Sector Working Group Uplands

Northern Upland Sustainable Development Programme (NUSDP)

Core Coherent Programme Design and Feasibility

Consultant Report on Foreign Direct Investments

Weiyi Shi

weiyishi@gmail.com

Table of Contents

List of Figures and Displays

1. Introduction

The Core Coherent Programs (CCP) aim to achieve secured and improved livelihoods of the rural poor in selected areas of the northern uplands based on sustainable land and natural resource management and community driven development. FDI as a contextual issue is highly relevant to a number of CCP priorities:

- FDI presents opportunities for scaling up production, commercializing agriculture, and linking farmers to global markets.
- Commercialization of agriculture through FDI may heighten risks and compromise food security for certain vulnerable groups.
- FDI through land concessions (or contract farming) has significant implications for land and natural resource management.
- Current decision processes in FDI approval present challenges for bottom-up planning and the community driven development approach.
- Appropriate governance of FDI is pivotal to ensuring benefits for the poor and fostering a healthy, competitive business environment.

This document first provides a background assessment of FDI in the Lao northern upland, with a particular focus on agriculture. Based on the assessment, I then present inputs contributing to the design of program activities, implementation, and cost estimates.

2. The Context of FDI in the Northern Uplands

FDI plays an increasingly prominent role in the Lao economy. The ratio of FDI inflow to GDP has risen from 1.8% in 2000 to a predicted 15% in 2009 (World Bank, 2007).[1] The energy sector (driven mainly by investments in hydroelectric plants) accounts for the greatest cumulative investment value, followed by agriculture and mining (Table 1). Though agricultural investments may not account for the largest amount of FDI inflow, they have far reaching implications for the rural poor in the northern region. Agriculture accounts for 56% of GDP in northern provinces compared to the national average of 32%. Around 90% of the northern population is engaged in agriculture as their principal livelihood.

Table 1 Foreign Direct Investments in Lao PDR

	2001	2002	2003	2004	2005	2006	2007	2008
				(USD million)				
Electricity	-	1.0	85.8	5.5	1065.3	1776.7	360.5	40.0
Agriculture	18.6	14.0	17.3	75.7	17.4	458.5	183.8	80.5
Mining	8.9	0.5	20.7	312.1	93.5	73.8	115.3	100.2
Services	16.7	49.8	253.1	92.4	48.6	262.8	280.6	264.6
Industry	9.9	67.8	89.1	47.5	20.6	127.9	196.7	173.9

Source: Ministry of Planning and Investments.

[1] FDI has declined since 2006, but the pattern is driven mostly by hydro investments and is reflective of FDI trends in the region (GTZ, 2007).

2. 1 The policy framework

The government of Laos' (GoL) Open Door Policy promotes the private sector, including FDI, as a key pathway to increasing economic opportunities (NGPES). In an effort to entice FDI and improve the investment climate, GoL adopted a series of regulatory changes in recent years. Main efforts include a gradual decentralization of FDI approval (PM Decree 64, 2003, and its subsequent absorption in the Foreign Investment Law)[2], favorable tax breaks and revenue retention policies for investors based on promoted zones and sectors (Amended Law on the Promotion of Foreign Investments, 2004)[3], and streamlining enterprise registration through automatic registration based on the Negative List (Enterprise Law, officially promulgated in 2006).[4]

Meanwhile, it is GoL's priority to stop shifting cultivation, increase forest cover, and commercialize agriculture (NGPES, National Socioeconomic Development Plans, Forestry Strategy 2020). This puts both upland farmers and various levels of government under pressure to develop alternative permanent crops for former shifting cultivation areas, creating opportunities for foreign as well as domestic investors in developing commercial agriculture.

2.2 Regional economic context

The Lao northern uplands are surrounded by the region's fastest growing economies. Regional trade integration and improved infrastructure create greater demand for Lao PDR's resources and products.[5] Compared to its populous neighbors, Lao PDR possesses relatively ample land resources that make it an attractive destination for agricultural investments. FDI in the northern agricultural sector originates mainly from China and Vietnam.[6] Thailand serves as a significant trading partner and market destination but has made limited direct investments in the sector. With the recent global economic downturn, however, both FDI and trade volumes are expected to decline in the near future. It is in this economic context we must

---

[2] Decree 64 (2003) decentralized the power of managing foreign investments, giving major provinces (Vientiane Municipality, Savannakhet, Champasak and Luang Prabang Provinces) authorities to approve investments of up to 2 million USD and other provinces up to 1 million USD. In 2004, the implementation decree of Implementing Decree of the Law on the Promotion of Foreign Investment (Article 53) further lifted the caps to 5 and 3 million USD respectively.

[3] For example, corporate income tax ranges from 10-20% depending on the zonal classification (and is even lower during the initial tax reduction period) compared to the general profit tax of 35%.

[4] The Foreign Investment Law is currently being revised for a potential merger of the Domestic and Foreign Investment laws and ensuring compatibility with the new Enterprise Law. The new Enterprise Law is deemed a substantial step forward in simplifying and streamlining the business registration process: Unless a proposed investment project is on the Negative List, the business will be registered automatically through "One-Stop Service" at MOIC and its associated provincial and local entities within 10 working days. However, the Law has been implemented to a very limited extent in practice.

[5] The Lao PDR joined the ASEAN Free Trade Agreement (AFTA) in 1997. The China-ASEAN Trade in Goods Agreement (TIG) is in preparation for the creation of a China-ASEAN Free Trade Area (CAFTA) by 2010. The Thai government's Ayerwaddi - Chao Phraya - Mekong Economic

[5] The Lao PDR joined the ASEAN Free Trade Agreement (AFTA) in 1997. The China-ASEAN Trade in Goods Agreement (TIG) is in preparation for the creation of a China-ASEAN Free Trade Area (CAFTA) by 2010. The Thai government's Ayerwaddi - Chao Phraya - Mekong Economic Cooperation Strategy (ACMECS) Plan of Action has started strengthening trade and investment between Thailand, Cambodia, Lao PDR, Myanmar, and Vietnam (Diagnostic Study).

[6] In addition to market fundamentals, Chinese investors are driven by state subsidies to invest in agriculture in northern Lao PDR and Myanmar under the Poppy Replacement Plantation, or Alternative Development, program.

consider the opportunities and challenges faced by the agriculture sector of Lao PDR.

3. General Patterns of FDI in the Northern Agricultural Sector

Investments and trade are intricately linked and the distinction between the two can be slight in practice. Agricultural investors mainly operate through the 2+3 contract farming model in the northern uplands, in which they are expected to provide capital, farming technology, and marketing channels. In implementation, however, "investors," due to a lack of either capacity or incentives, may fail to provide such inputs, rendering them marginally different from traders. In some contract farming cases, owing partially to a limited level of competition, "investors" provide little more than a seedling loan to secure exclusive rights to harvests. This is particularly common for annual crops. Investors' input in perennial crops (e.g. rubber) tend to be more substantial, due in part to the higher initial investments required.

The modes of operation and contract farming schemes are highly varied in the northern uplands. In addition to the 2+3 model, agricultural land concessions are concentrated in rubber and limited in scale compared to those in southern provinces. 1+4, a variant of 2+3 and considered sometimes equivalent to land concessions, is also common in rubber investments.[7]

In terms of crop varieties, investments and trade are concentrated in the production of cash crops and commercial trees, including maize, rubber, sugarcane, tea, cassava, job's tear, sesame, soybean, paper mulberry, stick lac, and seasonal fruits in certain areas (e.g. watermelons). Most are planted in former fallow to replace upland rice; others (such as watermelons) are planted in off-season paddies. Crop selections are driven mainly by regional commodity demands and promotional strategies of the provinces. Plans on specific crops are built into the provincial socioeconomic plans and sometimes highlighted as stand-alone policies. Luang Namtha, for example, has issued provincial regulations on the promotion and governing of rubber development. Certain decisions, such as the promotion of stick lac, are made at the central level and implemented henceforth at the provincial and local levels.

