

MULTI-ANNUAL INDICATIVE PROGRAMME

(2007-2010)

LAOS

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***The amount will depend on the result of the discussions on the financial perspectives.**

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1 EC-Lao PDR SP

The 2007-2013 Strategy Paper for Lao PDR is closely aligned with the principles outlined in the development policy of the European Commission. These envisage a move away from traditional project activities towards operations with a more strategic focus such as budget support and strategic dialogue with the Government, Member States and other donors. As a result, the SP concentrates on one focal area and three non-focal areas of activity. The focal area is support to the Government's National Poverty Reduction Strategy, currently the National Growth and Poverty Eradication Strategy (NGPES) but soon expected to be incorporated into the National Socio-Economic Development Plan (2006-2010). The three non-focal areas of activity are: support to remote communities in the uplands, governance and trade. While the number of areas will be smaller than in the previous SP, the amount of financing will be higher, making the EC an important donor in Laos.

2 Summary of the MIP

The focal area under the Multi-annual Indicative Programme for 2007-2010 is support to the Government of Lao PDR's reform agenda. This can be achieved by contributing to the Poverty Reduction Support Operation (PRSO), a policy-based budget support tool. The PRSO articulates a policy reform programme of the Government of Lao PDR, supported by an IDA grant from the World Bank, focusing on three substantive areas of the National Development Strategy:

- 1) deepening reforms in public expenditure management, the financial sector, State-owned enterprises, State banks and utilities;
- 2) investing in the social sectors to expand access and improve the quality of services, particularly in the health and education sectors;
- 3) fostering sustained growth through private-sector and trade development and natural resource management.

By means of the PRSO, the EC would be able to target National Development Strategy goals by implementing a set of key policy reforms. Progress on the reform agenda will be jointly monitored in dialogue between the Government and development partners, which is bound to encourage closer alignment of donors with the national development agenda.

The first non-focal area will be support to reduce poverty in remote villages through dialogue on relocation policy. The poorest groups in Lao PDR are primarily ethnic minority swidden farmers. These groups are often the target of relocation efforts by the Government designed to achieve its objectives of eliminating swidden agricultural practices, eradicating opium poppy cultivation and bringing people closer to Government services and markets. Where successful, the policy results in preservation of natural resources, particularly forests, eradication of an illegal activity and an increase in the welfare of the relocated communities. However, these objectives have not always been achieved and there are many cases where relocated people have become worse off than they were before moving. In order for Lao PDR to achieve the long-term objective of eradicating poverty by 2020 and moving out of the category of least developed countries, the possibility of poverty increasing as a result of villages being relocated needs to be addressed.

The second non-focal area will be governance. Activities will be defined by the Working Group on Institution-Building and Administrative Reform, Governance and Human Rights.

The third non-focal area will be trade. EC activities will concentrate on improving the trading environment by supporting reforms in the areas identified under the Diagnostic Trade Integration Study (DTIS)¹ and they will build upon the current Multilateral Trade Assistance Project (MULTRAP) to support Lao PDR's accession to the WTO, particularly as this may take some years. A further priority should be to equip Lao PDR to negotiate, implement and benefit from existing and future FTAs in the Asian region, including with the EU.

3 Budget

During the period covered by the Multi-annual Indicative Programme for 2007-2010, a total EC grant of 32 million euros can be committed to EC-Lao PDR cooperation. The breakdown of this amount is as follows:

Focal area: Support to the GoL's reform agenda	60%
Additional actions	40%
Support to sustainable development in the uplands and policy dialogue on relocation	25%
Governance	5%
Trade	10%

4 Focal area: Support to the Government of Lao PDR's reform agenda

4.1 Strategic context/justification

In the past few years the policy agenda of the Government of Lao PDR has shifted decisively towards targeting poverty reduction within a strategic, long-term development framework. The Sixth Five-Year National Socio-Economic Development Plan (NSEDPlan)- contains an ambitious agenda of development priorities and was formulated in consultation with stakeholders. It integrates plans that were created earlier, including the (2003) Growth and Poverty Eradication Strategy (NGPES). Donors have increasingly begun aligning their aid with this policy agenda..

The momentum of structural financial and economic reforms has recently accelerated, with particular impetus created by the revenue flows expected from new infrastructure projects, especially the Nam Theun II hydroelectric dam (NT II). The Government has contributed to this by designing a Public Expenditure Management Strengthening Programme (PEMSP). It also recently completed a "pilot" costing exercise for the four priority sectors (education, health, infrastructure and agriculture), indicating a large financing gap for both capital investment and recurring expenditure. In addition, it is examining ways to promote trade and to create an enabling environment for the private sector.

In March 2005 the World Bank approved a partial risk guarantee for Nam Theun II (NT II), accompanied by a Poverty Reduction Support Operation (PRSO). The PRSO is a programmed, three-year budget support tool. It consists of an IDA grant from the World Bank

¹ The DTIS is expected to be completed by September 2006. Priority areas are likely to include: strengthening capacity-building for negotiation and implementation of bilateral and multilateral trade agreements, improving trade facilitation and customs procedures, and enhancing capacity in the area of sanitary and phytosanitary measures (SPS).

which can be supplemented by grants from bilateral donors (the value of PRSO-2 was USD 10 million). The PRSO supports the Government's own reform agenda, sets realistic targets and links these to monitorable indicators.

Until 2009, when the NT II dam project is expected to start generating revenue channelled into the State budget, PRSO operations will focus mainly on public finance management. This is appropriate in order to ensure that the new revenue is channelled towards the pro-poor priority sectors (health, education, rural development and infrastructure) and to build proper control systems for public finances prior to the inflow of the new funds. The PRSO will also target social sectors, aiming to ensure that a growing proportion of the State budget is allocated to health and education. The budgetary process needs to be strengthened in order to demonstrate clearly that the revenue from NT II is in addition to other investments in the priority sectors. In the long run the scheme is expected gradually to deepen the Government's policy reform agenda in the social sectors, trade, private-sector development and natural resource management.

EC support to the Government's poverty reduction policy within the framework of the reform agenda can be envisaged as general budget support linked to the PRSO. In this way, the transaction costs of aid can be minimised and aid effectiveness can be enhanced through harmonisation and coordination. If the PRSO exercise is successful, donors' policies are likely to become gradually more aligned with the national policy and institutional reform agenda and the national budget cycle. This will enhance budget predictability and thereby facilitate public expenditure planning. Work on developing a Medium-Term Expenditure Framework (MTEF) will expand beyond the four priority sectors. Government policy formulation will also become rooted in a more open, accountable and consultative process.

4.1.1 General objective

The overall objective is to facilitate attainment of the Government's national development policy objectives.

4.1.2 Results

Achieving the Government-led reform agenda.

Initially, progress is expected in the following main clusters of reform:

- **Strengthening public financial management** systems for revenue collection as well as allocating, executing and monitoring public expenditure, at both national and provincial levels. This includes strengthening revenue collection, financial discipline and restructuring of State-owned banks and enterprises, as well as a reform of public utilities such as electricity and water.
- Increasing the impact of public spending in terms of poverty reduction by **aligning budget resources with pro-poor National Development Strategy goals**. Public expenditure will be redirected to basic services that improve human development outcomes.
- **Promoting sustained growth** through a stronger private sector, a greater volume of trade and sustainable management of natural resources. This involves improving the business environment, making progress on implementing AFTA commitments and managing forests and rivers more sustainably.

