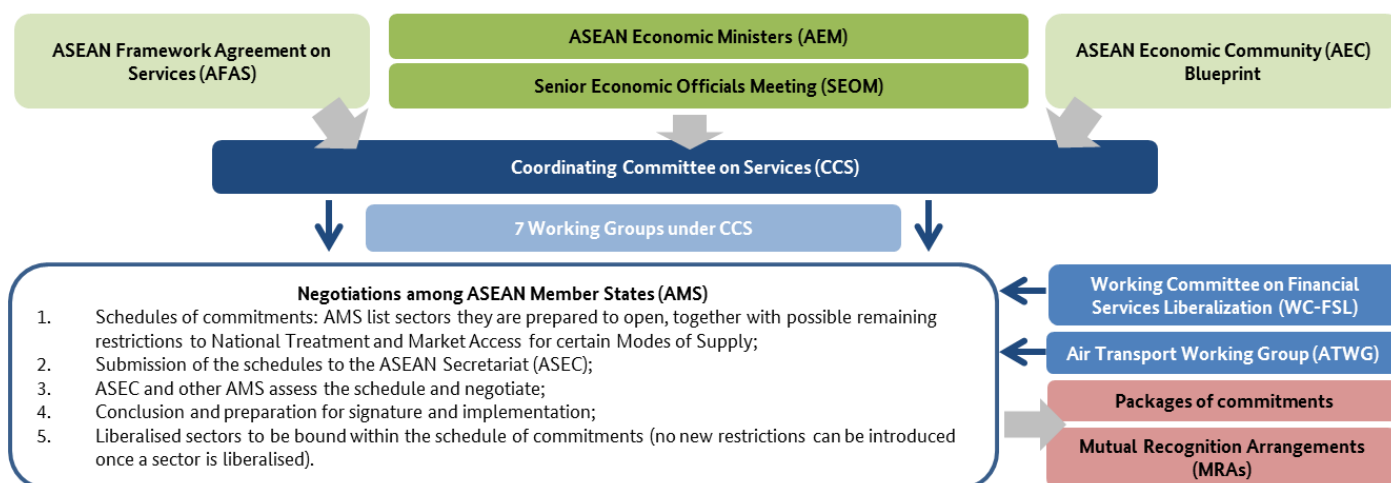
10th and final AFAS package of commitments has been delayed to 2016. In addition, implementation of commitments is lacking behind and will require considerably more time. At the national level, coordination between line ministries is a challenge.

Negotiations will continue under the future ASEAN Trade in Services Agreement (ATISA). The new AEC Blueprint 2025 confirms the commitment to 'broaden and deepen services integration within ASEAN'. It mandates the negotiations and implementation of ATISA as the legal instrument for further integration and calls for a review of existing flexibilities, limitations, and carve-outs. However, the Blueprint 2025 remains vague and so far lacks the targets and timelines necessary to achieve progress. Services liberalisation will need to become more ambitious to truly create a "single market" for services in ASEAN – and to secure business opportunities and sustain economic growth.

Box 2. Mutual Recognition Arrangements (MRAs)
MRAs enable services providers that are certified or registered by relevant domestic authorities to be mutually recognized by signatory AMS. MRAs for the following 8 professions have been signed and ratified by ASEAN countries:

1. Engineers	5. Nurses
2. Surveyors	6. Medical professionals
3. Architects	7. Dental professionals
4. Accountants	8. Tourism professionals

Towards 'Free Flow of Services': Legal Framework and Negotiation Process to Liberalise Trade in Services in ASEAN



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Free Flow of Investment in the ASEAN Single Market

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Foreign investment in ASEAN and Lao PDR is increasing, notably intra-ASEAN investment

Foreign Direct Investment (FDI) in ASEAN has increased from US\$21.8 billion in 2000 to US\$136.2 billion in 2014. In 2014, US\$111.8 billion in FDI came from third-party countries, while US\$24.4 billion (or 17.9% of total FDI) were intra-ASEAN investment. Intra-ASEAN FDI flows increased considerably over the past 15 years, up from only US\$1.22 billion in 2000.

Lao PDR attracted US\$900 million in foreign investment in 2014; 15% of it came from other ASEAN Member States (AMS). FDI inflows to Lao PDR have been increasing, albeit from very low levels. For the moment, Lao PDR is attracting FDI mostly in electricity generation and mining, with Chinese companies being the main source of FDI. Chinese investment goes into hydropower, mining and real estate while Intra-ASEAN investors (mostly Thai and Vietnamese) target forestry and agriculture (e.g. timber and rubber). Chinese, Thai and Vietnamese investment accounted for more than three quarters of total FDI between 2001 and 2011.

The ASEAN Comprehensive Investment Agreement (ACIA) guides ASEAN Member States in their reform of investment regimes

The 2007 ASEAN Summit affirmed the commitment of ASEAN countries to establish the ASEAN Economic Community (AEC) by 2015. The AEC Blueprint 2015 defines a liberal, facilitative, transparent and competitive investment environment as integral aspect of the ASEAN Single Market and Production Base.