A wide variety of NTFPs are traded, including wild tea, cardamom, incense bark, broom grass, benzoin, bamboo shoots, galangal fruits (*mak kha*) and a number of medicinal plants. Most NTFP trades are limited to bulk collection and sale with little quality differentiation, processing, or investment in domesticating the plant species for commercial production. NTFP exports are expected to decline due to the dwindling resource base.

---

[7] 2+3 is a contract farming model officially promoted by the GoL. In this model farmers contribute land and labor inputs while investors are responsible for capital, techniques, and product marketing. For annual crops, this implies that farmers plant and investors/traders collect. For perennial crops like rubber, 2+3 is often associated with profit or product sharing schemes between farmers and investors (with farmers claiming a typical 70%). In the 1+4 model, farmers obtain a worse share by contributing only land. Investors are responsible for the other inputs. If farmers work for the investors in this model, they receive wage compensation. In rubber investments, it is widely known that many 2+3 contracts dissolve into the 1+4 model in implementation because farmers lack alternative income sources during the pre-tapping years.

4. Diverse Scenarios in the Northern Uplands

The general trade and investment patterns should not obscure the diverse scenarios of provinces in the northern uplands: It is dangerous to consider the north as one homogenous entity when there exists immense variety in production systems, market access, and poverty levels (World Bank, 2008a). While border provinces such as Luang Namtha and Oudomxai have enjoyed vibrant investment and trading activities in agriculture in recent years, other, more isolated communities have had relatively little exposure. Table 2 presents provincial FDI patterns across sectors. The sectoral compositions of FDI are drastically different across the three pilot provinces selected for the CCP, Luang Prabang, Huaphanh and Phongsaly. While agricultural FDI dominates in Phongsaly, it plays a limited role in Luang Prabang (dominated by services and hospitality) and Huaphanh (dominated by mining).

Table 2 Foreign Direct Investments by Sector and Province: 2004-2008

	Agriculture	Mining	Services	Industry
		(USD Million)		
Attapeu	47.2	4.0	0.5	0.6
Bokeo	1.0	5.0	129.1	0.1
Borlikhamxay	13.7	5.7	0.8	132.8
Champassak	101.5	47.1	39.0	25.8
Huaphanh	2.9	56.2	2.7	3.5
Khammouan	13.3	54.9	1.2	71.2
Luang Namtha	4.8	10.9	0.7	1.1
Luang Prabang	3.4	7.1	19.4	1.8
Oudomxay	9.5	19.6	2.9	8.7
Phongsaly	20.4	10.8	-	1.2
Saravan	11.1	11.5	0.8	0.4
Savannakhet	124.6	39.3	3.1	10.7
Vientiane	44.8	2.7	1.0	15.4
Vientiane Capital	151.4	401.6	1,446.9	558.9
Xayaboury	6.3	6.0	1.1	57.9
Xiengkhouang	16.0	24.6	2.9	8.2
Unidentified location	353.2	8.5	26.8	-
Total	925.1	715.5	1,678.7	898.4

Source: Ministry of Planning and Investments, Departments of Planning and Investments in Huaphanh, Phongsaly, and Luang Prabang.
Note: When investment amounts reported by DPI and MPI differ, the higher value is taken. Data exclude hydro investments. There may be significant under reporting among provinces where the team did not collect data from provincial authorities.

4. 1 Luang Prabang

Luang Prabang presents the dichotomy of a booming, service-oriented urban center (driven entirely by tourism) surrounded by isolated, subsistence-oriented rural communities. Of the province's 92 formally registered foreign investment projects since 1999, only 9 are in agriculture, including investments in rubber, stick lac, maize, tea, cassava, tobacco, and agarwood. The rest are in tourism amenities, construction, and light industry.[8] This pattern is in contrast to those of Luang Namtha, Oudomxai, and Phongsaly, where a vast majority of FDI is directed to the agricultural sector. It is also common in these provinces to observe internal capital flow from population centers to rural areas for agricultural investments. In Luang

[8] Based on cumulative FDI data provided by DPI Luang Prabang spanning 1999-2008.

Prabang, however, investment prospects in the urban service sector, thanks to the relative low risks and quick return, appear to out-compete agriculture and impede capital flow to rural vicinities. Rather, the center of agricultural investments in Luang Prabang is in Nambak District, adjacent to the commercial agricultural hub of Oudomxai.

The service sector of Luang Prabang City has only limited demand pull on surrounding areas.[9] The mismatch between the product demands of the tourism industry and the crude productive capacities of the rural poor implies that much of the urban consumption relies on import (from Chiangmai, Bangkok, and Hanoi), while the surrounding rural communities remain in largely subsistence-oriented livelihoods. In Pakxeng District, a district two hours drive away from Luang Prabang on an all-season road, farmers are presented with few commercial opportunities, except for nascent developments in maize, rubber, and stick lac promoted by the provincial and district governments.

4.2 Huaphanh

Although Huaphanh shares an extensive border with Vietnam, the province demonstrates limited FDI and trade activities in commercial agriculture. The number of foreign and domestic traders and middle agents is large (more than 10 on average per district), but they are singularly focused on farming maize to supply the Vietnamese animal feed industry. In 2008, maize production under contract farming exceeded 125,800 tons (PAFO Huaphanh). However, much of the production remains unsold due to a collapse in world commodity prices.[10] Traders/investors' inputs in contract farming schemes are often limited to providing seeds alone for loan or purchase. Huaphanh's other main category of export is NTFP, though the supply has been declining over the years. Compared to other northern provinces, rubber development is very limited in Huaphanh due to unfavorable terrain and climatic conditions (and has begun only in one district in Viengthong, with 100 ha in concession, subject to annual expansion, and 2,000 ha in 2+3 contracting farming with a Chinese investor). Rather, Huaphanh demonstrates active investment activities in the mining sector (10 sites already mining or under exploration), suggesting that mining may present an attractive alternative to agriculture for investors.

4.3 Phongsaly

The patterns of FDI and trade in Phongsaly resemble the earlier years of Luang Namtha and Oudomxai (the influx of agricultural FDI to Phongsaly arrived slightly later). All three provinces border China and their commercial production is geared to serve Chinese demand. Agricultural investments account for more than 85% of FDI in Phongsaly (by number of projects) and are directed mostly to rubber and tea plantations. There are currently 6 tea companies (3 foreign, 3 domestic) and 10 rubber companies (8 foreign, 2 domestic) operating in 6 districts. The province has

---

[9] This observation is confirmed by Ashley (2006). However, World Bank (2008a) finds that the markets of Luang Prabang and Vientiane constitute the dominant pull factor for agriculture commercialization in upland areas in the province. Specifically, livestock is being produced in the uplands for markets in Luang Prabang, Vientiane Province, and Vientiane Capital.

[10] Note that this is not entirely caused by traders' violation of contracts. The contracts specified a range of collection prices. However, farmers have sometimes refused to sell for less than the top of the range in the hope that prices may bounce back up. Due to a lack of storage facilities, however, a large quantity of maize degraded.

47,000 ha of land committed to rubber under contracts, of which 12,600 ha have been implemented in contract farming schemes and 930 ha in concession. Contract-farmed tea plantations now amount to 2,300 ha. In addition to formally registered companies, there are also developments by individual investors (both domestic and foreign). However it should be noted that even in Phongsaly, where there is substantial interest in agricultural investments, parts of the province remain isolated from commercial opportunities due to poor infrastructure and lack of suitable land.

The wide variation in FDI patterns supports the selection of these three pilot provinces to represent the diverse northern upland. This variation also implies that one unified approach in addressing FDI-related issues would be inappropriate. Although the set of tools and interventions may be similar, the priority and sequencing of interventions differ. While it may be a priority for some communities to strengthen negotiating positions with existing investors and enhance farmers' gains, the challenge for others may be to foster commercial opportunities in agriculture in the first place. Substantial FDI represented in sectors other than agriculture also speaks to the advantage of broadening the program's sectoral focus (Section 6.7).

