

**COMBINED PROJECT INFORMATION DOCUMENTS / INTERGRATED
SAFEGUARDS DATA SHEET (PID /ISDS)**

ADDITIONAL FINANCING

Report No.: 107904

Date Prepared/Updated: July 22, 2016

I. BASIC INFORMATION

A. Basic Project Data

Country:	Lao People's Democratic Republic	Project ID:	P159060
		Parent Project ID:	P130512
Project Name:	AF - Lao PDR Second Trade Development Facility Project		
Parent Project Name:	Lao PDR Second Trade Development Facility Project		
Region:	EAST ASIA AND PACIFIC		
Estimated Appraisal Date:	August 28, 2016	Estimated Board Date:	September 29, 2016
Practice Area (Lead):	T&C	Lending Instrument:	Investment Project Financing
Sector(s):	General industry and trade sector (50%), Other domestic and international trade (25%), Public administration - industry and trade (25%)		
Theme(s):	Trade facilitation and market access (30%), Regional integration (25%), Export development and competitiveness (25%), Legal institutions for a market economy (10%), Other Private Sector Development (10%)		
Borrower(s)	Ministry of Finance		
Implementing Agency	Ministry of Industry and Commerce		
Financing (in USD Million)			
Financing Source			Amount
BORROWER/RECIPIENT			
International Development Association (IDA)			4
International Bank of reconstruction and Development (IBRD)			
Others			12.2
Financing Gap			
Total			16.2
Environmental Category	C-Not Required		
Decision	N/A		

Other Decision (as needed)	N/A
Is this a Repeater project?	no

B. Introduction and Context

1. Lao PDR has enjoyed annual GDP growth averaging over 7 percent throughout the two decades to 2014, enabling the country to halve its poverty rate and multiply per capita incomes.

During the period 1992 – 2013 the poverty headcount fell from 46 percent to 23 percent while per capita GDP rose from US\$ 227 in 1990 to US\$ 1,600 in 2014,¹ a more than seven-fold increase. Lao PDR attained lower middle-income country status in 2012 and real GDP is expected to grow at average annual rate of 7 percent from 2016-2020. However, high economic growth has been accompanied by a less than proportionate decline in poverty and rising inequality. While poverty declined from 33.5 percent in 2002/03 to 23.2 percent in 2012/13, the elasticity of poverty reduction to economy growth is less than unity. For every 1 percent increase in GDP, poverty has fallen by approximately 0.47 percent. This uneven trend suggests that the benefits of economic growth are not translating into shared benefits for all and in some cases may have widened inequality.

2. As part of this strong growth, the Lao economy has gone through a rapid structural shift from agriculture to natural-resource based economy.

The share of natural resource-based sectors to GDP almost tripled between 1998 and 2010, increasing from 5.9 percent in 1998 to 16.1 percent in 2010. The share of non-tradables (services) to GDP grew more moderately, driven by increases in tourism and trade in recent years as well as an expansion in infrastructure construction. Similarly, manufacturing (garments, wood and wood products, construction materials, light manufacturing, handicrafts, and, increasingly, food, beverages and related processing) as a share of GDP has also expanded, but at a relatively slower rate. These non-resource sectors remain critical to creating more job opportunities and moving people out of poverty. However, growth in these sectors has been modest relative to potential largely due to a complex business environment that hampers private sector operations. According to the Investment Climate Assessment from 2014, deeper investment climate reforms will be necessary to unlock the full potential of the Lao economy, to attract higher quality private sector investment in a wider range of diversified sectors, and to benefit more fully from natural resource development spillovers.

3. The country is located within a region that includes some of the most dynamic and fastest growing economies in the world,

and it has benefited significantly from growing external demand for goods and services as well as increased inflows of foreign direct investment. However, to more strongly benefit from these regional market opportunities, a number of challenges in the business environment will still have to be addressed. Given its small size, investments into Lao PDR (outside the natural resource sector) will be largely efficiency seeking. For this type of investment investors are particularly looking for a transparent, dynamic and streamlined business environment (and trade environment) as they compare alternative investment locations. It will therefore be particularly important for Lao PDR to improve the business environment to compensate for the natural disadvantages the country faces as a land-locked economy.

4. In fact, Lao PDR's growing dependence on the natural resource sector has tended to erode national competitiveness in sectors that have the potential to create jobs and reduce poverty in the long term.

While the natural resource sector has been the key driver of economic growth in recent years and has led to high rates of foreign investment, the positive spillovers from this growth have largely been limited to an expansion in the services and constructions sectors. While important, these sectors will not

¹ Lao PDR Economic Monitor, The World Bank.

generate the kind of employment growth needed to absorb the estimated 900,000 new job seekers joining the workforce in the next decade². This suggests that urgent attention needs to be directed toward reforms that have the potential to support growth in the non-natural resources sector, particularly in agriculture and manufacturing but also the services sectors. It is in these sectors where most employment is likely to be generated over the short to medium term that could contribute to broad-based income growth and contribute to achieving the twin goals. Agriculture alone currently accounts for 75 percent of Lao PDR's entire workforce.