4.1.3 Activities

PRSO grants, which follow an annual cycle (April to March), are subject to successful completion of a range of reform-oriented prior action by the Government. Each of the three components of the PRSO involves a set of “expected action” and outcome indicators. Successful progress against the Government’s own plans, the key elements of which are identified as “expected action” in the PRSO, will enable donors to release funds, while completion of a series of “triggers” (the “expected action” considered most critical by the Government and the PRSO financiers) will help donors to decide to begin preparations for the next PRSO. Currently there are 37 expected actions, of which 11 have been agreed as triggers in PRSO-3, offering a rigorous framework for measuring progress on reform (see Annex 2). The “expected action” will be established in agreement with the Government by the donors supporting the PRSO, with the priority of deepening the key reforms rather than expanding the policy agenda prematurely.

The activities covered in PRSO-2 include:

A. Public resource management

- Public expenditure management: adopting the Medium-Term Expenditure Framework as the key planning tool and continuing the capacity-building activities under the Public Expenditure Management Strengthening Programme (2004-2009);
- Strengthening revenue collection;
- State commercial banks: improving their governance to reduce fiscal risks;
- State-owned enterprises: continuing independent audits and privatisation/liquidation of chronically loss-making companies;
- Public utilities: monitoring the introduction of new tariff plans and improving open competition in the utility sectors through the entry of foreign/private operators into the market.

B. Public expenditure policy

- Health and education: further increasing the shares of these sectors in the national budget and improving the balance between recurrent and capital expenditure;
- Infrastructure: further improving the quality of and access to water and sanitation and improving maintenance of roads;
- Monitoring alignment of expenditure with national development goals: further improving the quality of data.

C. Sustained growth

- Private sector: continuing legislative reforms and clarifying the regulatory environment, particularly for SMEs, and creating more confidence among foreign investors;
- Trade: WTO accession and AFTA integration;
- Natural resource management: further strengthening fiscal policy, particularly concerning collection of timber royalties, and improving transparency of management in the forestry sector.

4.1.4 Implementation

The PRSO is the most appropriate - and currently the only - pool-funding mechanism to support the Government’s reform agenda in Lao PDR. The EC will assist and closely monitor the Government’s performance, particularly in public financial management. This will be

achieved through technical assistance to support policy and institutional reforms, coupled with continuous assessment of the Government's reform performance against the PRSO indicators.

In 2004 the EC financed three studies which contributed to formulation of PRSO-1, 2 and 3. The EC closely followed the process leading to definition of PRSO-2 and plans to second a full team member for the PRSO-3 negotiations from January to March 2007. The next EC contribution to the PRSO is expected to be disbursed for PRSO-3 which will be negotiated by March 2007 and disbursed before the start of the 2007-08 fiscal year (i.e. not later than 30 September 2007). Hence, the first EC action will consist of PRSO-3 operations only. Before preparing another PRSO grant, the EC will make an assessment of the first three-year PRSO series as a whole, with particular emphasis on PRSO-3 and on the experience gained from EC involvement in the PRSO overall. If the assessment is positive, a second PRSO grant can be prepared, but if further support is not recommended or is not possible for other reasons, alternative avenues for supporting the Government's reform agenda can be sought.

The EC support to PRSO-3 may take the form of general budget support channelled directly to the Treasury, while being directly linked to the PRSO in all substantive areas of policy reform and in terms of monitoring progress. The EC will retain ultimate responsibility as far as the final decision to disburse EC funds is concerned. In addition, a minimum of between 5% and 7% of the funds will be earmarked for technical assistance. These will be managed either by the multi-donor trust fund under the Public Expenditure Management Strengthening Programme (PEMSP) or directly by the EC. TA can also be made available for the social sectors as necessary.

4.1.5 Risks and conditions

There is a risk that the Government's commitment to some of the reforms might fail, resulting in poor policy performance and unclear accountability between institutions and lines of administration. This risk is mitigated by the ongoing policy dialogue between the authorities and development partners to review progress based on the "prior action" matrix of the PRSO. Secondly, budget support inevitably involves fiduciary risks, which in the case of Lao PDR are quite high. The inflow of revenue from the proposed NT II hydroelectricity project, which will generate increased resources for poverty reduction from 2009/10 onwards, highlights the urgency of public expenditure management reform. However, fiduciary risks are mitigated by the ongoing efforts to improve public financial management systems under PRSO-1, 2 and 3.

The EC intends to participate actively in preparation, appraisal and negotiation of PRSO-3. It will also play an active role in definition of a new series of PRSO. In order to become closely involved in the ongoing policy dialogue between PRSO stakeholders, the EC has already participated in the public expenditure review (PER) led by the World Bank in 2005-2006. Given the crucial importance of PFM (public finance management) reforms, the EC also commissioned a diagnostic study on public financial management that assesses the viability of budget support in Lao PDR. This study concluded that the **public financial management** systems in Lao PDR are weak, but **likely to improve sufficiently by 2007 for provision of EC budget support** (see Annex 1). The final decision on such support will be further informed by the final version of this study and will also be based on the criteria in the European Commission's *Guide to programming and implementation of budget support for third countries* (new version expected in 2006). These criteria include a viable medium-term macroeconomic framework, a positive trend towards transparency, accountability and

efficiency in public finance management (PFM) and a reform programme supported, but not necessarily financed, by the Bretton Woods Institutions (World Bank and IMF).

There is currently no IMF programme in Lao PDR due to the lack of independent external auditing of the State bank. The Government has indicated that auditing is to be performed by the State Audit Office, in accordance with international auditing standards, and the ADB is building capacity in this area. The IMF is continuing to work in the country through its enhanced surveillance mechanism. In addition, the standard Article 4 consultations are conducted yearly and the IMF also issues 6-monthly reviews and participates in the public expenditure review. The IMF has stated that it can provide a letter of confidence in support of EC participation in the PRSO.

4.1.6 Indicators

The PRSO involves a rigorous framework of performance indicators, which is currently aligned with the NGPES but which is expected to be consistent with the NSEDP as well. For future PRSOs these indicators will be defined jointly by the Government and its co-financiers and in consultation with other donors. In 2006 the indicators are being closely monitored prior to the final decision on EC support to the PRSO. The EC attaches particular importance to indicators which relate to budget expenditure and budget implementation in the social sectors. Examples include:

- increase in percentage of expenditure on the health and education sectors: for health from 5.5% to 7.5% of the budget by 2007, and for education from 11% in 2005 to 13% by 2007;
- improved textbook/student ratios: from 1:5 in fiscal year (FY) 2004/05 to 1:1 in FY 2006/07 in grades 1 and 2;
- halving the delays in payment of teachers' salaries: from 20% of teachers' salaries with over two months' delay in 2004 to less than 10% with any delay in 2007;
- pilot community school grants programmes implemented: from zero in 2004 to 500 grants in 300 villages in FY 2006/07;
- increase in percentage of health expenditure going to district hospitals and health centres: from 22% in 2003 to 45% by 2007.

The EC will seek to link the Public Expenditure and Financial Accountability (PEFA) indicators to the PEMSP and the PRSO. Preliminary discussions with the WB and GoL indicate that all stakeholders are likely to accept PEFA indicators as the key mechanism for monitoring reform performance in PFM in the long term.

Sustainable use of natural resources is one of the key challenges facing Lao PDR. The current PRSO identifies one "trigger" linked to improved forest management: a Government action plan for timber marketing and revenue sharing. Where appropriate, the EC will support assessments of the environmental impact of PRSO reforms, possibly through the PER or through a strategic environmental assessment (SEA). The EC will also support analytical work on gender and indigenous peoples/ethnic minorities in order to incorporate these aspects into the PRSO reform matrix more systematically, particularly in relation to the impact of public expenditure on vulnerable groups in remote communities (where ethnic minorities make up a majority of the population).

4.1.7 Financial envelope

19,2 million euros .

4.1.8 Timeframe

2006	Policy dialogue with the Government, donors and other partners
Autumn 2006	Formulation of financing proposal
Spring 2007	Joint appraisal, negotiation and commitment of funds
By mid-2007	Disbursement
Autumn 2007	Assessment of the possibilities for future EC involvement in the PRSO

This timeframe is indicative only, and depends on the performance of the GoL in the reform agenda.