5. Opportunities and Challenges in Agricultural FDI

FDI brings opportunities as well as challenges for the northern Lao agricultural sector. As the upland transitions from largely subsistence livelihoods to commercial production, FDI brings much needed capital, access to global markets, and opportunities for technology transfer. However, reaping the benefits of FDI hinges on a number of contingencies: the provision of an enabling environment, appropriate governance, and empowered local communities capable of negotiating and capitalizing on commercial opportunities.

5.1 Inappropriate state interventions limit farmers' options

In developing a healthy private sector, the role of the government is best described to provide an enabling environment: The government provides public goods and services (e.g. infrastructure, R&D, a legal framework), maintains the competitiveness of the markets (preventing monopolistic practices), and intervenes in the case of market failures (e.g. mitigation of social and environmental impacts). However, as an economy in transition, GoL still is in a gradual process of decentralization and deregulation. The government at various levels plays a substantial, direct role in making economic decisions. State interventions in commercial agricultural activities are manifested in the following ways:

1) Market segmentation and artificial monopolies

Across the northern provinces, it is observed that PAFO and DAFO and relevant line agencies, together with traders and investors, create inefficient market segmentation and artificial monopolies. This is widely observed for contract farming in maize and tea, where traders/investors are each allocated a set of villages to collect products from. Collection from other areas is not allowed. Farmers can legitimately access only one buyer at a time and therefore must accept whatever prices and quantities the buyer offers. Even when there is a pre-agreed contract price, farmers are left in a disadvantageous position when traders violate contracts, since the farmers have no alternative buyers to turn to.[11] However, it is known that farmers sometimes sell to buyers in other market segments secretly when they perceive better prices.

Case 1 Artificial Trader/Investor Monopolies
In Phongsaly the district assigns each tea company to a partition of villages and disallows trading across partitions. In a village assigned to a Malaysian tea company, the company cannot absorb fully the villagers' production due to limited storage capacity and stringent quality requirements. An adjacent factory is willing to collect but cannot due to the partition rule. Huaphanh has a similar situation where maize traders are assigned to their respective clusters of villages. In Luang Prabang, the entire province is dependent on one stick lac buyer (a Chinese company with a provincial contract), severely limiting farmers' options.

Market segmentation is desired by traders/investors as it eliminates competition. It is favored by PAFO/DAFO and associated agencies as it presents a façade of better order and control in the tradition of a planned economy. There is a general fear that an open market would create chaos and distrust in villagers' abilities to discern and negotiate competing market offers. In some cases, PAFO or DAFO are compensated by traders/investors to maintain an uncompetitive environment in their favor.

2) Top-down decision-making, hindering direct interactions between investors and farmers

The government's extensive involvement in agricultural investment decisions hinders direct interactions between the private sector and the farmers, where the demands and interests of both sides can be communicated and negotiated openly. Instead, FDI decisions, in agriculture or otherwise, are often made at a higher level (provincial and central) without thorough assessment of local situations. Investment contracts with higher authorities then become instruments for negotiation with local authorities and farmers. Farmers are left with little room to negotiate. The top-down decision process is common across rubber, maize, and tea, as well as in the promotion of stick lac in Luang Prabang Province.

When government plays an interceding role between the private sector and farmers, the two sides often do not demonstrate a consistent understanding of contractual arrangements or mutual trust, creating possibilities for later disputes. The process is not unlike an "arranged marriage," where the needs of investors/traders and farmers are sometimes mismatched. A rubber investor could well be assigned to a village where farmers have no desire to plant the crop, or where the farmers possess enough funds for planting already.

Top-down, multi-tiered decision-making also presents challenges for information sharing and coordination across the hierarchy. Decisions on agricultural investments, depending on the size of investment, land area, and nature of the agreement, can be made at the district, provincial, or central levels. However, the coordination and information flow across the hierarchy is limited, leading to sometimes overlapping land designations. Information sharing across sectors is also

[11] In some cases, such arrangements are further cemented by investors/traders' involvement in the development of local infrastructure (in exchange they secure exclusive collection rights for an extended period of time).

sorely lacking (e.g. mining concessions are coordinated only at the central level and do not involve or report to provincial land management authorities).

5.2 Lack of accountability

Accountability pertains to all parties involved in commercial agriculture: GoL, farmers, and businesses.

1) The government is not accountable. PAFO/DAFO and relevant agencies play a fluid role in agricultural investments: They are the facilitators and organizers by way of promoting contract farming/land concession and encouraging/persuading farmers to collaborate or concede. They are the legal signers of contracts in addition to or in place of the business parties (farmers as suppliers). They are the planner in allocating market shares to traders and investors. They are the implementers and service providers, sometimes paid by investors that lack capacity to carry out seedling distribution and technical extension. They also play a role in monitoring investment projects and in mediating disputes. This holistic approach without clear boundaries or responsibilities makes it difficult to ensure line agencies act in the interest of farmers. It is also difficult to hold PAFO/DAFO and related agencies accountable for the investment decisions they make and the services they provide, since the minimal monitoring and evaluation efforts currently available also rest with the government.

Case 2 Lack of Accountability
In the Pakxeng District of Luang Prabang, a small investor/trader from Nambak entered into contract farming with local villagers through DAFO. The investor provides seedling loans to villagers while DAFO promotes the crop to villagers and instructs them on planting methods. However, DAFO told villagers to plant at the beginning of the dry season and the rubber trees all ended up dying. Now the villagers, after laboring in vain, owe money to the investor/trader that they are unlikely to repay. Both the investor and villagers lose in this case while DAFO is not held accountable for its mismanagement.

2) Investors/traders are not accountable: There is a lack of effective mechanisms to hold investors/traders accountable for contract conditions. Monitoring of private investments is weak and often limited to self-reporting and checking for proper registrations and licensing documents. DPI and PAFO report a lack of both staff capacity and established criteria for evaluating investor performance. Some report that the “evaluation” is mostly crisis-driven, based on the disputes and complaints of villagers. However, there have been encouraging signs of learning among provinces and districts that are relative latecomers to contract farming. Compared to the early rubber contracts in Luang Namtha, many newer contracts have built in performance-based conditions. Investors are given incremental land access provided that their performance is satisfactory.

3) Farmers are not accountable: It is equally important to raise awareness of contract compliance among farmers. As is indicated in Section 5.5, a culture of contract enforcement by all parties is an important element in improving the business environment.

5.3 Increased insecurity, heightened risks shared unequally

Agriculture commercialization is necessarily linked with exposure to market risks. The question is then 1) how the heightened risks are distributed among stakeholders, 2) whether farmers make informed decisions on the risks they take, and 3) what's done to manage and mitigate risks. Our assessment indicates that there is a wide spectrum of risk sharing scenarios. Depending on the specific commodity and contractual arrangements, risk distribution can be highly skewed, borne mostly by farmers. Governmental policies and interventions have in some cases limited farmers' choices and increased their exposure to risks.

Case 3 Skewed Risk Sharing
In some contract farming schemes farmers are the sole bearer of risks. For example, the Nanyoby Bank provides loans to farmers in Luang Prabang to engage in contract farming with a Chinese company for stick lac. The company bears minimal risk in this arrangement because it simply promotes the crop and farmers pay for input costs with borrowed money. If market conditions are favorable, the company reaps profits. When prices drop, as they have with the global economic downturn, the company refuses to collect at prices specified in the contract. As there are no effective mechanisms to hold the company accountable, the losses from capital and labor inputs are borne entirely by the farmers, who are now saddled with unsold stick lac and owe payments to the bank. Similar stories are repeated throughout the northern uplands.