The ASEAN Comprehensive Investment Agreement (ACIA), adopted in 2012, guides the implementation of a free and open investment regime in AMS. The ACIA revised, improved and consequently supersedes two previous ASEAN investment agree-

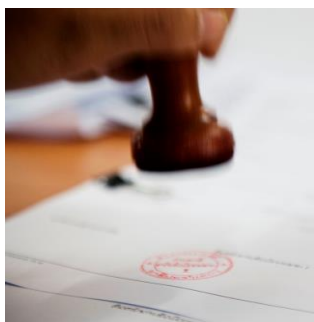
ments, namely the 1998 Framework Agreement on the ASEAN Investment Area (AIA) and the 1987 ASEAN Investment Guarantee Agreement. Implementation of the ACIA is overseen by the ASEAN Investment Area (AIA) Council, constituted of the 10 Economic Ministers. The Coordinating Committee on Investment (CCI) serves as a forum for information exchange and discussion.

The legal framework: What the ACIA offers for ASEAN and ASEAN-based investors

The ACIA is a modern investment treaty and matches international best practices in terms of scope, rights and obligations. The ACIA covers all types of investment in the sectors manufacturing, agriculture, fishery, mining and quarrying, as well as services incidental to these sectors. The ACIA applies to ASEAN investors, as well as 3rd country investors that own or control an ASEAN-based legal entity. Thematically, the ACIA has 4 pillars: investment liberalisation, facilitation, promotion and protection.

1. Liberalisation: ACIA seeks progressive liberalisation of investment regimes. This includes according preferential treatment to ASEAN-based investors and no back-tracking of commitments. Investors are guaranteed national treatment and free choice of senior management and board of directors (SMBD); except for sectors currently on the single reservation list (the 'ACIA Schedule'). AMS will continuously eliminate restrictions to entry and other restrictive measures, e.g. performance requirements.

2. Facilitation: AMS agreed to jointly work towards more transparent, consistent and harmonized investment policies, regulations, and procedures in ASEAN. Work towards this end includes among others the simplification of procedures for investment applications and approvals; the creation of one-stop shops for investors; and improving consultation with the private sector.



Foreign
Investment
in Lao PDR

3. Promotion: AMS seek to promote the region as an integrated investment area and production network to both intra- and extra-ASEAN investors. This includes for example promoting investments from ASEAN-6 to CLMV; or conducting joint investment missions that focus on regional clusters and production networks. AMS also created a network of bilateral double taxation treaties.

4. Protection: ACIA guarantees certain protections to all investors and their investments, in all sectors, including services sectors. Measures towards this end include fair and equitable treatment; free transfer and repatriation of funds, capital, profits, and dividends; transparent coverage of expropriation and compensation; and compensation for losses resulting from strife. ACIA also provides for investor-state dispute settlement mechanisms.

Implementation of the ACIA requires significant policy reform in Member States

The ACIA features a built-in agenda for continuous liberalisation and facilitation which countries will need to realize at the national level. AMS are required to continuously reduce investment impediments (measures that do not conform to national treatment or SMBD obligations) which are listed in the ACIA Schedule; and are not allowed to add new items to the list. AMS agreed to conduct regular Investment Peer Reviews and to report any changes in laws, regulations, or administrative guidelines to the ASEAN Secretariat. Only if all AMS ensure implementation, ASEAN investors and ASEAN-based foreign investors will be able to take full advantage of the opportunities that ACIA provides.

In Lao PDR, multiple reform requirements of the ACIA have been implemented with the 2009 revision of the Investment Promotion Law (IPL). A new revision of the IPL (expected in 2016) will be used to further eliminate discriminatory measures and improve protection provisions, as foreseen in the ACIA. A one-stop-shop for investors has been developed but is operational only to a limited extent. A Law on Special Economic Zones (SEZ) is to be discussed by the National Assembly in 2015, aiming at attracting quality investments in SEZs.

Lao PDR has some leeway to reduce non-conforming measures on its ACIA Schedule. For example, multiple sectors of agriculture, forestry and mining are still reserved for Lao nationals. For other sectors, foreign investors need to obtain special licenses depending on the amount of the investment. Land ownership is

limited to Lao nationals and foreign investors with registered capital above US\$500,000. For joint-ventures, Lao PDR requires a minimum foreign equity input of 30% of the total or US\$100,000.

Future prospects of attracting and liberalising investment in ASEAN and Lao PDR

ASEAN will continue to attract FDI, thanks to the strong economic outlook of the regional bloc and the established value chains in multiple industries. Several AMS are among the top destinations globally for foreign investors due to strong economic growth, large and increasingly wealthy populations, as well as political and economic stability. Intra-ASEAN investments are increasing, reflecting regional production networks. Nevertheless, to ensure future investment, AMS will need to invest in infrastructure, skilled workers, and innovative capabilities; and support the creation of agglomerations with suppliers, producers, and support services.