5 Additional action

5.1 Support to sustainable development in the uplands and policy dialogue on relocation

5.1.1 Strategic context/justification

The Government of Lao PDR is seeking the most effective way both to improve livelihoods and effectively to deliver services to people in remote districts and communities. Strategies revolve around giving priority to 47 districts, mainly in the uplands, for poverty reduction programmes. The policy is to direct development programmes towards these areas and to finance local development funds.

This action is being taken within the context of the Government's broad rural development policy of "stabilisation" of settlement. This broad policy incorporates land allocation directives, eradication of slash-and-burn agriculture and elimination of poppy cultivation and attempts to bring people closer to services such as education, health care, and water and sanitation.

The Government has faced two major constraints in implementing its strategy: firstly, the cost of preparing sites for relocation has far exceeded the Government's means; secondly, a lack of suitable unoccupied land in the quantities required. As a result, in several cases access to agricultural land, forests and Government services has been inadequate to meet the needs of the relocated communities. Studies have demonstrated that food security, health and the traditional culture of ethnic minority groups can suffer seriously as a result.

Social, economic and environmental benefits can be gained from better management of development in the uplands. Allocation of larger amounts of resources will allow participatory assessment, case by case, of options for sustainable development. This approach could significantly ease the difficult process of deciding whether villages should move or not and, when they do, improve the outcomes of the transition.

The Government has requested assistance and has indicated that it is willing to enter into dialogue with the EC and other donors on the matter.

5.1.2 Objectives

The overall objective is to contribute to poverty reduction, food security and environmental and cultural sustainability through support to sustainable development in the uplands and dialogue on reform of current policy.

5.1.3 Results

- Introduction of participatory planning in villages in priority districts;
- Improved social infrastructure and rural livelihoods in highland villages with good potential for economic and environmental sustainability *in situ*;
- Improved health and livelihoods in recently relocated or consolidated villages;
- Improved planning and preparation of new locations for village relocation where remaining *in situ* is not a viable proposition and villagers are willing to move.

5.1.4 Activities

To be decided in accordance with an agreed policy and method of implementation.

5.1.5 Implementation

Dialogue with the GoL will begin with a discussion of Government priorities and an examination of existing information on options for sustainable development in the uplands and the nature, extent and effects of relocation. To this end, the EC is co-financing a World Bank study on the impact of Government policy towards remote communities on poverty. Implementation of any action will be such that the choice of development should respect the indigenous peoples' right to choose their own development path and to respect their right to a free, prior and informed consent on programmes and projects affecting their communities. Specifically implementation will respect the following principles:

- the development option chosen should fit in with a long-term vision of sustainable development which is based on the results of sound research;
- the development option chosen should be based on participatory assessment of the current situation, possible alternative courses of action, and the social, economic and environmental viability of those alternatives;
- villages that have potential for development where they are should be encouraged to harness it;
- any relocation should be voluntary and based on a participatory approach that respects cultural and sociological considerations;
- where relocation is the preferred option, sites should be developed in advance of occupation with the full participation of those who will be moved, should be adequate for their needs and should be subject to safeguards against negative environmental impacts;
- a follow-up programme of capacity-building involving training in agricultural techniques, sanitation, primary health care, income-earning opportunities and village governance should be provided.

The limited resources in comparison with the scale of the problem must be recognised. For this reason, initial efforts will be piloted in the districts selected by the Government for its own poverty reduction programmes.

5.1.6 Risks and conditions

Major risks are associated with the poor outcome of past efforts by the Government to stabilise the location of villages and to make their agricultural practices sedentary. These activities have often resulted in a decline in the food security and health status of relocated villagers. Independent reports on village relocation have highlighted the problems. Some European political voices may therefore seek to deter the Commission from involvement in an activity with a poor international image.

However, the poor image of past outcomes in the uplands should not be a reason for not tackling the important issue of improving the access of remote communities to development opportunities. It has to be recognised that any action by development agencies targeting poverty reduction will have to confront the issue of how best to service remote communities. The task is to find better solutions.

In the past the Government has been reluctant to discuss its rural development policy and in particular the issue of “stabilisation”. Initial approaches to discuss the issue with the Government have, however, been well received. Nevertheless, the true marker of success will be progress towards achieving the results outlined in section 5.1.3.

Donors’ and NGOs’ approaches to this issue differ widely. Some simply have other priorities, others consider the fate of remote communities an important human rights issue. Many international NGOs would prefer to champion efforts to bring development services to remote villages rather than bring the villages to the services. Achieving a common approach between donors and NGOs may prove to be elusive. However, most of the major donors have indicated their support for this initiative.

5.1.7 Indicators

The following indicators will be used to measure the impact of the initiative on villages resettled and not resettled (developed “*in situ*”):

- food security, measured in terms of number of months of rice sufficiency for each village;
- food production, measured in terms of increases in rice, other cereal, vegetable and livestock production and labour input per hectare cultivated or per tonne of rice production, broken down by gender;
- alternative livelihoods, measured in terms of introduction of and increases in non-traditional and cash crops, wage labour, non-agricultural businesses and income-earning ventures;
- health status, measured in terms of numbers of protected water supplies installed, increases in malaria prevention practices, recorded mortality and morbidity rates;
- service delivery indicators, including numbers of visits by extension staff, vaccinations administered, numbers and proportions of children in school, and literacy rates;
- cross-cutting indicators, such as environmental impact assessment reports, gender impact reports and cultural impact reports.
- specific indicators in accordance with the EC and World Bank policies on Indigenous Peoples

5.1.8 Financial envelope

8 million euros .

5.1.9 Timeframe

2006	Ongoing policy dialogue with the Government, donors and civil society
End 2006	Identification
2007	Formulation of financing proposal
Late 2007	Commitment
2008	Implementation

5.2 Governance – rule of law and human rights

5.2.1 Strategic context/justification

In June 2005 the EC and Lao PDR held their first informal Working Group on Institution-Building and Administrative Reform, Governance and Human Rights. Activities financed by the EC in the field of governance and human rights (including both bilateral aid and horizontal budget lines) will be linked to the policy dialogue in this Working Group.

The Ministry of Justice is currently working on a strategic vision for reform across the legal sector up until 2020. This should be completed by summer 2006. Depending on the progress made, the Commission may decide to join other donors in financing this area.

5.2.2 Objectives

To support the Government of Lao PDR in its activities in the fields of governance, rule of law and human rights.

5.2.3 Specific objective (if the legal sector is chosen)

To assist the Government of Lao PDR to develop a coherent, credible and predictable legal, financial and administrative framework for all its citizens and to promote and protect all human rights.

5.2.4 Results

The capacity of the Government of Lao PDR to address key justice, rule of law and other human rights issues will be enhanced.

5.2.5 Activities

To be identified by a mission but will draw on indicators established by the Government of Lao PDR under the Governance Reform Road Map and Legal Sector Master Plan currently being drafted to highlight the key priority initiatives to be implemented over the next three years (2006-2008).

5.2.6 Implementation

The means of implementation will be chosen once the action has been identified, bearing in mind the need to provide assistance in a flexible way and maximise the added value of EC support in this strategic field.

5.2.7 Risks and conditions

EC activity must include all involved to make sure that the activities financed are not isolated in one department but have an effect across the sector. EC support must also be coordinated with EU Member States and other donors. The Government has to be fully committed to and accountable for the reform process for the long term, especially as such wide-ranging reforms will be necessary.

5.2.8 Indicators

To be identified on the basis of the areas(s) of activity (by a mission).

5.2.9 Total appropriation

5.2.10 Financial envelope

1,6 million euros .