In addition, the provinces' tendency to promote a single crop increases villagers' vulnerability to market fluctuations. As most of these crops are promoted as an alternative to upland rice, commodity price fluctuations pose direct threats to villagers' food security. Lack of alternative incomes also weakens farmers' negotiating positions. In the case of rubber, many villagers exchange shares of future profits for payments today because they do not possess alternative means of income during the pre-tapping years.

5.4 Inadequate investment appraisal, lack of long-term vision to attract FDI

As part of the decentralization policy, provinces have been given greater autonomy in attracting and approving foreign investments.[12] However, they lack coherent strategies for attracting FDI based on long-term development priorities. Investments are approved mostly on a non-discriminatory, first come first serve basis. There is limited awareness and capacity at DPI, DOIC, and other line agencies for devising strategies to actively seek and identify potential investors. The investment promotion section of DPI, contrary to what the title suggests, serves only administrative and licensing functions for already identified investment prospects. The Lao National Chamber of Commerce and Industry has facilitated trade fairs and bi-lateral trade negotiations, but as a recently formed social organization, its capacity is limited at the provincial level (Phongsaly does not currently have a Chamber of Commerce but will begin one in 2009).

Capacity is limited at both DPI and relevant technical line agencies to properly appraise investment proposals for technical merits and socioeconomic implications. Investment trends are driven entirely by fluctuant regional commodity demands, be it

[12] Major provinces (Vientiane Municipality, Savannakhet, Champasak and Luang Prabang Provinces) are given the authority to approve investments up to 5 million USD and others up to 3 million.

for maize or rubber, with inadequate consideration for mitigating risks and social or environmental impacts.

5.5 Poor investment climate attracts speculative investors

The overall investment climate in the northern uplands, though seemingly removed from specific issues arising from commercial agriculture, is in fact of immediate consequence: It is correlated with both the number and quality of investors the area is able to attract. Many factors contribute to the quality of the investment climate, including factors related to resources and endowments (e.g. physical infrastructure, human resources) and those related to governance (e.g. registration and licensing procedures, competition, contract enforcements, transparency and the legal environment). The northern uplands face challenges in both regards: basic and market infrastructures (roads, electricity, communications, irrigation, post-harvest storage and processing facilities, banking and credit etc.) are underdeveloped; terrain and climatic conditions allow limited varieties of suitable crops; the majority of the labor force is poorly educated and untrained in technologies for commercial agriculture.

In governing investments, Lao PDR is equally challenged:

1) Investment and trade procedures are in need of further simplification and streamlining. In spite of the promulgation of the Enterprise Law and development of the Negative List, business registration and licensing remain far from an automatic process in implementation. World Bank's *Doing Business Indicators* ranks Lao PDR one of the last in the region in ease to establish a business and conduct cross-border trades. It takes on average 103 days (8 procedures) to start a business and 50 days (9 documents) for export (World Bank, 2008b).

2) Unpredictable informal charges increase costs of business and disrupt fair competition. Investors and traders feel that they have to pay informal fees in order to facilitate the business process. Decisions on investments, often made ultimately by the government rather than business parties, are not transparent. For agricultural projects, such decisions are seldom based on sound appraisals due to a lack of both capacity and proper incentives.

3) The culture of respecting and enforcing contracts is weak. Agricultural investors, particularly those engaged in higher risk, perennial crops such as rubber, predominantly fear the prospect of contract breach by both the government (signers) and farmers (responsible for production).

A poorly governed investment climate leads to the following immediate consequences:

1) An uncertain environment tends to attract speculators. When contract enforcement is weak and outcomes are highly uncertain, investors are not committed to making long-term investments with mutual benefits. This may have contributed to some seemingly ambitious investment projects (particularly in rubber and mining) turning out to be empty shells, with investors arbitraging for speculative, quick gains from land or resource access without committing substantial inputs to actually develop the sector.

2) Poor governance and corrupt institutions attract and encourage unfair business practices: Businesses that are willing and able to bribe are rewarded and given an unfair advantage. These businesses in turn support and strengthen the institutions, thereby perpetuating a perverse incentive structure. More accountable companies that do not subscribe to the status quo system face a competitive disadvantage.

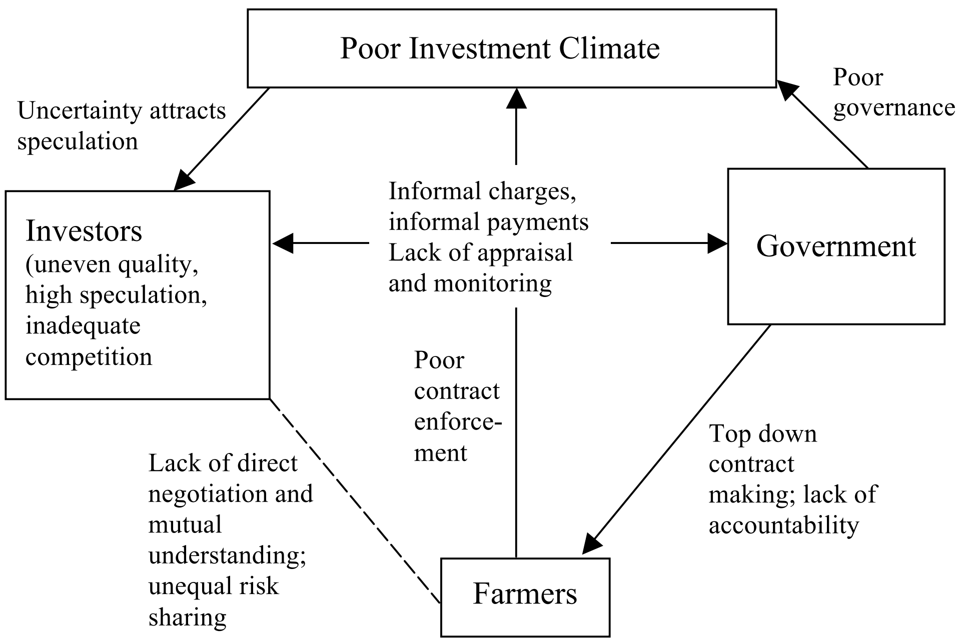
3) Poor governance disproportionately disadvantages micro to small investors, who often choose to stay under the radar to avoid informal costs. This gray status prevents them from expanding to the formal sectors for greater commercial opportunities.

The quality of the business environment has over-arching implications. It is not only important for the long-term, sustainable economic growth of the country, but also highly relevant for the rural, upland poor: They need quality investors (foreign or domestic) who are committed to the long-term, sustainable development of the agricultural sector and also enabling conditions to carry out their own entrepreneurial endeavors. Improving the investment environment (both in infrastructure and governance) should be a coherent theme through CCP and PBA.

5.6 Summary Problem Chart

At the risk of oversimplification, I summarize the key issues in a problem chart:

Figure 1 Summary Problem Chart for FDI Governance



These challenges are interdependent and can influence one another in a circular fashion. For example, to strengthen farmers' negotiating positions and give them more options, the state needs to reduce its involvement in the contract-making process and increase the level of competition among traders and investors. To bring in more and higher-quality traders and investors, however, we also need to work on improving the investment climate.

These connected issues call for a multi-level approach that can address them simultaneously (farmer groups need to be strengthened at the village level, whereas improving the business environment and strengthening economic liberalization involve policy dialogues).

6. Program Design and Feasibility

6.1 Overall objective and approach

In this section I design program activities based on the assessment of FDI related issues above. The overall objective of these activities is to ensure farmers benefit from increased FDI in agriculture and to promote private investments in the sector. The approach is to devise multi-leveled interventions that involve multiple stakeholders. This component will work at the central and provincial levels to facilitate policy dialogues on reducing state involvement in contract-farming and trading arrangements. It will also work at the district and village levels to facilitate investor farmer interactions. In addition to working with line agencies and villagers, the program will work with the private sector ***directly***. Most of the activities contribute to the 'Agriculture Production and Marketing – Commercialization' element of the CCP. Activities are organized according to expected results in the following five aspects:

- **Expected Result 1: Reduced state control; expanded options for farmers.**
- **Expected Result 2: Farmers' negotiating positions strengthened.**
- **Expected Result 3: Increased cooperation with the private sector.**
- **Expected Result 4: Improved appraisal and monitoring of FDI.**
- **Expected Result 5: Improved investment climate, and investment promotion strengthened.**

6. 2 Interfacing with other program areas

It should be noted that FDI as a contextual topic intersects with a number of other components of CCP. It is difficult for this portion of the design to address all these connections thoroughly. Agricultural FDI's implications for land management (through concessions or contract farming) will be addressed in the Land and Natural Resource Management component of the CCP. There may also be overlap with activities in Value Chain Development, Village Networks, and Governance and Planning.