5. Importantly, strong economic growth has tended to mask the costs and constraints imposed on business of a still largely unreformed business and investment environment. The difficult business environment in Lao PDR (ranked 134th out of 189 economies on the 2016 Ease of Doing Business ranking) generates significant costs for new investments as well as the expansion of existing ones. The overall ranking, and a particularly low ranking for 'starting a business' (153) and 'paying taxes' (127) directly affecting business operations, further suggests that the few improvements made have resulted in an overall pace of reform far too slow to make a meaningful difference. The 2016 Enterprise Survey data further points to the challenges in the business environment. While trade indicators continue to improve the time to obtain operating licenses in the manufacturing sector has been increasing since 2009 and now takes longest for small enterprises. External reform commitments (under the WTO and ASEAN) have driven reforms in some areas, such as tariff and service trade liberalization, rationalization of non-tariff measures (NTMs), as well as improvements in trade facilitation and border management systems. As a result, constraints in the business environment have become relatively more important for the private sector.

6. Available analytical work, consultations with the private sector, and data indicate that the business environment remains complex and risky, negatively affecting investment flows into the non-resource sectors. Laws and secondary legislation on regulatory requirements is frequently unavailable despite recent modernization in many areas (notably as part of the WTO accession), and clear procedures on how to meet such requirements are absent. Business licensing is still largely manual and paper-based, transactions are not standardized and require face-to-face interactions. Coordination among Ministries is not fully formalized, generating high transaction costs and drawn-out processes. Together with a broadening gap between the "law in the books" and the "law in practice" (de jure/de facto gap) as well as a lack of predictability (resulting from significant divergence in the interpretation and enforcement of the same rules by different line ministries and by provincial authorities), this regulatory uncertainty function as barriers to business entry and operation—and undermine the confidence of the private sector. Anecdotal evidence indicates that compliance with regulations can be avoided, or processes be accelerated, by informal means. While large companies might be able to navigate such an environment (characterized by negotiation and discretionary decisions), it particularly places burden on smaller, including women-owned, companies and new entrants that might not have established relationships, complicating new entry and reducing competition in the market.³ Business registration as well as complex and opaque sector-specific business licensing requirements are frequently reported as key constraints facing SMEs.

7. Improving the business and investment regime will require consistent and comprehensive reforms and will be critical to diversifying sources of growth and facilitating investment, especially in the context of the ASEAN Economic Community (AEC). Improving the environment for starting and operating businesses would have to consist of increasing transparency (including regarding taxation), simplification of regulatory requirements, reducing policy restrictions on market entry, and increasing consistency and predictability of how existing rules and procedures are applied in practice. It would remove restrictions on market entry and levelling the playing field between new, existing, formal, and

² Lao PDR Systematic Country Diagnostic, The World Bank, 2016.

³ The increased use of concession agreements (case by case negotiation of discretionary package of incentives) in multiple sectors and by multiple agencies also raises concerns regarding transparency and competition.

(often large) informal businesses, encouraging competition through new business entry and the formalization of existing economic activity. Addressing the business environment will be critical if Lao PDR wants to use the private sector as an engine for poverty reduction and job creation. The fact that a number of new investments focusing on the assembly of parts have recently come in, concentrated in Special Economic Zones, indicates that simplifying the business environment and putting the right conditions in place can lead to increased investment in labor-intensive sectors.

C. Proposed Development Objective(s)

The PDO remains to support the implementation of government's trade and integration priorities outlined in the 2012 DTIS Roadmap, and in particular to contribute to improved competitiveness and diversification, focusing outside the natural resource sectors.

D. Project Description

The proposed Additional Financing operation will extend support to existing sub-components and add two additional sub-components. It will be funded from an additional contribution by Australia to the existing multi-donor trust fund supporting the Second Trade Development Facility (financed by Australia, the European Union, Germany, Ireland, and USAID).

Component A: Trade Facilitation, Trade Policy, and Regulations: As a result of the small market size of Lao PDR, continued economic integration with neighbors will be important to allow future investments to benefit from economies of scale and reduce the current dis-incentives for investment (domestic and foreign) in Lao PDR. Trade facilitation support under the Second Trade Development Facility has supported Lao PDR in reducing the cost related to accessing imported inputs (goods and services) and bringing goods to markets (including capacity building) and the Additional Financing aims to continue that support, particularly regarding the implementation of the Trade Facilitation Agreement (which Lao PDR ratified as 18th WTO member) under the existing sub-component. As Lao PDR has already ratified Category A commitments, focus would be on Category C. Likewise, support to reviewing and streamlining non-tariff measures and procedures will be strengthened while support to FTTPD in developing their capacity for trade negotiations and domestic policy coordination around trade in services will be continued. Support to establishing and maintaining the Services Trade and Investment Portal (STIP), and maintaining the Lao Trade Portal, will continue.