Lao PDR will need a clear investment strategy to receive its share of the cake. Distribution of FDI within ASEAN is very unequal. Singapore alone receives 50% of ASEAN investment inflows; and Singapore, Indonesia, Thailand and Malaysia together account for 75-85% of ASEAN FDI. For Lao PDR this means that it will need to focus on attracting intra-ASEAN investment from foreign investors that have a primary presence in another AMS. A promising trend has been a shift of labour intensive and low-skilled segments of production processes from Thailand to Lao PDR. Lao PDR may find its place in regional value chains by leveraging lower labour, land and energy costs while also offering geographic proximity and language and cultural similarity. Nevertheless, and beyond ACIA, Lao PDR will need to keep improving the overall trade and business environment. Reduction of barriers to trade, as well as a competitive business climate, offer guarantees to investors that they will see returns on their investment.

The ACIA will remain the key instrument to maintain investment attractiveness of ASEAN but it would benefit from improvements to its institutional approach. For the moment, ACIA does not sufficiently address issues such as performance requirements, restrictions on capital movements, and constraints on labour movements; and it does not cover services sectors. Investment in services is negotiated under the ASEAN Framework Agreement on Services (AFAS) – however, some way of coordination between the two agreements needs to be found.

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The Lao Private Sector in the ASEAN Economic Community (AEC)

What the Single Market means for business in Lao PDR

Strong economic growth, ASEAN economic integration and regulatory reforms have set the Lao private sector on a path to modernity

The private sector is driving economic growth in Lao PDR, but output is dominated by natural resource exploitation. Lao PDR is the smallest economy in the ASEAN with a GDP of US\$11.8 billion (2014). For the last two decades, the Lao economy grew on average by 7% per year, reaching 8.5% growth in 2013. Economic output has been heavily dependent on e.g. mining and hydro-power, which also facilitated the growth of the services sector (particularly construction), but has not created the necessary jobs. Agriculture still accounts for 75% of employment; another 20% are absorbed by Small and Medium Sized Enterprises (SMEs).

The Lao private sector consists largely of SMEs with low levels of productivity. More than 99% of services and manufacturing companies in Lao PDR are SMEs that lack access to credit, skills and technology. Skills levels and labour productivity are significantly lower than in other ASEAN countries. Around 80% of Lao exports are natural resources (wood products, minerals); but the share of other exports is growing, e.g. coffee, fresh food, clothing and tourism. With increased foreign investment in production, a new generation of modern manufacturing companies, producing labour intensive goods and parts of goods, is now emerging.

ASEAN economic integration has been a driving force behind a move towards trade openness and economic reform. Lao PDR joined ASEAN in 1997 and the World Trade Organisation in 2013; the ASEAN Economic Community (AEC) will be established in 2015. In the process, Lao PDR has eased import barriers, reduced tariffs, and facilitated better access and credit for private firms. Reforms have made it easier to start a business and attract foreign investment. Political commitment to trade openness is high.

What does AEC mean for Lao businesses? More competition, more risk – and more opportunities for business expansion

The AEC brings risks and opportunities – but no alternatives. The AEC has been officially launched at the ASEAN Summit in November 2015. Based on the AEC Blueprint, the key features of the AEC include free flow of goods, services, investment and skilled labour, as well as freer flow of capital. Easier access for Lao goods and services to a much larger market and more affluent populations is a huge opportunity. However, Lao PDR's exports and investment inflows are not expected to instantly rise, due to supply side constraints and lack of competitiveness. Nevertheless, the AEC represents the most promising strategy for the Lao private sector to increase competitiveness, upgrade technology and skills, and access global value chains through the regional market.

Competition will increase inexorably for goods and services producers in Lao PDR. By 2018, Lao PDR will have eliminated import tariffs for 99% of products. ASEAN is also working towards simplifying and integrating customs procedures, improving transport connectivity and logistics networks. Imports from other ASEAN Member States (AMS), therefore, will become cheaper and may surge – thereby improving efficiency of firms that use imported materials and benefitting consumers of imports. Domestic producers, who compete with imported products, will face tougher competition. Liberalisation of Trade in Services has been slower; but producers in sectors such as transport, logistics, tourism, or business services will also see increased competition.

Investment flows to Lao PDR will continue to increase; particularly in resource and real estate sectors, and to some extent in manufacturing and services if conditions are right. In the AEC, countries will fully liberalise investment from ASEAN-based



Companies in Savan-Seno Special Economic Zone (SEZ), Savannakhet Province, Lao PDR

investors. For Lao PDR, this is an opportunity to attract more foreign investment in manufacturing; for example in Special Economic Zones (SEZs) where investors enjoy a large range of benefits and incentives. Lao private companies will be able to engage in joint ventures and other business activities (suppliers, distribution, transport and logistics) with foreign investors, benefiting from capital inflows, technology and knowledge transfers, as well as better export conditions. Since foreign investors in Lao PDR produce generally for export, the competition for local SMEs (that cater to the domestic market) is less of a concern. Benefits to foreign investors in Lao PDR accrue through low labour costs, low energy costs, political stability.