6.3 Detailed Activities

<u>Expected Result 1: Reduced state control; expanded options for farmers</u>

Activity 1: Remove artificial trader monopolies by piloting "open marketing" zones.

An open marketing zone is where the government does not intervene in contract farming schemes or allocate market shares to traders. Contracts are signed directly between farmers and buyers based on mutual and voluntary agreement without state interference. Note that this is not related to the concept of Special Economic Zones or Free Trade Zones granted only through the authority of the Prime Minister's Office.

These small "open marketing" zones are local experiments requiring no adjustments to or exemptions from existing laws and regulations on trade and investments. This activity is designed to demonstrate the potential benefits of reducing state intervention in contract-making, allowing more buyer competition, and expanding farmers' economic choices. Specifically, this activity involves the following tasks:

- Hold workshops with PAFO/DAFO, DOIC and DPI to discuss market principles and potential gains for farmers through increasing buyer competition. This is an exercise to communicate the rationale of the pilot to relevant authorities as well as to enhance their understanding and awareness of market principles.

- In consultation with line agencies, select the pilot zone. An ideal pilot location should be geographically accessible and possess a number of active or potential traders in annual crops (perennial crops are associated with long contract durations. Implementing the pilot may imply breaching existing contracts).

- In cooperation with relevant line agencies, hold workshops/meetings with existing and prospecting traders or investors to communicate the rationale and content of the pilot experiment. As traders/investors' current contracts expire, the province/district will no longer play a role in renewing them. Contracts will then be signed directly between farmers or farmer groups and traders with no pre-designation by the government. The role of the government will be limited to renewing business licenses and other administrative tasks.

- Develop mechanisms for monitoring the progress of this marketing pilot and a knowledge capitalization process.

Risks/Assumptions: There can be a lack of will from both line agencies and businesses to support this pilot as it is to the traders' advantage to maintain artificial monopolies through the government. To demonstrate maximum impact, it is important that this activity, which removes institutional barriers, be implemented simultaneously with other activities that facilitate direct linkages between farmers and the private sector. In the early stage there may also be a period of relative chaos as farmers learn to negotiate increased market options. Some farmers will be cheated; some will ignore contracts they signed when a better offer comes along. However, this provides a learning process for farmers.

Activity 2: Refine the contract-making process for new investments in agriculture.

On a larger scale, the top-down contract-making approach may not be changed entirely overnight (institutional inertia and resistance by interest groups). Therefore, in addition to experimenting with the (more drastic but small) open marketing pilots (Activity 1), it is important to facilitate incremental refinements of the overall approach to reduce state control gradually:

- Facilitate repeated policy dialogues with line agencies on reducing the state's role in making economic decisions and specifically in orchestrating top-down contract farming/trading arrangements.

- Remove specific conditions such as land allocation (e.g. specific number of hectares) and profit sharing percentages from the higher-level contracts (these conditions should be decided by the farmers and investors through direct negotiations).
- Develop mechanisms for thorough consultation with villagers. Ensure consistent understanding of contract conditions among all parties.
- Require agreements be signed with villagers directly.
- Eventually phase out governmental contracts.

Risks/assumptions: The implementing agent for the villager consultation process must maintain neutrality. It will jeopardize the activity if the implementing agent simply becomes a paid agent representing traders/investors' interests.

Activity 3: Facilitate direct interactions between farmers and investors/traders. Enhance farmers' participation in market opportunities (see also the Value Chain Development Working Paper of CCP).

- Facilitate regular trader-farmer meetings.
- Organize market study tours for farmers and farmer groups.
- Facilitate farmer groups' participation in trade fairs.

Expected Result 2: Farmers' negotiating positions strengthened.

Activity 4: Facilitate and support the formation of farmer groups (see also the Value Chain Development Working Paper of CCP):

Lessons Learned 1: Ban Had Ngao's Farmers' Association

The idea of organizing farmer groups and producer groups is far from new. In the Lao northern uplands there is one such homegrown example of success, Ban Had Hgao. Had Hgao is a Hmong village in Luang Namtha Province that has planted rubber since the mid 1990s in the form of a farmer's association. The association is self-organized, has a revolving fund (which began initially with a governmental loan), and is managed by educated, respected village elders. Villagers conducted several market study tours to China on planting techniques as well as marketing channels. Latex sale is organized and made to a number of middle agents and to Chinese processing factories directly. Villagers are well informed about market prices through their established business networks. When a Chinese investor built a preliminary processing facility in the vicinity of Had Ngao, villagers didn't sell any latex to the facility due to the lower collection prices. The association eventually procured the facility from the investor, who had to abandon it due to the lack of latex supply. Had Ngao's example serves to illustrate how farmers' positions are strengthened significantly when they organize and have access to an open market as well as credit.

Activity 5: Enhance farmer's and farmer groups' capacity for understanding, interpreting, and developing contracts and skills for negotiation. Specifically, this activity involves:

- Ensure understanding of the basic elements of a contract and what it means to sign a contract.
- Develop a checklist of considerations for farmers when presented with a contract proposal by investors, traders, or the government (e.g. collection time, quantity, minimum price, quality specification).
- Develop a simple contract template that farmers/farmer groups can use to initiate their own negotiations with potential traders and investors.
- Conduct training on negotiation skills (may also include training in languages).
- Conduct training on dealing with contract violations by traders and investors through mediation.
- Facilitate peer learning and exchange of experiences among villagers in negotiating with traders/investors.

Risks/Assumptions: this activity will have the most impact when combined with successful efforts in reducing the top-down approach in contract-making and achieving greater and more direct interactions between farmers and investors/traders.

Lessons Learned 2: Model Contracts
The Lao Extension for Agriculture Project (LEAP) has prepared a model contract to strengthen farmers' negotiating positions in contract farming schemes. Other organizations including GTZ have made similar efforts. However, these model contracts have achieved very little use by the communities. The lack of their impact results from: 1) contract scenarios are extremely diverse. It is impossible to develop one model contract to suit all situations (e.g. for annual vs. perennial crops, for contracting with traders vs. an investor with significant levels of input). 2) Under the top-down contract-making approach, farmers are seldom involved in the contract negotiation process. Past experiences in developing model contracts demonstrate that activities in refining the technical aspects of the contracts are unlikely to be effective on their own. They must be combined with facilitating changes in the governing institutions and be they must be flexible enough to adapt to the diverse situations farmers face.

Activity 6: Enhance farmer's and farmer groups' awareness of risks in commercial production. This activity is designed to ensure farmers make informed decisions regarding risks. In current community consultation mechanisms, farmers' access to information is incomplete. The crops are promoted without disclosing the associated risks as well as benefits.

- Conduct a study to assess market risks associated with certain commercial crops and their implications for farmers' livelihoods.
- Conduct training on appraising risks in the context of farmers' livelihood systems and mitigating risks through diversification.
- Raise awareness that risks should be a consideration in contract negotiations. Risks should be shared between contracting parties.
- Organize knowledge sharing workshops and study tours.

Risks/assumptions: same as above.