5.2.11 Timeframe

2007	Identification
2007	Formulation of financing proposal
Late 2007	Commitment
2008	Implementation

5.3 Trade

5.3.1 Strategic context/justification

Trade is one of the six priority areas for EC development cooperation. The role that trade can play in generating pro-poor growth is well recognised. Therefore, the EC will continue to play an active role in this area, building on the activities of the previous Strategy Paper, particularly with regard to the Multilateral Trade Assistance Project to support WTO accession.

The Government recognises that trade development is an important component of poverty eradication and paid special attention to private-sector development in the NGPES. EC activities on trade will come under the Integrated Framework exercise which aims at ensuring that trade policy is integrated into wider development policy in Lao PDR and at assisting coordinated delivery of trade-related technical assistance to Lao PDR. Cross-cutting issues, such as the environment and gender, are expected to be mainstreamed in the DTIS (Diagnostic Trade Integration Study) and, consequently, in the EC's operations. The DTIS started with a preliminary mission in July 2004, and the plan is to have the final results and activity matrices for donor support ready by autumn 2006.

5.3.2 Objectives

The overall objective of this action is to provide trade-related assistance to Lao PDR to enhance its capacity to integrate into regional and international trade systems, leading to economic growth and in turn to reduction of poverty.

5.3.3 Results

- Ø Reduction of poverty, thanks to enhanced trade performance;
- Ø Lao PDR will participate effectively and become more integrated in regional and international trade systems;

- Ø Greater capacity for trade policy formulation and implementation, including customs and border measures and trade facilitation and “behind-the-border” regulatory issues;
- Ø Improved knowledge on the part of Lao officials of the legal and regulatory framework (in particular of customs and SPS issues) and administrative capacity to ensure compliance with WTO requirements;
- Ø Improved trade facilitation leading to increased import/export flows and control over transit flows;
- Ø Revised legal and regulatory framework with better implementation and enforcement;
- Ø Stronger negotiating skills on the part of Lao officials;
- Ø Stronger expertise on the part of Lao officials on subjects and issues covered under comprehensive FTAs, and better understanding of the interests/priorities/consequences /impact of negotiating future FTAs.

5.3.4 Activities

On the basis of consultations with the Government and the analysis carried out so far under the Diagnostic Trade Integration Study of the Integrated Framework the main focus of the EC operations is likely to be on supporting the GoL’s effort to improve trade facilitation and enhancing capacity in the area of customs and sanitary and phytosanitary measures (SPS). The detailed activities will be agreed upon and further defined once the DTIS has been finalised. Support for increasing exports may be provided in the following sectors: agriculture, wood and forestry products, and manufacturing. The capacity of Laotian officials will be strengthened by providing training on how not only to negotiate multilateral, regional and bilateral trade agreements effectively but also to implement/enforce them (paying special attention to dispute-settlement mechanisms and customs administration).

5.3.5 Implementation

All trade-related activities will come under the Integrated Framework. Activities should ideally be jointly financed with other donors, but could also be part of individual donor projects financed under the Integrated Framework. The private sector will be consulted during preparation of the EC operations and will be involved as much as possible during implementation, including by supporting the Government/private sector dialogue. Joint missions with other donors will be the preferred method for the new operations.

5.3.6 Risks and conditions

EC trade activities should be coordinated with other donors as part of the on-going Integrated Framework exercise. There is a risk that the IF process may be delayed. There is also a risk that donors will not commit themselves to genuine coordination. The Integrated Framework process could lose momentum because of lack of follow-up by the Government. Other risks include lack of political will and commitment in the Government to join the WTO and lack of qualified staff and resources in the Government. Having identified the risks, the active involvement of the EC, as an important player in the field of trade-related assistance, including the IF process, can be expected to minimise/overcome them.

5.3.7 Indicators

Monitoring indicators will be fine-tuned during formulation of the project, when the list of activities will be defined in greater detail. The main indicators will be:

- a) reduction in the cost and time needed for customs clearance;
- b) increase in the value of official trade;
- c) increase in customs revenue;

- d) increase in the number of business operators requesting a licence;
- f) increase in the quality of inputs provided by the Ministry of Commerce in the WTO accession process/AFTA.

5.3.8 Financial envelope

3,2 million euros .

5.3.9 Timeframe

2005/06	Ongoing dialogue with the Government, donors and other partners
2006	Formulation of financing proposal/ALA Comm./EC Decision
2007	Start of implementation

ANNEX 1: Summary of the draft Diagnostic Study on Public Financial Management in Lao PDR (May 2006)

Background

The Poverty Reduction Support Operations (PRSOs) are linked to the Nam Theun II (NT II) hydroelectricity project, helping to ensure that the revenue from NT II will be used to support the Government's priority poverty reduction programmes, as set out in its National Poverty Reduction Strategy. In order to achieve this objective, significant progress would have to be made on strengthening the Government's Public Expenditure Management Reform Strategy.

Public Expenditure Management Strengthening Programme (PEMSP)

The Ministry of Finance (MOF) recently prepared a Public Expenditure Management Strengthening Programme (PEMSP) to put this strategy into operation. The PEMSP identifies key public expenditure management reforms to be implemented in the period up to fiscal year (FY) 2008. These are: fiscal planning and budget preparation; budget execution, accounting and financial reporting; local government financial management; financial legislation and regulatory framework; and capacity-building.

The strategic objective of the PEMSP is to improve policy consistency, efficiency, transparency and accountability in public expenditure management by strengthening institutional systems and capacity-building and making progress towards appropriate international financial management standards. The PEMSP is based on substantial analytical work undertaken in recent PERs and other assessments of the Government's PFM systems, including IMF reviews. The PEMSP will provide a framework for involving all levels of PFM administration in Lao PDR (central, provincial and district) and for mobilising and coordinating external support for the Government's PFM initiatives. In this context, the PEMSP is intended to be a comprehensive Government-led programme that ensures a consistent technical approach and sequencing. Under the next multi-year programme document which is currently under preparation, **the PEMSP reform outcomes will be linked directly to the PEFA framework** in order to make it easier to monitor performance.

The main achievements since the PEMSP was launched in November 2005 can be summarised as follows:

- Steering Committee and Implementation Committee established;
- Technical Adviser and Capacity-Building Adviser both recruited;
- Secretariat established and staffed under the MoF's Fiscal Policy Department;
- Draft work plan and programme document distributed;
- Three provincial and one national workshop held to discuss a more detailed work plan;
- Support from the UNDP secured for the running costs of the Secretariat;
- ADB technical assistance secured for "expenditure planning".

A Consultative Forum and three thematic Task Forces are expected to be set up. The Consultative Forum will be the main window for donor participation in the PEMSP. The three Task Forces will cover: planning and budgeting; budget execution, internal controls and reporting; and cross-cutting issues.

Key findings of the Diagnostic Study

Public financial management (PFM) reform has been under way for a number of years. In general, PFM systems remain weak owing to severe capacity constraints. In some areas (e.g. internal and external audit or budget analysis) there are acute staff shortages. However, the picture is not entirely negative. **Although the pace of reform is slow, it is moving in the right direction.**

The **public finance system is strongly decentralised** in Lao PDR (or more properly described as “deconcentrated”, as sub-national administration has no legal identity separate from central government), with the provinces accounting for 60 percent of Government revenue collected and 48 percent of total Government expenditure. As a result, the topic of reforming central/local fiscal relations is critical to the overall reform of the public finances. A separate study was conducted on this topic.

The budget preparation process is mainly “bottom-up”, as line ministries and provinces plan their budget requests before receiving their financial ceiling from the Ministry of Finance (MOF). **The budget preparation cycle is both too compressed and too late.** The budget submitted for approval to the National Assembly before the start of the fiscal year is top-level only, without details. Detailed budgets for line ministries and provinces are completed at least three months *after* the start of the fiscal year. There are no common guidelines on preparation of budgets – only percentage increases in main categories of revenue and expenditure; the resultant incremental budgeting is not conducive to realignment of expenditure with changing policy priorities.