Professional and business services and skilled labour might become more easily available in Lao PDR. Lao PDR already raised the maximum foreign equity share in many services sectors to 70 or even 100%; making it easier for foreign providers to deliver services in Lao PDR. This is good news for Lao private companies whose competitiveness depends on the availability of high quality commercial services. In addition, ASEAN countries concluded 8 Mutual Recognition Arrangements (MRAs) which will facilitate the movement of highly skilled professionals – another desirable process given the shortage of skilled labour in Lao PDR. MRAs have been completed for engineers, surveyors, architects, nurses, medical practitioners, dental practitioners, accountants, and tourism professionals. Practical implementation is slow, however, and any impact will depend on efforts to streamline domestic laws and regulations, e.g. regarding work permits and visas.

How can Lao businesses prepare for the AEC? Invest in skills and quality; and understand the need to “think regionally”

Looking beyond Lao borders will be mandatory for business success. In the single market, business decisions are no longer based on geography. Entrepreneurs need to understand the economy and society of other ASEAN countries, to make informed decisions on exporting and sourcing potentials. Key skills in the Single Market include communication and networking (to build new supplier and distribution partnerships), market research, marketing and branding (to reach new consumer groups in other AMS), as well as logistics (to manoeuvre export and im-

port procedures). In the same way, the Lao private sector needs to be active in learning about the regulatory changes that the AEC brings; and providing inputs during regulatory consultations.

Upgrading into regional value chains requires quality improvements. The AEC provides an opportunity for more and more companies in Lao PDR to become part of regional or global value chains, thereby increasing value added, income and employment in Lao PDR. One opportunity is through joint ventures with foreign investors which may come with existing supplier and distribution networks, as well as customers. Another possibility is SMEs supplying to foreign producers in Lao PDR or neighbouring countries, e.g. services (construction, cleaning, transport and logistics, distribution) or inputs (raw materials or lightly processed goods). Integration into regional supply chains, however, requires the ability to meet and maintain quality standards, ensure reliable delivery, and upgrade management and accounting capacities.

Policy makers in Lao PDR will need to support businesses in addressing supply side constraints and creating a more conducive business environment. Key constraints to competitiveness include access to finance, better education and skills, trade facilitation and streamlining and simplifying regulatory procedures to decrease transaction costs. It will also be important to fully implement ASEAN agreements – and socialize legal changes to the private sector. ASEAN is a priority for the private sector – and the private sector should be a priority for policy makers.

The ASEAN Business Advisory Council (ASEAN-BAC) Private sector participation in ASEAN decision-making

ASEAN-BAC is the main voice of the private sector in ASEAN. The body consists of high-level CEOs from companies of the ASEAN region; including SME representatives. ASEAN-BAC advises ASEAN leaders on the implementation of the AEC, and also promotes awareness of the AEC among the private sector. ASEAN-BAC’s flagship event is the annual Business and Investment Summit that brings together the ASEAN business community, as well as political leaders of ASEAN Member States and partner countries. The prestigious ASEAN Business Awards (ABA) are also awarded once a year during the Summit.

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Lao SMEs in the ASEAN Single Market

How can Small and Medium-Sized Enterprises (SMEs) in Lao PDR benefit from the ASEAN Economic Community (AEC)?

SMEs in ASEAN and Lao PDR are driving economic growth but face significant productivity challenges.

SMEs are a driver of growth, employment creation and poverty reduction in ASEAN. SMEs account for more than 96% of all enterprises and 50%-85% of domestic employment in ASEAN countries. Their contribution to national GDP ranges from 30% to 53% and contribution to exports from 19% to 31%, depending on the country. SMEs are key stakeholders if ASEAN economic integration is to deliver benefits to communities and people.

Most companies in Lao PDR are SMEs but their output and productivity are still low. In Lao PDR, 99% of companies are SMEs (210,000 in 2010). Most SMEs are located in the central provinces, e.g. Vientiane and Savannaketh. SMEs in Lao PDR mostly cater to domestic markets in sectors such as wholesale and retail trade and motor repairing (64.5% of SMEs). Around 20% of SMEs are active in processing industries. While up to 75% of the population is still employed in agriculture, SMEs absorb the majority (approx. 80%) of the non-agricultural workforce. However, productivity of SMEs is low and their contribution to total domestic output is small, contributing around 16% of GDP (2010).

Lao SMEs will need to improve quality, comply with standards and participate in regional value chains in order to benefit from the AEC.

Establishing the AEC in 2015 will create a single market with 625 million consumers and a single production base with abundant resources and low manufacturing costs. Once fully implemented, free(r) flows of goods, services, investment and capital, as well as free movement of skilled workers across the region will make ASEAN more dynamic and competitive. ASEAN also aims at

streamlining domestic procedures, regulations, legislation and laws related to trade, investment, competition, consumer protection, intellectual property and infrastructure across ASEAN Member States (AMS). The AEC will have a significant impact on SMEs in ASEAN. The impact may be negative or positive, depending on a variety of factors such as economic sector, location, business strategy, and adaption and innovation capacity.