Activity 7: Develop a neutral conflict mediation process and related facilities. Current dispute resolution, when it occurs, is facilitated through a committee of relevant line agencies including PAFO, DPI, DOIC, and PLMA (in Huaphanh, however, this process is coordinated through the Chamber of Commerce). Because of the holistic, multi-faceted role governmental agencies play in agricultural investment projects (pg. 9), it is difficult to ensure fair resolution of the disputes. This activity involves:

- Conduct study to review existing conflict resolution process and capacity.
- Develop and pilot a regular process for resolving disputes at the district and provincial levels.
- Document successful and unsuccessful cases of dispute resolution for experience sharing.

Risks/assumptions: Neutrality is difficult to ensure unless governmental interests and business interests can be untangled.

Expected Result 3 Increased cooperation with the private sector in select initiatives.

Activity 8: Work with select investors to demonstrate appropriate production technologies. There are a number of demonstrations established by foreign investors in the northern region for commercial crops.[13] They are exclusively mono-cropping plantations. This activity aims to work with select investors to improve upon their existing practices. Specifically,

- Ensure the existing demonstrations established by private investors are technically sound.
- Dialogue with investors about demonstrating alternatives to mono-crop technologies and provide them with necessary technical and financial support in demonstrating alternative techniques.
- Facilitate and provide necessary support to small private investors in disseminating production technology to farmers both within and outside contract farming schemes.
- Develop monitoring mechanisms to hold the private sector accountable in delivering proper technical extension.

Risks/assumptions: Lack of investor interest. Selection of the "right" investors and providing them with economic incentives can be paramount. Note also that this is not to promote a new, parallel extension system to PAFO/DAFO services. In most contract farming schemes, particularly for perennial crops, investors are already providing (or required to provide) technical input.

Activity 9: Work with select investors and farmer groups in developing medium to advanced processing facilities for high value, niche products (e.g. tea processing):

- Support feasibility and market studies.
- Work with select investors to scale up their existing facilities and marketing channels (e.g., for tea processing: higher quality standards, greater product differentiation, and enhanced packaging and marketing strategies).

[13] One may argue the real intent for these demonstrations is but to secure small plots of conessions.

- Ensure that the added benefits from scaling up are shared between farmers and investors. Facilitate negotiation and cooperation between farmer groups and the investors. Support farmer groups in the negotiation process.
- In exchange for technical and marketing support offered to investors, develop mechanisms for holding investors to a higher level of socioeconomic and environmental conduct.

Risks/assumptions: The global economic downturn makes it difficult to seek out marketing opportunities. However, this is also a good time to invest in niche processing because farmers and traders will have fewer opportunities in selling unprocessed bulk commodities in the coming years while niche, high quality products are more resistant to commodity market fluctuations. As is in the previous activity, it is important to cooperate with investors selectively by focusing on smaller investors committed to long-term business prospects.

Lessons Learned 3: Phoufa Tea Factory

Phoufa Tea Factory in Phongsaly District, Phongsaly Province, is run by a Chinese investor who began planting tea with local villagers in 1999. The investor started with 9 ton annual production and has now expanded to an annual yield of 150 tons of organic tea from 850 ha of plantations. The bottleneck the factory faces now is in workshop upgrading and product packaging and marketing. The investor has sold tea to as far as Japan and Germany, but this is done through several layers of middle agents as the factory 1) does not possess direct marketing channels; 2) lacks the capacity to improve product packing to appeal to high-end consumers; 3) the basic conditions of the processing facility cannot pass the certification and inspection requirements of these developed economies. Cases like Phoufa Tea Factory present good opportunities for direct cooperation between a donor project and the private sector in a market-based approach. In providing support to upgrade this factory, the project can, as part of the conditions, facilitate greater involvement of farmers and farmer groups in value adding activities so that this proves a win-win situation for all. Such practice takes advantage of and expands upon the existing production, processing, and marketing infrastructure and is therefore both effective and cost-saving.

Lessons Learned 4: **Working with a Rubber Investor**

Lao Jin Se, a Chinese rubber investor in Bokeo, has been working with the local communities since the late 1990s. In 2008 the investor expressed interest in building a latex processing facility, but lacked technical capacity in setting up the operation. The GTZ Rural Development in Mountainous Area Program and CIM Regional Planning, based in Bokeo, took the opportunity to offer Lao Jin Se technical support. This provides a pathway for the donor project to encourage higher environmental standards in establishing the facility. Lao Jin Se, GTZ, and Bokeo DPI have signed a tri-party agreement to hold the rubber company to codes of conduct (However, GTZ has since left the province due to the end of a project phase). Lao Jin Se provides another example where a donor project can work with foreign investors directly to improve their conduct based on mutual needs and benefits.

Expected Result 4. Improved appraisal and monitoring of FDI

Activity 10: Improve capacity for appraising investment proposals, with increased consideration for social and environmental implications:

- Develop measurable criteria for appraisals.
- Build staff capacity at MPI/DPI, MAF/PAFO, and other relevant agencies and conduct training in investment appraisals.

Risks/assumptions: Potential corruption in the decision process will compromise the impact of this activity.

Activity 11: Develop a vertically and horizontally integrated tracking system for investment application and approval. This activity is designed to enhance inter-agency as well as cross-level coordination. It also enhances transparency of the decision process.

- Review current channels in cross-departmental and cross-level information sharing on FDI approval.
- Based on this assessment, develop a database system where the status of an investment project can be accessed and reviewed by all agencies (e.g., currently under review by MAF, decision to be made on XX date) at multiple levels (central and provincial).
- Allow flexibility in the application to accommodate potential changes in agency responsibilities (e.g. the new Enterprise Law, though implemented to a very limited extent thus far, is expected to reallocate much of the licensing responsibility from MPI to MOIC through automatic registration. Ongoing revisions in the Investment Law will also redefine the roles of MPI and relevant agencies).
- Allow capacity to expand the application to also track monitoring and evaluation results.
- Procure necessary computer equipment, staff capacity, and conduct staff training at relevant line agencies.

Risks/assumptions: Lack of institutional will for vertical and horizontal information sharing. Ongoing changes in investment and enterprise regulations also present institutional uncertainty.

Activity 12: Strengthen monitoring and evaluation of private investors.

- Review current process for the M&E of public investments for examples of good practices (e.g. PCAP project implemented through MPI).
- Develop procedures and measurable criteria specifically for monitoring private investments.
- Develop mechanisms to translate M&E results to accountability (e.g. penalty and reward systems based on the enforcement of contract conditions, compliance to environmental standards etc.).
- Procure necessary equipment, staff capacity, and conduct staff training.

Risks/assumptions: Institutional corruption will limit the impact of this activity.

Expected Result 5: Improved investment climate, and investment promotion strengthened.

Activity 13. Develop provincial strategies in attracting FDI.

- Policy dialogue on the comparative advantages of the province and provincial development priorities.
- Develop provincial level investors' guide in multiple languages and for different sectors (within CCP, only for the agriculture sector).
- Attend regional trade fairs to promote the province's potential (note however that this potential may not be best represented by agriculture).

Activity 14. Facilitate regular public-private dialogue at the provincial level to discuss constraints faced by the private sector (e.g. cumbersome import-export procedures, rampant informal charges etc.)

> **Lessons Learned 5: Public Private Dialogue**
> In many ways the Public Private Dialogue, being piloted by the GTZ HRDME program in Luang Namtha, Luang Prabang, Savannakhet and Champassak, is as much about discussing the content as it is about institutionalizing a process, an "open" communication channel between the government and the private sector. The Dialogue is being expanded further in 2009 to Xiekhuang and Huaphanh. This is a collaborative initiative between MPI, LNCCI, and their associated local offices. In building upon this existing practice, the Program should enhance the participation of foreign investors and particularly SMEs. Both groups are currently under-represented in the dialogue process.

Activity 15. Strengthen the Chamber of Commerce and associated provincial offices to:

- Advocate for the needs and concerns of the private sector (e.g. simplify import/export procedures, reduce informal charges etc.)
- Establish investor protection and mechanisms to address investor complaints (focusing on small to medium enterprises)

Other activities: Improving the investment climate is a broad target requiring multi-faceted interventions beyond the scope of CCP. See Section 6.7 for additional activities and possible partners in improving the investment climate.