There are **two budgets** – one for recurrent expenditure (MOF) and one for capital spending (CPI) – with no clear links between them. There are also no clear links between policy, planning and budgeting, as the sector strategies outlined in annual and five-year development plans are based on needs and not on available resources, with no firm budget constraints.

Although improvements have been made in budget nomenclature (simplified in 2004), there is still **no functional classification of the budget.** Budget nomenclature is a mixture of economic and administrative classifications. The lack of a functional classification is a considerable obstacle to tracking expenditure on priority activities and linking policy-making, planning and budgeting, although the new sub-coding structure of the **Government Financial Information System** (GFIS; see below) can assist in this. Benchmarks for NT II “additionality”² need to be established as soon as FY 2005/06 out-turn becomes known.

The provinces account for 60% of revenue and 48% of expenditure (although these figures are higher in education, at 78%, and health, on 73%). **Revenue collection and submission to the centre are below target** as provinces with surpluses have little incentive to submit revenue in excess of targets. Revenue forecasts are over-optimistic, so planned expenditure is unrealistic – resulting in a system of cash rationing and build-up of payment arrears. **Over-optimistic revenue forecasts** destabilise the expenditure side of the budget. When the actual revenue

² The revenue generated by NT II must be channelled into the specific poverty reduction programmes for priority sectors (infrastructure, education, health, rural development) and the authorities must be able to demonstrate that these funds are additional to the existing flows of funding into these programmes. In other words, the Government is not allowed to relax its efforts in financing these programmes and fill the resulting gap with NT II revenue.

collected becomes known each quarter (invariably below target), the expenditure budget is revised downwards throughout the year, with adverse spillover effects into the next FY.

Poor provincial revenue performance reflects a combination of over-estimation (budget issue), weak collection and remittance incentives – for provinces in surplus and deficit alike – and the ability of provinces to withhold amounts collected. **Revenue leakage** is known to be significant. Provinces are powerful politically in relation to the centre and have effective control over a wide range of critical functions and resources (particularly in the priority sectors). There is no system for equitably allocating those resources that are mobilised across the country and in line with national priorities. As a result, there are **wide variations between provinces in per capita recurrent spending on priority sectors**.

Budgets do not reflect the full fiscal position, as they do not include some statutory funds, other revenue (local livestock taxes and bed taxes) and capital projects fully funded by donors. There is evidence of a substantial “tax gap”.

Roll-out of a **new integrated computerised Government Financial Information System (GFIS)** began in July 2005 under detailed daily management by the MOF’s Treasury Department with technical support from the Accounting Department. The Budget Department monitors budget implementation through the new system on a monthly basis. Through the GFIS system, the central Treasury is now connected to 39 central line ministries, the 18 provincial Treasury offices, 4 provincial tax offices and 17 customs offices at border crossing points. (Links with the tax and customs offices provide information only to the central Treasury, as opposed to being a system for central Treasury control.) The GFIS covers recurrent expenditure and capital expenditure financed from domestic revenue, and is currently fully operational in 14 of the 18 provinces. The GFIS has not yet been implemented at district level. This will take time. The districts use manual procedures for reporting to the provinces, which in turn use the GFIS to report to the central Treasury.

The new system is beginning to “settle down”. **Internal controls are generally good**, but there is **no sub-system for non-salary commitment control**. This results in significant payment arrears to suppliers and contractors and, in turn, to higher purchase prices for the Government.

Reporting formats under the GFIS need to be re-designed and simplified to provide better information on budget execution and cash forecasts/management. Financial statements have not yet been produced in the new format required under the new accounting regulations (2002).

Also, there is **no culture of internal audit** in Lao PDR, and external audit (by the State Audit Organisation) plays only a minor role, reporting to the Prime Minister’s office instead of to the legislature.

Gradual (incremental) improvements are being made. For example, the **new accounting regulations** approved in 2002 marked the first step towards international standards. A new computerised budget execution system was introduced nationwide in July 2005 and full roll-out is expected by the end of FY 2005/06. The new (draft) Budget Law currently under discussion addresses many of the weaknesses in the current budget preparation system, including the introduction of greater clarity in revenue and expenditure assignments at various levels of government and a more appropriate budget timetable.

Recommendations

The consultants' overall conclusion about the state of the PFM system in Lao PDR is that, although the pace of reform is slow, there is evidence that solid progress is being made and that **the reforms are moving in the right direction**. The PFM systems in Lao PDR are currently weak, but the gradual improvements that are being made, particularly with the new Treasury and accounting systems, suggest that they will improve sufficiently by 2007 for the provision of EU budget support.

The most appropriate channel for EC budget support would be within the framework of the WB-led **PRSOs and the associated PEMSP**, which is effectively a component of the PRSO. These programmes establish overall framework conditions for encouraging the Government to implement measures that will strengthen public financial management. In terms of establishing indicators for possible EU budget support, the appropriate approach would seem to be to monitor implementation of the policy action identified within the PRSO framework (and agreed with the Government) and the related PEFA indicators.

The process of establishing “triggers” for the release of funds under the PRSO grant arrangements is already in use. These “triggers” form part of an implementation path that already constitutes the PEMSP and thus provide the best method for both the WB and the EU to act jointly in supporting PFM reforms. Furthermore, the NT II additionality conditions provide further assurance that future budget support can be directed towards the high-priority sectors that will have the greatest impact on reducing poverty. Because of the severe capacity constraints referred to earlier, substantial technical assistance will be needed to support implementation of the PEMSP. In this context, the Ministry of Finance, its PEMSP Technical and Capacity-Building Advisers, the WB and other interested donors should support the plans for establishing a **Multi-Donor Trust Fund (MDTF)** linked to the PEMSP, to provide much-needed technical assistance, computer equipment, teaching materials and manuals of procedures for wide dissemination of improved PFM practices at all levels of Government.

The annual content of the PEMSP needs to be adjusted from time to time. The six main areas that need to be given greater prominence in the PEMSP are:

- preparation of the detailed budget before the start of the fiscal year (the new draft Budget Law addresses this issue);
- more realistic revenue forecasts in budget planning; over-optimistic revenue forecasts destabilise budget execution as expenditure allocations are regularly reduced (every quarter) throughout the fiscal year; a useful maxim should be understood – it is possible to implement a well-prepared budget badly, it is not possible to implement a badly prepared budget well;
- reducing revenue leakage prior to the point of collection, at the point of collection and after the point of collection. At present, the revenue side of PFM systems is not covered at all in the existing PEMSP. At a meeting on 9 January 2006 the PEMSP Steering Committee decided that the revenue side should be gradually included in the PEMSP. The exclusion of the revenue side of the budget is a significant weakness of the PEMSP, so this decision is a positive development;
- no controls exist for commitments of non-salary recurrent expenditure and capital expenditure financed from revenue.

Internal audit is non-existent at present and external audit is very weak.

ANNEX 2: PRSO matrix

LAO PEOPLE'S DEMOCRATIC REPUBLIC SECOND POVERTY REDUCTION SUPPORT OPERATION UPDATED PROGRAMME MATRIX (Draft 10 February 2006)

[Note: Square brackets around PRSO2 action/triggers indicate that the action/triggers had not yet been verified as completed at the time of writing although it was hoped that they would be completed by the end of February 2006. PRSO3 action/triggers are subject to negotiation.]