For Lao SMEs, the AEC brings some particular opportunities:

- Competitive Lao SMEs may expand their business by exporting their products, by serving new economic entities and sectors in Lao PDR, or by supplying to niche markets in ASEAN;
- Upgrading into regional supply chains will become easier through stronger linkages with better integrated neighbours;
- The AEC will help to attract investment for Lao SMEs, e.g. through joint ventures and access to capital markets;
- The AEC enables Lao SMEs to learn best practices and access technology and innovative practices through joint business undertakings with ASEAN companies;

However, the opportunities of the AEC stand against a set of challenges for Lao SMEs:

- Many products do not yet meet international standards and quality control remains a challenge;
- Limited capacity to absorb technology, increase productivity;
- Lack of skills and technical tools with respect to bookkeeping, market research, marketing, sales or customer care;
- Burdensome business regulations (Lao PDR ranks only 134th out of 189 countries in the Doing Business Index);
- No existing business linkages with large enterprises abroad.

Lao SMEs need to become active to overcome potential challenges now, in order to grasp the opportunities down the road.

The upcoming AEC should incentivize SMEs to improve quality of their products and services, in order to comply with regional and international standards. Lao SMEs also need to actively seek out



Motor vehicle repair and maintenance is a typical economic activity of Lao SMEs.

support to understand what the AEC means. Business networking or taking part in trade shows will allow SMEs to broaden their network of potential suppliers, customers, and business partners in the region. Becoming part of regional supply chains will require Lao SMEs to step out of their comfort zone and innovate.

AMS endorsed an ambitious agenda for SME promotion and integration in the AEC.

With the ASEAN Policy Blueprint for SME Development, ASEAN launched a number of support initiatives for SMEs. The ASEAN SME Agencies Working Group (SMEWG) is the ASEAN body responsible for SME development and promotion. First achievements include the development of the SME Services Centre Web Portal, the SME Guidebook towards AEC 2015, as well as the ASEAN Benchmark for SME Credit Rating Methodology. ASEAN also publishes Directories of outstanding and innovative SMEs. For policy makers in AMS, SMEWG has compiled reviews, best practices and guidelines for SME promotion. ASEAN holds multiple SME events such as SME Trade Fairs, or the ASEAN SME Showcase, which help SMEs to connect across the region.

More tangible results are needed. Many important deliverables in the field of SMEs such as a common curriculum for entrepreneurship or a regional SME development fund still remain to be realized. The new AEC Blueprint 2025 and the ASEAN Strategic Action Plan for SME Development 2015-2025 set 5 objectives for the coming period, namely: (i) promote productivity, technology and innovation; (ii) increase access to finance; (iii) enhance market access and internationalisation; (iv) enhance Policy and Regulatory Environment; and (v) promote entrepreneurship and human capital development.

‘Think regionally and act locally’ – the way forward for SME policy in Lao PDR.

The Lao government has taken some important steps to support SMEs in the AEC – however, much more needs to be done. SME policy is coordinated by the Department of Small and Medium Enterprise Promotion (DOSMEP), within the Ministry of Industry and Commerce. DOSMEP established a pool of 25 Business Development Service Providers (BDSP) in 2012. DOSMEP will support capacity development for BDSPs so that in the future they

will not only offer technical assistance on general SME development but also on ASEAN-related matters (such as competitiveness, market access and standards). An ASEAN service centre could help Lao SMEs to understand procedural changes that result from the AEC, as well as ways to indirectly or directly access the ASEAN Single Market.

Improving the domestic business environment will be key to see benefits materialize for Lao SMEs. Lao PDR needs to adjust and streamline procedures, rules and regulations that affect SME business undertakings. This includes for example simplifying the system for issuing Certificates of Origin (CO) (necessary to enjoy ASEAN preferential tariffs when exporting) in many sectors. Access to finance continues to be a major stumbling block in Lao PDR. SMEs will also need better funded and more diversified services providers that effectively help them improve quality, use modern technology and understand export procedures. Capacity building on IT and the use of the internet will be important for moving ahead. The government should also intensify public-private dialogues for effective ways to solve problems in time and understand what inhibits competitiveness in Lao PDR.

How can your company take advantage of the AEC?

« The 5 R's »

- 1. Know the Region** - understand the ASEAN as a region and as a market. Scan the environment and know what affects the needs, decisions, and behaviours of consumers, regulators, competitors, and other stakeholders.
- 2. Know the Rules** - study which AEC-related agreements and policies may affect your business. These rules may include those pertaining to tariff, foreign ownership of businesses, capital requirement, nationalities of board members, etc.
- 3. Know the Risks** - there are risks and challenges related to the AEC. SMEs who know these possible roadblocks are better prepared and equipped to compete.
- 4. Know your Resources** - do an ‘inventory of resources’ that can help you prepare. Check internal resources such as current workforce, company savings, intellectual properties, etc. Ask around for scheduled AEC information roadshows, skills training and workshops, and other relevant programs.
- 5. Know the Rewards** - be inspired and get motivated. Discover the benefits and imagine AEC’s vast opportunities to get you started. Be innovative and forward looking.