6. 4 Implementation

The activities will be carried out through relevant line agencies (MAF, MPI, LNCCI and their associated provincial offices and applicable district offices), Technical Assistance, and project staff. In addition to several task-specific specialists (Value Chain, Database, Mediation, M&E) to be procured as needed, two types of full-time project staff will facilitate and coordinate the implementation of most activities:

An **International Advisor on Private Sector Development** will be responsible for policy dialogues on reducing the role of the state (Activities 1-2) and improving the investment climate (10-12) and play a coordinating and facilitating role in cooperation with the private sector (Activities 8-9) and in strengthening the monitoring of FDI (Activity 14). This full-time, long-term position will be split among 3 pilot provinces. It is STRONGLY RECOMMENDED that this TA be NOT broken into short-term consulting procurements as it takes a substantial amount of time to establish trust and rapport with governmental as well as private sector counterparts in order to facilitate effective policy dialogues and institutional changes.

Marketing Facilitators will be based in all 9 districts to carry out activities on facilitating direct interactions between investors and farmers and in strengthening farmers' bargaining positions (Activities 3-6). Similarly, it will be important to minimize staff turnover in these positions (possibly by offering a performance-based wage premium) as it is time-consuming to build relationships and rapport.

Program implementation should allow flexibility in adjusting to local situations. For example, efforts to eliminate artificial trader monopoly would be irrelevant in extremely isolated communities where there are few traders to begin with.

Certain activities may propose challenges for the current funding mechanism. To finance direct cooperation with the private sector (e.g. Activities 8-9), it will be inappropriate to channel associated funds and resources through MAF. It is highly recommended that parallel funds be made available for these activities.

Section 6.5 provides further information on specific implementation responsibilities.

6.5 Design Summary

CCP Agricultural Produciton and Marketing - Commercialization

			Target/Indicator	Implementing Responsibility
Expected Result 1: Reduced state control; expanded options for farmers				
	Activity 1	Remove artificial trader monopolies by piloting “open marketing” zones	1 zone per province	PAFO/DAFO, Intl Advisor on Private Sector Development
	Activity 2	Refine the contract-making process for new investments in agriculture	Direct contracts between villagers and investors	PAFO/DAFO, DPI, Intl Advisor on Private Sector Development
	Activity 3	Facilitate direct interactions between farmers and investors/traders. Enhance farmers’ participation in market opportunities	Regular farmer-trader meetings held in all 9 districts; study tours for farmers in all 9 districts at least once per year	Marketing Facilitator
Expected Result 2: Strengthen farmers’ negotiating positions.				
	Activity 4	Facilitate and support the formation of farmer groups	Farmer groups held in all 9 districts	Marketing Facilitator
	Activity 5	Enhance farmers and farmer groups’ capacity for understanding, interpreting, and developing contracts and skills for negotiation	Training held in 9 districts	Marketing Facilitator
	Activity 6	Enhance farmers and farmer groups’ awareness of risks in commercial production.	Training held in 9 districts	Marketing Facilitator
	Activity 7	Develop a neutral conflict mediation process and related facilities.	Process developed	Marketing Facilitator + Mediation Specialist
Expected Result 3: Increased cooperation with the private sector in select initiatives.				
	Activity 8	Work with select investors to demonstrate appropriate production technologies	1 pilot	Intl Advisor on Private Sector Development

Expected Result 4: Improved investment climate and investment promotion strengthened.			
Activity 10	Develop provincial strategies in attracting FDI	Policy dialogue in 3 provinces	DPI, Intl Advisor on Private Sector Development
Activity 11	Facilitate regular public-private dialogue at the provincial level to address constraints faced by the private sector	Policy dialogue in 3 provinces	Chamber of Commerce, Intl Advisor on Private Sector Development
Activity 12	Strengthen the Chamber of Commerce and relevant provincial offices		Chamber of Commerce, Intl Advisor on Private Sector Development

CCP Other

Expected Result 5: Improved appraisal and monitoring of FDI			
Activity 13	Improve capacity for appraising investment proposals	Process developed, staff trained	MPI/DPI, MAF/PAFO, + TA support
Activity 14	Develop a vertically and horizontally integrated tracking system for investment application and approval.	Syestem developed and tested, staff trained	MPI/DPI, Database Specialist, Intl Advisor on Private Sector Development
Activity 15	Strengthen monitoring and evaluation of private investors	Process developed, staff trained	MPI/DPI, MAF/PAFO, + TA support

6.6. Activity Costing

CCP Agricultural Produciton and Marketing - Commercialization

		Cost Items	Unit	Unit Cost (euro)	2009	2010	2011	2012	sum (euro)
Activity 1	Remove artificial trader monopolies by piloting “open marketing” zones	TA (PSDA)	p/months	15,000	2	2	2	2	120,000
		workshops	lump sum	3,000	1	1	1	1	12,000
		car	lump sum	30,000	1				30,000
		fuel and other travel	lump sum	2,500	1	1	1		7,500
Activity 2	Refine the contract-making process for new investments in agriculture	TA (PSDA)	p/months	15,000	1	1	1	1	60,000
Activity 3	Facilitate direct interactions between farmers and investors/traders. Enhance farmers’ participation in market opportunities	Marketing Facilitator	lump sum (9 districts)	5,000	9	9	9	9	180,000
		study tours/ trade fair	lump sum (9 districts)	2,000	9	9	9	9	72,000
		Motorbikes (1 per district)	lump sum (9 districts)	2,500	9				22,500
		fuel for motorbike	lump sum (9 districts)	1,000	9	9	9	9	36,000
Activity 4	Facilitate and support the formation of farmer groups	Personel and equipment already accounted for in Activity 3							-

6.6 Activity Costing (Cont'd)

		Cost Items	Unit	Unit Cost (euro)	2009	2010	2011	2012	sum (euro)
Activity 5	Enhance farmers and farmer groups' capacity for understanding, interpreting, and developing contracts and skills for negotiation	Trainers, training sessions	lump sum (9 districts)	1,000	9	9	9	9	36,000
Activity 6	Enhance farmers and farmer groups' awareness of risks in commercial production.	Trainers, training sessions	lump sum (9 districts)	1,000	9	9	9	9	36,000
Activity 7	Develop a neutral conflict mediation process and related facilities.	Mediation Specialist (national)	p/months	1,400	3	3	2	1	12,600
Activity 8	Work with select investors to demonstrate appropriate production technologies.	TA (PSDA), TA (Agriculture)	p/months	15,000	1.5	1.5	1.5	1.5	90,000
		Equipment and other resource	lump sum	20,000	1	1	1	1	80,000
Activity 9	Work with select investors (and farmer groups) in developing medium to advanced processing facilities for high value, niche products.	TA (PSDA), TA (Value chain)	p/months	15,000	1.5	1.5	1.5	1.5	90,000
		Equipment and other resource	lump sum	50,000	1	1	1	1	200,000

6.6 Activity Costing (Cont'd)

		Cost Items	Unit	Unit Cost (euro)	2009	2010	2011	2012	sum (euro)
Activity 10	Develop provincial strategies in attracting FDI	TA (PSDA)	p/months	15,000	2	2	2	2	120,000
		Materials	lump sum (3 provinces)	1,500	3	3	3	3	18,000
		Workshops	p/months	3,000	3	3	3	3	36,000
Activity 11	Facilitate regular public-private dialogue at the provincial level to address constraints faced by the private sector	TA (PSDA)	p/months	15,000	1	1	1	1	60,000
		Workshops	lump sum (3 provinces)	3,000	3	3	3	3	36,000
Activity 12	Strengthen the Chamber of Commerce and relevant provincial offices	TA (PSDA)	p/months	15,000	3	3	3	3	180,000

CCP Other

		Cost Items	Unit	Unit Cost (euro)	2009	2010	2011	2012	sum (euro)
Activity 13	Improve capacity for appraising investment proposals	TA (appraisal)	p/months	15,000	2	2	1	1	90,000
		Training	lump sum (3 provinces)	3,000	3	3	3	3	36,000
Activity 14	Develop a vertically and horizontally integrated tracking system for investment application and approval.	Equipment for MPI/DPI	lump sum (3 provinces)	4,000	3				12,000
		TA (database)	p/months	15,000	3		1		60,000
		training	lump sum (3 provinces)	3,000	3	3	3	3	36,000
		TA (PSDA)	p/months	15,000	1	1	1	1	60,000
Activity 15	Strengthen monitoring and evaluation of private investors	TA (M&E)	p/months	15,000	1	1	1	1	60,000
		training	lump sum (3 provinces)	3,000	3	3	3	3	36,000
Note: PSDA=Private Sector Development Advisor (12 pmonths/yr position allocated acdross activities)									1,924,600

6.7 Working toward PBA: Broaden the Sectoral Focus

FDI is a contextual topic. In working toward PBA, the current focus on agricu FDI should be broadened to consider

- FDI in all sectors
- The greater context of private sector development.