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Component 1: Public resource management					
1.1 Strengthening public expenditure management					
A. Expenditure planning and budgeting	<ul style="list-style-type: none"> - The MOF approved the five-year Public Expenditure Management Strengthening Programme (PEMSP), together with the annual implementation plan for FY 2004-05. - The MOF issued a request for expressions of interest (EOI) for long-term technical assistance for PEMSP. 	<ul style="list-style-type: none"> - The MOF approved the PEMSP annual implementation plan and capacity-building plan for FY 2005-06. - The MOF contracted long-term technical assistance for the PEMSP. 	<ul style="list-style-type: none"> - The MOF will update the PEMSP based on the 2005 PER analysis and demonstrate the progress being made with implementation and capacity-building. 	<p>Outcome: Strengthened public expenditure management capacity.</p> <p>Indicator: Task completion against implementation schedule.</p>	<p>NGPES</p> <ul style="list-style-type: none"> - Part 1, Chapter 2, Chapter 3, Chapter 7 - Part 3, Chapter 1 - Part 5, Chapter 1, Chapter 3 <p>CAS</p> <ul style="list-style-type: none"> - Objective 2.1
Planning	<ul style="list-style-type: none"> - The CPI and MOF updated the MTEF. 	<ul style="list-style-type: none"> - [The MOF and CPI updated the indicative MTEF, including costings for priority sectors/programmes.] - [The Government approved the indicative MTEF as part of the NSEDP.] 	<ul style="list-style-type: none"> - The MOF, MOH, MOE and provinces will pilot specific budget allocations for education and health programmes in each province. 	<p>Outcome: Improved predictability and NGPES alignment of expenditure allocations.</p> <p>Indicators: Expenditure on NGPES sectors and priority programmes (% of total); non-wage recurrent spending (% of total).</p>	

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Budget	- The MOF provided the IDA with a summary of the revised FY 2004-05 budget.	- The MOF prepared the revised budget cycle in preparation for the revised budget law. - The MOF prepared the FY 2005-06 budget with: i) administrative classification; ii) priority expenditure sectors/programmes; iii) summary data on statutory funds]. [- The MOF published the FY 2005-06 budget summary, within three months of the start of the FY (i.e. in January).]	- The MOF will prepare the FY 2006-07 budget with: i) administrative classification; ii) priority expenditure sectors/programmes; iii) summary data on statutory and non-statutory funds. - The MOF will publish the FY 2006-07 budget summary within two months of the start of the FY (i.e. in December).	Outcome: Streamlined budget preparation process and timely publication of budget. Indicators: Timely publication of budget books; % of Government financial operations covered in budget documentation.	
B. Budget execution and financial reporting		- The MOF initiated preparation of an issues paper on Budget Law revision, including a discussion of options for restructuring and strengthening the Treasury and consolidating budget execution functions.	- The MOF will draft an appropriately revised Budget Law, Treasury Decree and other implementing regulations and guidelines.	Outcome: Progress towards centralised Treasury with consolidated functions. Indicator: % of central revenues available to central Treasury.	NGPES - Part 1, Chapter 2, Chapter 3, Chapter 7 - Part 3, Chapter 1 - Part 5, Chapter 1, Chapter 3 CAS - Objective 2.1
Reporting		- The MOF initiated a programme to develop a new, GFS-compatible chart of accounts, budget nomenclature and implementation strategy. - The Government made progress with GFIS roll-out.	- The MOF will approve the revised GFS-compatible chart of accounts, budget nomenclature and implementation strategy, following consultations with key stakeholders. - The Government will approve and start implementing a longer-term strategy for strengthening Government financial management information.	Outcome: Consolidated and more transparent financial reporting system. Indicator: Financial statements follow reporting standards.	

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Cash management	- The Treasury updated registers of i) accounts payable, by period, at the end of FY 2003-04; ii) Government bank accounts, with corresponding balances, at the end of FY 2003-04.	- The Treasury prepared and monitored for central administration and selected provinces i) monthly register of accounts payable; and ii) monthly reports on the Treasury balances.	- The Treasury will pilot quarterly consolidated budget execution reports for all ministries and provinces, following completion of GFIS roll-out. - The MOF will take steps to rationalise and consolidate bank accounts at each level of Government and close unauthorised accounts.	Outcome: Enhanced predictability, efficiency and transparency of budget execution. Indicators: % budget execution in priority sectors; % of central and sub-treasury reports on time; arrears to suppliers and salary arrears as % of expenditure.	
Procurement	- The MOF approved the Charter of the PrMO. - The PrMO developed the draft Procurement Manual, including the standard bidding documents.	- The PrMO prepared and circulated the [Harmonised Procurement Manual, including] standard bidding documents.	- The PrMO will establish an electronic procurement website and bulletin; and a procurement benchmarking, monitoring and evaluation system.	Outcome: Enhanced efficiency and transparency of national procurement system. Indicator: % of public procurement through competitive procedures.	
C. Provinces		- The MOF initiated preparation of an issues paper on Budget Law revision, including a discussion of options for revenue and expenditure apportionment and inter-governmental fiscal transfers.	- The revised Budget Law will be submitted to the National Assembly, including clarification of revenue and expenditure apportionment and intergovernmental transfers.	Outcome: Increased coherence between provincial expenditure allocation and the NGPES priorities. Indicators: NGPES sectors as % of provincial expenditure; provincial % variation in NGPES sector spending per capita.	NGPES - Part 1, Chapter 2, Chapter 3, Chapter 7 - Part 3, Chapter 1 - Part 5, Chapter 1, Chapter 3 CAS - Objective 2.1
1.2 Strengthening the banking sector					

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
A. State-owned banks	<p>- The BOL submitted to the MOF the independent IAS audits of the 2003 accounts for the BCEL and LDB.</p> <p>- The APB submitted the draft independent IAS audit of its 2003 accounts to the BOL.</p>	<p>[- The BOL submitted to the MOF the independent IAS 2004 audits for the BCEL and LDB and procured an auditor for the IAS 2004 audits for the APB.]</p> <p>[- The MOF appointed qualified MOF representatives to the Boards of the BCEL, LDB and APB.]</p> <p>[- The MOF, BOL and SCBs agreed on revised Governance Agreements and recapitalisation plans for SCBs.]</p>	<p>- The BOL will submit to the MOF the independent IAS 2005 audits for the BCEL, LDB and APB within six months of the end of the year and follow up the recommendations made in the 2004 audits.</p> <p>- The Bank Restructuring Committee will ensure progress towards full compliance with revised Governance Agreements and recapitalisation plans for SCBs, taking appropriate steps to deal with non-compliance.</p>	<p>Outcome: Enhanced commercialisation and transparency of State-owned banks.</p> <p>Indicators: % NPL reduction; % NPL from new risk activities and breakdown; number of risk activities approved without IBA concurrence; reduction in concentration; % growth in risk activities.</p>	<p>NGPES - Part 4, Chapter 5, Section 5.7</p> <p>CAS - Objective 2.1</p>
1.3 Improving the performance of State-owned enterprises					