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Tourism and the ASEAN Single Market

The ASEAN Economic Community (AEC) : Impact on the Tourism Sector in Lao PDR

Tourism in ASEAN and Lao PDR

Tourism is one of the biggest economic sectors in ASEAN. In 2013, tourist arrivals in ASEAN reached 98 million and generated US\$112.6 billion in foreign exchange earnings and US\$294.4 billion in value added linked to tourism (e.g. shopping, entertainment, transportation, and various other tourism-related service occupations and productive sectors). Tourism accounts for approximately one tenth of regional GDP. The majority of ASEAN tourist arrivals are seen in Malaysia and Thailand (each sees roughly one quarter of total arrivals); Lao PDR received 3-5% of tourists in recent years (a total of 4.15 million in 2014).

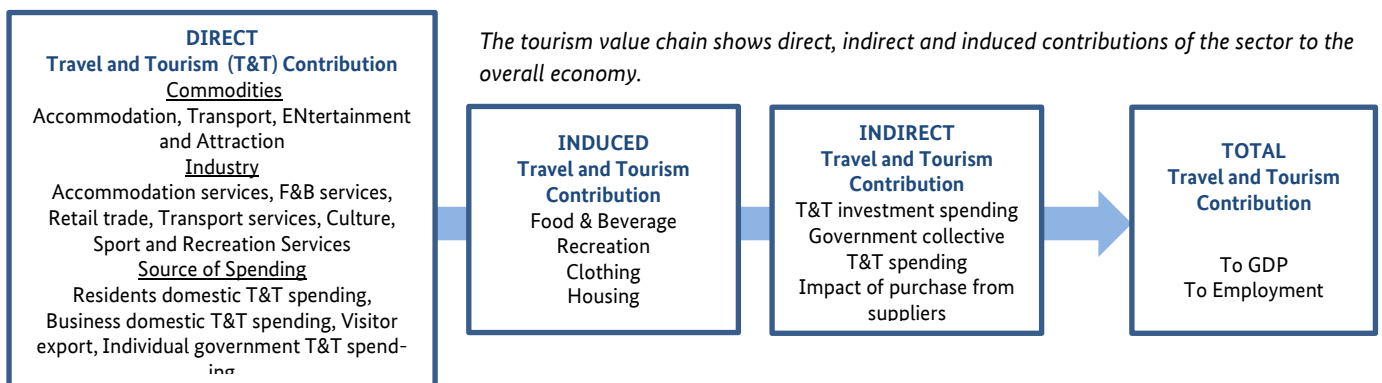
In Lao PDR, tourism directly contributes around 5.4% of GDP (2014); and 5% of all jobs are directly or indirectly linked to the tourism sector. Tourism arrivals have been growing by on average 18% per year in Lao PDR over the past two decades; reaching 4.1 million arrivals in 2014. International tourism receipts reached US\$641 million in 2014; sustaining around 3,000 SMEs, a core workforce of 17,000 people and another 165,000 jobs in input sectors. On average, tourists stay for 4.9 days and spend around US\$31 per day. A problem for the further development of the sector is the dominance of short-stay, low-spending visitors from neighbouring countries. Only around 15-20% of tourists were international arrivals in 2014 – but they generated more than half

of all tourism earnings. Average revenue by tourist in 2014 was only US\$154 – compared to US\$664 in Cambodia or US\$950 in Vietnam (figures for 2012).

The AEC's impact on the Lao Tourism Sector

The AEC will create a single market and production base with 625 million consumers and a regional GDP of US\$2.6 trillion (2014). Five core elements will characterise the AEC: Free flow of goods; free flow of services; free flow of investment; freer flow of capital; and free flow of skilled labour. Tourism is one of the priority sectors for integration by 2015. Tourism is also a cross-cutting sector, closely linked to a large number of economic sectors. The tourism industry therefore will be heavily influenced by the implementation of the AEC, in particular by two key ASEAN agreements, the ASEAN Trade in Goods Agreement (ATIGA) and ASEAN Framework Agreement on Services (AFAS). The Mutual Recognition Arrangement (MRA) on Tourism Professionals will facilitate the flow of skilled labour in the tourism sector.

Free flow of goods and the tourism sector: The elimination of 95% of tariffs in ASEAN is one of the key achievements of the AEC so far. For the tourism sector, lower tariffs mean cheaper imports, be it food, luxury items, construction material or transport vehicles. An example: Before the AEC, imports of agricultural



produce from Thailand and Vietnam such as onion, garlic, potato, banana, and cabbage were subject to a tariff rate of 30%. This rate still applies to extra-ASEAN imports, but for intra-ASEAN products the rate has been reduced to 5% (and 0% by 2018).

Liberalisation of investment and services provision in the tourism sector: The liberalisation of service provision and foreign investment in services sectors is negotiated under AFAS. For tourism, Lao PDR already allows for 100% foreign ownership in specific sub-sectors, including hotel lodging services with 3 stars or more, meal serving services with full restaurant service, beverage serving services without entertainment and tourism consulting services. For travel agencies and tour operators offering inbound services, 70% of foreign ownership is allowed.

Liberalisation of transport services: In the transport sector, passenger transportation on roads remains closed to foreign providers and investors. Liberalisation of air transport services resulted in first agreements but negotiations continue. Currently, Lao PDR has air service agreements signed with all ASEAN countries except the Philippines. However, direct flights go to only 5 ASEAN countries, as well as China and Korea. Ticket prices within and to Lao PDR remain high due to limited competition.