6.7.1 FDI in all sectors

FDI in hydroelectric generation accounts for 48.1% of the total foreign invest value since 2000 while mining accounts for 10.5% (MPI 2008 data). Major p hydro and mining (e.g. Nam Theun 2) have been dominant economic drivers country in the last few years. Excluding the contribution of mega resource pr GDP growth has in fact slowed since 2006. The resource sector contributes around 20% of total governmental revenue and accounts for over 60% of tot (World Bank, 2008c).

Of the 26 power projects under construction or in the planning phase current (totaling 5,670 MW) are in the northern region, accounting for 58% of the tot capacity (MEM, 2009). Of the 156 mining sites currently in production or und exploration, 96 are in the north corresponding to 1.3 million ha in area (72% country total) (MEM, 2007). The significance of the resource sector in the no economy should not be neglected.

Hydro and mining projects present different challenges for local livelihoods t investments in agriculture, which tend to be smaller in scale and pose less p threats to land rights. In the northern uplands, a vast majority of agricultural channeled through contract farming rather than concession (though one may the so-called "1+4" contract farming scheme is no different from concession essence). Compared to agricultural development, mega resource projects br significant revenue to the governments, but have a much harder time transfe direct benefits to the local communities. Mega projects also cause more imm environmental and social repercussions than smaller, more incremental com agricultural developments.

In certain areas, non-agricultural investments can out-compete the agricultur in attracting and retaining funds (Luang Prabang and Huaphanh for example suggests the possibility that in these areas commercial agricultural developm important component of CCP) may not be to their best comparative advanta worth considering development alternatives outside agriculture or niche prod and marketing to distinguish these areas from the commercial production hu as Oudomxai and Luang Namtha.

6.7.2 Private sector development

This document narrowly touches on the subject of improving investment clim the context of agricultural commercialization. However, improving the busine environment and enabling private sector development (domestic investment as FDI) requires a much broader approach. This design component has not addressed, but only built in possibilities for change through proposed policy dialogues, the wide range of issues impeding the private sector in the northe upland area. Additional important issues in the broader PBA include:

- Cumbersome business registration and licensing procedures
- Complicated export procedures and long waits at border inspection
- Low labor productivity and a poorly trained labor force
- Lack of infrastructure and high transportation costs
- Lack of a property system
- Underdeveloped financial services
- Un-transparent tax administration
- Poor contract enforcement

There are a number of current donor initiatives engaged in promoting private sector development in Lao PDR, funded by ADB, EC, Germany, Japan, SNV, and the World Bank Group (IFC and World Bank). Of these, the work of the International Finance Corporation-Mekong Private Sector Development Facility (IFC-MPDF) is particularly wide ranging and covers comprehensively areas related to private sector development. IFC-MPDF is also a multi-donor initiative jointly funded by 12 donor agencies. Its work pertains to improving the business environment, increasing access to finance, improving environmental and social sustainability in private firms, increasing value added in specific supply chains, and increasing private sector access to infrastructure.

MPDF's most noted work to date in Lao PDR is the development and promulgation of the new Enterprise Law. To streamline business registration, the Law requires a change from the current government practice of requiring all businesses to obtain approval from relevant line ministries before registering to a system where firms are registered automatically through MOIC (unless the proposals are highly sensitive and qualify for the Negative List) and monitored subsequently by sectoral agencies (LNCCI, 2007). However, the Law has been implemented to a very limited extent in practice, partly because it conflicts with existing laws on foreign and domestic investments (currently under revision). The existing investment laws require business applications be directed through the Committee for Promotion and Management of Investments (CPMI) under MPI. MPI and CPMI hence remain the first point of contact for investors as well as the final approver in practice. Replicating the process of developing the new Enterprise Law, MPDF is also facilitating new finance sector legislation.

Another notable program in private sector development is the HRDME program of GTZ. In addition to facilitating public private dialogues on constraints facing the private sector and promoting vocational training, HRDME has supported the "One-Stop Shop" service through CPMI. This work is now left in uncertainty with the promulgation of the Enterprise Law and the subsequent, impending revisions to the investment laws. It is suggested that MPI may still retain jurisdiction over investment activities in the promoted zones and sectors in spite of the Enterprise Law. Apart from GTZ, JICA also supports MPI in investment promotion and MOIC in the promotion of trade.

Based on the current institutional and legislative uncertainties in the governance of investment procedures, streamlining these procedures, though noted in the consultant's ToR, was not proposed as part of CCP. This activity was not deemed feasible as one can accomplish very little at the provincial level when the ministerial roles are being redefined and legislation changed. The uncoordinated donor efforts in this case attest to the advantage of PBA, where multiple donor initiatives may be brought together in the future in addressing broad based issues such as private sector development. Going forward, it should be a priority to resolve conflicting laws and continue simplifying business registration and licensing. It is equally important to improve contract law and contract enforcements, as it is a crucial factor for attracting investors committed to maintaining a long-term interest in Lao PDR.

Annex 1 List of Acronyms

ADB	Asian Development Bank
CCP	Core Coherent Program
DAFO	District Agriculture and Forestry Office
DPI	Department of Planning and Investment
EC	European Commission
FDI	Foreign Direct Investment
GoL	Government of Lao PDR
GTZ	German Technical Cooperation
HRDME	Human Resource Development for Market Economy
IFC	International Finance Corporation
LEAP	Lao Extension in Agriculture Project
LNCCI	Lao National Chamber of Commerce and Industry
M&E	Monitoring and Evaluation
MAF	Ministry of Agriculture and Forestry
MEM	Ministry of Energy and Mines
MOIC	Ministry of Industry and Commerce
MPDF	Mekong Private Sector Development Facility
MPI	Ministry of Planning and Investment
NGPES	National Growth and Poverty Eradication Strategy
NTFP	Non-Timber Forest Product
NUSDP	Northern Upland Sustainable Development Program
PAFO	Provincial Agriculture and Forestry Office
PBA	Program Based Approach
PCAP	Project for Capacity Building in PIP Management
PIP	Public Investment Project
PLMA	Provincial Land Management Authority
PSDA	Private Sector Development Advisor
SNV	Netherlands Development Organization
TA	Technical Assistance

Annex 2 References

Caroline Ashley, 2006. Participation by the poor in Luang Prabang tourism economy: Current earnings and opportunities for expansion.

GTZ, 2007. FDI SME Linkages: Two Case Studies.

LNCCI, 2007. Business Issues Bulletin, No.4.

World Bank, 2007. Lao PDR Key Indicators

World Bank, 2008a. Lao People's Democratic Republic: Policy, Market, and Agriculture Transition in the Northern Uplands.

World Bank, 2008b. Doing Business 2009: Country Profile for Lao PDR.

World Bank, 2008c. Lao PDR Economic Monitor.