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
A. Enterprise restructuring	<ul style="list-style-type: none"> - The Government completed State audits for FY 03 for Lao Airlines (LA), Nam Papa Lao (NPNL) and Pharmaceutical Factory 3 (PH3). - The BPO issued calls for EOI for an independent IAS audit of Lao Airline, NPL, PH3 and BPKP for FY 2004. - The Government carried out the restructuring of Lao Airlines and BPKP as per the restructuring plan and Notice No 059/CPMO of 29 April 2004. - The Government approved the SAMD (MOF) performance monitoring and assessment for all SOEs for FY 03. 	<ul style="list-style-type: none"> - The Government launched independent external audits of the financial accounts for FY 04 for Lao Airlines (LA), Nam Papa Lao (NPNL), Pharmaceutical Factory 3 (PH3) and Bolisat Pattana Khet Poudoi (BPKP). [- The Prime Minister's Office (PMO) prepared restructuring plans for the DAFI Group, Agriculture Industry Development Import-Export State-Owned Enterprise (DAI), Lao State Fuel Company (LSFC), Société Lao Import-Export (SLIE), Road Bridge Construction Company No 13 (CC13) as per Notice No 059/CPMO of 29 April 2004.] - The Government approved restructuring and started to prepare restructuring plans for 4 of the 14 non-performing SOEs identified in the State Asset Management Department's 2003 assessment: Lane Xang Phatthana (LXP), Lat Visahakit Sanong Vatthou Technique (LVSVT), Lat Visahakit Konchak Kasikam (LVKK) and Borisath Phalithaphanh Beton Lao (BPBL). - The Government completed and approved the SAMD performance monitoring and assessment for all SOEs for FY 04. 	<ul style="list-style-type: none"> - The Government will complete independent external audits of financial accounts for FY 05 for the DAFI Group, DAI, LSFC, SLIE and CC13. - The Government will approve the restructuring plans for the DAFI Group, DAI, LSFC, SLIE and CC13 and for LXP, LVSVT, LVKK and BPBL. - The Government will ensure that SOEs make progress in implementing approved restructuring plans. - The Government will complete and approve SAMD performance monitoring and assessment for all SOEs for FY 05. 	<p>Outcome: Reduced SOE losses, greater transparency and commercial viability of SOEs.</p> <p>Indicators: Less than 20% of all SOEs loss-making; combined annual loss of loss-making SOEs reduced from 200 billion kip for FY 2003 to less than 100 billion kip by FY 2007; effective mechanism to handle SOE liquidation in place and operational.</p>	<p>NGPES - Part 4, Chapter 5, Section 5.8</p> <p>CAS - Objective 2.1</p>

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
1.4 Financial sustainability of utilities					
A. Tariffs	<p>- All provincial government authorities adjusted urban water supply tariffs towards full cost recovery, in line with the National Water Supply Tariff Policy, Decree No 57/PM, dated 7 May 2004.</p> <p>- Electricité du Laos and MIH presented their Tariff Action Plan to the Prime Minister's Office.</p>	<p>- The Government adopted an action plan for financial sustainability of the power sector to ensure the continued financial viability of Electricité du Laos.</p> <p>- The Government implemented first-phase reform measures under the power sector action plan.</p> <p>- The Government promulgated the Decree on Regulation of Urban Water Supply Operations.</p>	<p>- The Government and Electricité du Laos will implement successive phases of the power sector action plan.</p> <p>The Government will implement successive phases of water tariff revision.</p>	<p>Outcome: Increased efficiency and sustainability of the utilities sector.</p> <p>Indicator: % of cost recovery.</p>	<p>NGPES</p> <p>- Part 3, Chapter 4</p> <p>- Part 4, Chapter 5, Section 5.1</p> <p>CAS</p> <p>- Objective 2.1</p>
Component 2: Public expenditure policies					
2.1 Aligning spending with pro-poor NGPES/NSEDP priorities					
A. Health Budget resources	<p>- The CPI and MOH initiated costing and planning of priority health programmes, as identified in the NGPES.</p>	<p>[- The MOF, PMO and MOH ensured that costing and prioritisation of health programmes are reflected in the budget allocations for FY 2005-06.]</p>	<p>- The MOF, MOH, MOE and provinces will pilot specific budget allocations for education and health programmes in each province.</p>	<p>Outcome: Improved intermediate health indicators; better expenditure planning and execution for health priority programmes.</p>	<p>NGPES</p> <p>- Part 1, Chapter 4, Section 4.2, Chapter 7</p> <p>CAS</p> <p>- Objective 2.1</p>
Intra-sectoral allocation	<p>- The MOF allocated 5.5% of the total State budget (including external financing) to the health sector in FY 2004-05.</p>	<p>[- The MOF, PMO and MOH ensured that the allocations to health programmes delivered via district hospitals and health centres increased as a share of total health spending in FY 2005-06 relative to FY 2004-05.]</p>		<p>Indicators: Increased % of budget – with and without external financing - devoted to health (planned and actual); increased % of health expenditure going to district hospitals and health centres.</p> <p>Increased % of recurrent</p>	

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Recurrent costs and incentives for providers	- The MOH has paid the salaries of health care workers so that no more than 20% of health care workers' salaries remaining due had been outstanding for more than 2 months.	[- The Government paid the salaries of health care workers so that no more than 10% of health care workers' salaries remaining due had been outstanding for more than 1 month.]	- The Government will continue to pay the salaries of health care workers and teachers so that no more than 10% of salaries remaining due will have been outstanding for more than 1 month.	expenditure in the health budget; no delays in the payment of health workers' salaries	NGPES - Part 1, Chapter 4, Section 4.2, Chapter 7 CAS - Objective 2.1
[A. Health (cont/d)] Cost recovery and financing for the poor		- The National Assembly approved the Curative Health Law (October 2005) - The MOH reviewed the current system of exemption from payment of fees. - The MOH piloted the use of equity funds to subsidise services provided to the poor.	- The MOH will issue implementing instructions and decrees for the new Curative Health Law. - The MOF will issue and implement revised Decree 52 on health cost recovery. - The MOH will evaluate the results of pilot equity funds with a view to scaling-up.	Outcome: Improved access to basic health services for the poor. Indicators: Available fee payment options targeted at the poor population; number of pilot equity funds and community health insurance schemes implemented.	NGPES - Part 1, Chapter 4, Section 4.2, Chapter 7 CAS - Objective 2.1

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
<p>B. Education</p> <p>Budget resources</p> <p>Allocation of expenditure</p>	<p>- The CPI and MOE initiated costing and planning of priority education programmes as identified in the NGPES.</p> <p>- The MOF allocated 11% of the total State budget (including external financing) to the education sector in FY 2004-05.</p> <p>- The MOF and MOE increased and maintained the share of expenditure going to primary education to 50% of total education expenditure in FY 2003-04.</p>	<p>[- The MOF and MOE ensured that costing and prioritisation of education programmes are reflected in the budget allocations for FY 2005-06.]</p> <p>[- The MOF and MOE increased the FY 2005-06 allocation to primary education as a share of total education spending, relative to FY 2004-05.]</p>	<p>- The MOF, MOH, MOE and provinces will pilot specific budget allocations for education and health programmes in each province.</p>	<p>Outcome: Improved intermediate education indicators; strengthened expenditure planning and execution for education priority programmes; improved access to complete primary education and lower secondary education for the poor.</p> <p>Indicators: Increased % of budget – with and without external financing – devoted to education; increased % of education budget going to primary education; increased % of recurrent expenditure in education budget; no delays in payment of teachers' salaries; improved textbook/student ratios; pilot community school grant programme implemented.</p>	<p>NGPES</p> <p>- Part 4, Chapters 2 & 3</p> <p>CAS</p> <p>- Objective 2.2</p>

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
[B. Education (cont/d)]	- The Government paid the salaries of teachers so that no more than 20% of teachers' salaries remaining due had been outstanding for more than 2 months.	[- The Government paid the salaries of teachers so that no more than 10% of teachers' salaries remaining due had been outstanding for more than 1 month.] - The MOE initiated its multi-annual textbook publishing programme.	- The Government will continue to pay the salaries of teachers and health care workers so that no more than 10% of salaries remaining due have been outstanding for more than 1 month. - The MOE will finalise and approve a policy on ensuring appropriate teaching staff for schools in remote areas. - The MOE will draft and adopt an integrated framework and plan for development of an Education Management Information System (EMIS).		NGPES - Part 4, Chapter 2 & 3 CAS - Objective 2.2
Recurrent costs: Teachers' pay Incentives for providers Financing for the poor					
C. Infrastructure Rural electrification		- The MIH released the Off-grid Fund to establish a Rural Electrification Fund. [- The MIH contracted out management of the Rural Electrification Fund through a "Management Contract".]	- The MIH will present to PMO a plan for opening the Rural Electrification Fund to donors and private investors.	Outcome: Expanded access to infrastructure services; sustainable financing of infrastructure. Indicator: % of rural population with access to electricity.	NGPES - Part 1, Chapter 4, Section 4.3 - Part 4, Chapter 4. CAS - Objective 1.2