ASEAN Mutual Recognition Arrangement on Tourism Professionals Job Titles covered by the MRA	
Hotel Services	
Front Office	Front office manager, front office supervisor, receptionist, telephone operator, bell boy
Housekeeping	Executive housekeeper, laundry manager, floor supervisor, laundry attendant, room attendant, public area cleaner
Food Production	Executive chef, demi chef, commis chef, chef de partie, commis pastry, baker, butcher
Food and Beverage Services	F&B director, F&B outlet manager, head waiter, bartender, waiter
Travel Services	
Travel Agencies	General manager, assistant general manager, senior travel consultant, travel consultant
Tour Operation	Product manager, sales and marketing manager, credit manager, ticketing manager, tour manager

Free flow of tourism professionals: Highly relevant for the tourism industry is the ASEAN Mutual Recognition Arrangement on Tourism Professionals, signed in 2012. The qualification of a foreign tourism professional may be recognised by other Member States, and if such qualification is recognised, he/she may be eligible to work in a host country provided that he/she possesses a valid tourism competency certificate in a specific tourism job title as specified in the ASEAN Common Competency Standards for Tourism Professionals (ACCSTP) (see Table). The eligibility to work in a host country will be subjected to prevailing domestic laws and regulations concerning visa and migration.

The ASEAN joint regional agenda on Tourism

The further development of sustainable and high quality tourism in ASEAN needs a joint regional approach. ASEAN Member States (AMS) identified various challenges, such as creating a better balance in the distribution of the benefits of tourism between and within AMS; making cross border formalities more convenient and less costly; reducing the vulnerability of the natural and cultural heritage assets and related populations to climate change; and developing destinations that are inclusive, green and knowledge-based.

ASEAN Tourism Ministers (ATM) endorsed the ASEAN Tourism Strategic Plan (ATSP) 2016-2025 to jointly tackle challenges. Within the ATSP, National Tourism Organizations (NTOs) agreed to focus on the development of regional products and packages, creative marketing and promotion strategies, tourism investment, improvement of services quality, human resource development, as well as travel facilitation and ASEAN connectivity.

ASEAN countries are also working together to develop and implement ASEAN Tourism Standards that will help to streamline quality in the region. In 2012, ATM adopted six ASEAN Tourism Standards, namely on Green Hotels (lead coordinator: Thailand), Homestay (Malaysia), Spa Services (Thailand), Public Toilet (Brunei Darussalam), and Clean Tourist City (Cambodia), Community Based Tourism (Cambodia). Lao PDR already has 32 hotels meeting the Green Hotel Standards; recognition for meeting the Homestay Standard will first be awarded in 2016. The other standards are to be fully operational by 2018.

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Lao Coffee in the ASEAN Single Market

The ASEAN Economic Community (AEC): Impact on the Coffee Sector in Lao PDR

The Lao Coffee Sector – driving agricultural export earnings

Coffee is the most important agricultural sector in Lao PDR in terms of export earnings. Currently, coffee production is located in 10 out of 16 provinces in Lao PDR, with a high concentration in the three Southern provinces, Champasak, Sekong and Saravan, widely known as the Bolaven plateau. Coffee is mostly grown by poor smallholder farmers and their families; the livelihood of around 300,000 people depends on the coffee sector. The local coffee industry has significantly expanded in the past decade due to improving quality and access to new export markets such as the EU. More land, generally pristine, is being devoted to coffee production. The total area dedicated to coffee plantations has almost doubled since 2005; reaching 77,279 hectare in 2013. Out of the total area, 59,178 hectare were harvested in 2013. Total harvest was 70,530 tons in 2013; of which 30,180 tons (43%) have been exported (corresponding to 0.5 million of 60kg bags of green beans). Annual export earnings reached US\$72 million in 2013. Coffee currently makes up about 80% of the country's agricultural exports (and about 2.6% of total goods exports).¹

Export performance is still below its potential when compared to ASEAN neighbours. Lao PDR accounts for around 3-5% of coffee production in South-East Asia (much less than Vietnam and Indonesia, but more than Thailand and the Philippines), and its share in South-East Asia's coffee exports is around 1.5-2%. Based on data from the Lao Coffee Association, Lao coffee beans have been exported to 23 countries in 2013; including 5 ASEAN countries. Top destinations are Vietnam, Japan, Germany, Belgium and Poland. Nevertheless, Lao coffee remains a small niche

¹ The figures should be treated with caution as for some traders, cooperatives or associations data may not have been recorded; and much of the trading (especially with Vietnam) occurs without a proper reporting or recording system. Figures based on data from the Lao Coffee Association.

product, unrecognized at the international level. Lao PDR's export quantity accounts for approximately 0.4 % of world coffee market volumes and corresponds to only about 2-4 % of the coffee export volumes of neighbouring Vietnam (which exported between 22 and 28 million bags in recent years). Indonesia's annual export volume reached around 5-7 million bags in recent years.