Component B: Diversification and Competitiveness: Improving the overall business environment remains critical to increase competitiveness of the private sector and support diversification. To allow the private sector to benefit from improvements in the trade policy environment, component B will be broadened to include one additional sub-component (B3) to support rationalization of business regulations related to entry and operations of enterprises, particularly in non-resource sector. The new sub-component will aim to 1) increase transparency and predictability of obtaining business registration certificates and key operating licenses by mapping out related regulations, procedures, and processes, making such information publicly available, and supporting capacity building of government officials. It will further assist the government to 2) review and streamline selected regulations affecting the setting up and operating environment for private businesses, based on the process mapping. Other sub-component under this component (Business Assistance Facility and Labour Standards and manufacturing productivity) will be concluded as planned.

Component C: Mainstreaming Aid-for-Trade: The degree of mainstreaming trade into policy making in Lao PDR has been significantly supported by this component of the TDF-2. However, discussions among the private and public sector remain limited and need to be further strengthened if demand for policy reforms by national stakeholders is to translate into real impact on the ground, particularly now that MOIC is taking over the leadership of the Lao Business Forum (LBF) from MPI amid renewed government interest. While the LBF had been a forum for consultation between Government and the private sector in the past (led by LNCCI), the forum had been effectively discontinued over the last years. Aiming to strengthen the natural coordinating role of the MOIC for trade and private sector-related questions, a sub-component C4 will be added. It will support 1) MOIC in improving and making more inclusive the design of the LBF, improving coordination and feed-back between the public and private sector, and leading the LBF politically to ensure decisions are followed-up by relevant Ministries. The sub-component will also 2) support LNCCI technically to implement the LBF and making it more inclusive by supporting small and women-led enterprises in formulating their concerns in an actionable manner. The Government's capacity to flexibly respond to emerging priority areas will also further strengthened by allocating additional funds to the DTIS challenge facility and continuing support to the NIU and its ability to coordinate implementation of the TDF-2. Additional focus would be put on fiduciary capacity building and FM system strengthening of implementing agencies, and Government staff at the NIU would be involved increasingly with FM to ensure sustainability.

E. Project location and Salient physical characteristics relevant to the safeguard analysis (if known)

F. Environmental and Social Safeguards Specialists on the Team

Satoshi Ishihara (GSU02)

II. IMPLEMENTATION

III. SAFEGUARD POLICIES THAT MIGHT APPLY

Safeguard Policies	Triggered?	Explanation (Optional)
Environmental Assessment OP/BP 4.01	No	No safeguard policies are triggered.
Natural Habitats OP/BP 4.04	No	No safeguard policies are triggered.
Forests OP/BP 4.36	No	No safeguard policies are triggered.
Pest Management OP 4.09	No	No safeguard policies are triggered.
Physical Cultural Resources OP/BP 4.11	No	No safeguard policies are triggered.
Indigenous Peoples OP/BP 4.10	No	No safeguard policies are triggered.
Involuntary Resettlement OP/BP 4.12	No	No safeguard policies are triggered.
Safety of Dams OP/BP 4.37	No	No safeguard policies are triggered.
Projects on International Waterways OP/BP 7.50	No	No safeguard policies are triggered.

Projects in Disputed Areas OP/BP 7.60	No	No safeguard policies are triggered.
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IV. Key Safeguard Policy Issues and Their Management

A. Summary of Key Safeguard Issues

1. Describe any safeguard issues and impacts associated with the Restructured project. Identify and describe any potential large scale, significant and/or irreversible impacts:
The Project does not have any safeguard issues. The Project will not finance any civil works or any other activities that will have environmental implications. Given the nature of the project it also has no impact on social safeguards such as Involuntary Resettlement and Indigenous Peoples. No safeguard issue has been observed under the original project.
2. Describe any potential indirect and/or long term impacts due to anticipated future activities in the project area:
None foreseen.
3. Describe any project alternatives (if relevant) considered to help avoid or minimize adverse impacts.
Not applicable.
4. Describe measures taken by the borrower to address safeguard policy issues. Provide an assessment of borrower capacity to plan and implement the measures described.
Not applicable.
5. Identify the key stakeholders and describe the mechanisms for consultation and disclosure on safeguard policies, with an emphasis on potentially affected people.
Not applicable.

B. Disclosure Requirements (N.B. The sections below appear only if corresponding safeguard policy is triggered)

C. Compliance Monitoring Indicators at the Corporate Level (to be filled in when the ISDS is finalized by the project decision meeting) (N.B. The sections below appear only if corresponding safeguard policy is triggered)

The World Bank Policy on Disclosure of Information						
Have relevant safeguard policies documents been sent to the World Bank's Infoshop?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>
Have relevant documents been disclosed in-country in a public place in a form and language that are understandable and accessible to project-affected groups and local NGOs?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>
All Safeguard Policies						
Have satisfactory calendar, budget and clear institutional responsibilities been prepared for the implementation of measures related to safeguard policies?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>
Have costs related to safeguard policy measures been included in the project cost?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>

Does the Monitoring and Evaluation system of the project include the monitoring of safeguard impacts and measures related to safeguard policies?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>
Have satisfactory implementation arrangements been agreed with the borrower and the same been adequately reflected in the project legal documents?	Yes	<input type="checkbox"/>	No	<input type="checkbox"/>	NA	<input checked="" type="checkbox"/>

V. Contact point

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VII. Approval

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Country Director:	Name: Sally Burningham	Date: August 18, 2016