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Town and rural water supply and sanitation		- The MCTPC drafted a Water Supply Law, also addressing sanitation and taking into account customary tribal and ethnic law through extensive nationwide field research.	- The MCTPC will submit draft legislation on water supply and sanitation to the National Assembly.	Outcome: Improved quality and access to water supply. Indicators: Private-sector water supply providers servicing at least 8 poor small towns by 2008 (10% of towns not served).	NGPES - Part 1, Chapter 4, Chapter 5 - Part 4, Chapter 3, Chapter 8 CAS - Objective 1.2 - Objective 2.1
[C. Infrastructure (cont/d)] Transport	- The MCTPC set the minimum fuel levy for the Road Maintenance Fund at 100 Kips/litre.	- The MCTPC increased the fuel levy for the Road Maintenance Fund to 150 Kips/litre. - The MCTPC updated the road maintenance plan covering national and provincial roads. - The MCTPC prepared a draft policy statement on rural transport services.	- The MCTPC will increase the fuel levy for the Road Maintenance Fund to at least 200 Kips/litre. - The MCTPC will update the road maintenance plan covering national and provincial roads. - The MCTPC will prepare a draft ministerial directive on rural transport services.	Outcome: Improved maintenance of roads. Indicator: Routine maintenance on at least 90 percent and periodic maintenance on at least 8 percent of the national and provincial road networks are funded by domestic revenue, including revenue from road users (Road Maintenance Fund).	NGPES - Part 1, Chapter 2 - Part 4, Chapter 4 CAS - Objective 3.1
D. Pay reform		[- The PMO and MOF carried out a study on pay reform options.] [- The MOF made provision for pay reform in the MTEF forward estimates.]	- The PMO will conduct a civil service census as the baseline for a new civil service database. - The PMO and MOF will prepare a civil service pay and employment policy.	Outcome: Increased remuneration of civil servants consistent with increased output in efficiency. Indicator: Civil service pay as % of private-sector comparators.	NGPES - Part 3, Chapter 3 CAS - Objective 2.1
2.2 Monitoring alignment of spending with pro-poor NGPES priorities					

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
A. Tracking public spending	- The MOF, MOH, MOE and NSC launched the Public Expenditure Tracking Survey (PETS) on health and education.	- The MOF, MOH, MOE and NSC conducted the fieldwork for the [PETS and] Public Expenditure Review (PER).	- The MOF, MOH, MOE and NSC will report on the PETS and PER findings and launch preparations for further PETS and PER.	Outcome: Policymakers better informed about the effectiveness of social sector spending; enhanced transparency and accountability.	NGPES - Part 1, Chapter 7 - Part 2, Chapter 5 CAS - Objective 2.1
B. Poverty data		- The CPI approved and issued a Statistical Strategy consistent with international standards on producing and disseminating data.	- The National Statistical Centre will remain on track with implementing the Statistical Strategy.	Indicator: Regular dissemination and analysis of data.	NGPES - Part 2, Chapter 5 CAS - Objective 3.3
Component 3. Sustainable growth					
3.1 Strengthening private-sector development					
A. Business Environment Legal framework	- The National Assembly enacted the Revised Domestic and Foreign Investment Laws. - The CPI drafted Decrees implementing the Investment Laws. - The MOC prepared draft amendments to key business laws in consultation with the private sector (e.g. 1995 Business Law).	- The Government issued implementing decrees for Investment Laws and amended implementing regulations in line with the revised legislation. - The National Assembly approved amendments to the 1994 Business Law. - The Government drafted a policy framework and regulation to promote sustainable private investment in mining.	- The Government will make progress with implementation of the revised Enterprise Law. - The Government will adopt a strategy for SME development. - The MOF will submit a draft Accounting Law to the National Assembly. - The Government will submit a Standards Law to the National Assembly and ensure that there is no conflict between the new legislation and the Enterprise Law.	Outcome: Enhanced competitive environment for private-sector development. Indicator: Reduce number of days to start up a business from 198 to under 100 days.	NGPES - Part 1, Chapter 2 - Part 3, Chapter 2, Section 2.2 CAS - Objective 1.1

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
Dialogue between the Government and the private sector	- Government agreed with the private sector on a regular semi-annual consultation mechanism.	- The Government prepared the first semi-annual business forums with central and provincial private-sector focus groups.	- The Government will conduct the first semi-annual business forum.	Outcome: Greater confidence amongst private-sector operators. Indicator: Institutionalised consultations between the private sector and policymakers at central and provincial levels.	NGPES - Part 3, Chapter 2, Section 2.2 CAS - Objective 1.1
B. Financial sector	- The PM's Office submitted the amendment to the Decree of the President on Commercial Banks to the relevant Standing Committee of the National Assembly. - The BOL disseminated the Rural and Microfinance Policy and Action Plan in three provinces.	- The BOL issued the Microfinance Regulation to implement the Rural and Microfinance Policy and Action Plan. - In May 2005 the National Assembly approved the revised Secured Transaction Law which came into force in August 2005.	- The BOL will draft proposals to amend laws and regulations impeding competition by non-State financial institutions. - The BOL will develop proposals to strengthen monitoring of financial indicators for the private domestic banking sector.	Outcome: Increased diversity and competition of non-State financial institutions. Indicators: Increasing share of (i) State banks' credits to private sector; (ii) non-State financial institutions' credits.	NGPES - Part 3, Chapter 2 - Part 4, Chapter 5, Section 5.6 CAS - Objective 1.1
3.2 Accelerating regional and global integration					
A. Trade	- Prime Ministerial Decree on Trade Competition was issued. - The Government continued to implement commitments under AFTA, including moving 435 items into the Inclusion List (IL), raising coverage of tariff lines to 84% and reducing tariffs to 0-5% on 87% of the IL tariff lines.	- The Government initiated preparation of checklist documents required for WTO accession. - The Government continued to implement its AFTA commitments, including reduction of tariffs to 0-5% in the Inclusion List.	- The Government will make progress towards WTO accession and stay on track with AFTA commitments.	Outcome: Greater liberalisation of trade. Indicators: Level of tariffs on imports down to 0-20% by 2005 and 0-5% by 2008.	NGPES - Part 1, Chapter 2 - Part 4, Chapter 5, Section 5.9 CAS - Objective 1.1
3.3 Improving resource management					

POLICY AREA	PRSO1 ACTION COMPLETED (January 2005) (Prior action in bold)	PRSO2 ACTION [COMPLETED] (February 2006) (Prior action in bold)	PRSO3 ACTION EXPECTED (February 2007) (Triggers in bold)	EXPECTED END-OF-SERIES OUTCOMES AND INDICATORS (from first of programme document series)	LINKS WITH NGPES AND CAS
A. Revenue management		- The National Assembly approved the new Customs Law.	- The Government will issue implementing decrees and regulations for the new Customs Law.	Outcome: Strengthening fiscal policy and tax collection. Indicator: by 2008 14% of GDP in fiscal revenue.	NGPES - Part 1, Chapters 2 and 7 - Part 3, Chapter 1 Part 5, Chapters 1 and 2 CAS - Objective 3
B. Forest management	- The MAF completed the requirements for independent certification of sustainable forest management in pilot village forests in the Khammouane and Savannakhet provinces.	- The Forest Sector Monitoring System was established and ready to field-test.	-The Forest Sector Monitoring System will be field-tested in four pilot provinces. - The Government policy and action plan for timber marketing and revenue sharing will be finalised.	Outcome: Enhanced sustainability and participation in forest management. Indicator: Coverage of sustainable forest management plans to 528 000 hectares.	NGPES - Part 1, Chapter 5 - Part 4, Chapter 1 CAS - Objective 1.3