The AEC 2015 – new markets, new quality requirements and an opportunity to up-grade and invest in regional markets

Potential export markets widen. The ASEAN Single Market with its approximately 625 million consumers and growing middle class is an important target market for the Lao coffee. Indonesia, the Philippines, Vietnam and Thailand all consume between 2 and 4 million bags (of 60kg) per year. Per-capita consumption is still below 1kg in other ASEAN countries. Coffee consumption is expected to increase quickly in ASEAN, especially in countries like Indonesia, Malaysia and Vietnam where disposable income is increasing, and urban middle class is increasingly adopting a Western lifestyle. Brunei, Cambodia, Malaysia, Singapore, the Philippines and Myanmar are net importers of (raw) coffee in ASEAN. Market demand in Indonesia, the Philippines, Thailand and Malaysia tends to be driven by Robusta coffee (used in ready-to-drink or instant coffee products). Lao PDR exports predominantly Robusta coffee but the share of higher-quality Arabica in exports is also increasing (30-40% of exports).

Quality demands increase. Competitiveness of Lao coffee in the ASEAN Single market will depend on further efforts to reach premium quality; e.g. through increased use of technology and quality management. Exporting within the AEC will increasingly require compliance with regional and international standards such as ASEAN Coffee Standards, Good Agriculture Practice (GAP), Good Manufacturing Practice (GMP), Good Hygiene Prac-



Coffee production in the Southern Provinces of Lao PDR

tice (GHP), organic certificates or Geographic Identification (GI). Lao producers also need to be aware of inspection mechanisms including Hazard Analysis Critical Control Point (HACCP) and national Sanitary and Phytosanitary Standards (SPS).

Market access becomes easier and cheaper. Preferential tariff rates for coffee in ASEAN have come down to 0-5%. Outside the AEC (and its numerous Free Trade Agreements), Lao PDR and the Philippines still charge 40% import tax; Thailand's MFN (Most-Favourite Nation) tariff on coffee products is even 90% on average. This means that Lao coffee is particularly competitive in countries with a large difference between the low AEC preferential tariff and the MFN tariff charged on coffee from e.g. South America.

Opportunities for value chain up-grading are abundant. The AEC facilitates foreign investment which enables Lao coffee producers and processors to expand their operations beyond Lao PDR. A large Lao coffee producer has already begun to grow coffee in Northern Thailand. In addition, the AEC is an opportunity to dedicate greater resources to processing. At the moment, Lao PDR exports mostly raw (green) coffee beans which are then processed abroad. In order to capture a greater share of value added, Lao PDR could increasingly export processed coffee products.

ASEAN is a large market for instant coffee. Malaysia imports large amounts of raw coffee (around 2 million bags per year) and exports it again in form of soluble coffee. Lao PDR can take a share in this market by making use of the large endowment with raw coffee and the availability of cheap labour force.

Which way forward for the Lao coffee sector?

Coffee consumption and demand for Lao coffee is also promising in Asia-Pacific beyond ASEAN. A large export potential for Lao coffee is with ASEAN-plus partners. Consumption in neighbouring markets is growing rapidly. Japan consumed a total of 7.1 million bags in 2012, India 1.9 million, Korea 1.7 million, and China approx. 1 million. Coffee consumption in China is expected to raise to 2.8 million bags annually by 2020. Coffee consumption

in Japan and Korea is predominately Arabica, corresponding to the increasing Arabica share in Lao exports. Demand for high-quality niche coffee products, as well as sustainable, fair trade, organic and traceable coffee can be expected to be particularly strong and growing in more mature markets such as Japan, Korea, New Zealand and Australia, and in Europe.

Production costs will remain low. Competitiveness of Lao coffee might also remain stable or increase since production costs, particularly labour costs, will remain low in the close future: the potential labour force for coffee production (young rural population)

is high and wages are still relatively low; and both factors are changing more slowly than in other production countries. Nevertheless, the isolated small-holder production also brings challenges with it, particularly related to quality management and understanding export procedures. Improving planning and management capacity, as well as promoting linkages will become indispensable in times of the AEC.

Coffee has become a government priority.

The Lao government has prioritized the further development of Lao coffee as a top agricultural export product. The aim is to expand production to the whole country to cover a production area of 130,000 hectare by

2025. The Lao government also seeks to strengthen coffee production and exports based on Geographical Indicators (GI) concept (creating a "Lao" brand). Fair trade is another standard that could be leveraged to improve impact on producer's living standards. Lao PDR is already a member of the ASEAN Coffee Federation (ACF) and seeks to become a member of the International Coffee Organization (ICO). This will further help Lao coffee to become better known to processors and consumers around the world and will attract investment into the Lao coffee sector. If Lao PDR can further improve quality and branding of Lao coffee, the prospects for Lao coffee exports are positive.

Average Tariffs on Coffee & Coffee products in ASEAN

	AEC Preferential Tariff	MFN Tariff
Brunei	0%	0%
Cambodia	0-5%	27%
Indonesia	0%	5%
Lao PDR	0-5%	40%
Malaysia	0%	0%
Myanmar	0-5%	9%
Philippines	0%	40%
Singapore	0%	0%
Thailand	5%	90%
Vietnam	5%	25%

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