Japanese ODA Loan

Ex-Ante Evaluation (for Japanese ODA Loan)

1. Name of the Project

Country: Lao People's Democratic Republic

Project: Budget Strengthening Support Loan

Loan Agreement: November 9, 2009

Loan Amount: 1,500 million Yen

Borrower: The Government of Lao PDR

2. Background and Necessity of the Project

(1) Current State and Issues in Lao PDR

The government of Lao PDR introduced a policy called "Chintanakan Mai" (New Thinking) in 1986 and actively promoted the introduction of market economy principles and other open-economy policies under the New Economic Mechanism. As one of the least developed countries (LDC) of the ASEAN, Laos still has many development issues to address. Nevertheless, it has maintained high economic growth rates, and is proactively addressing various issues relating to poverty reduction and economic growth, so that it may achieve its long-term goal of graduating from LDC status by 2020.

Laos has achieved GDP growth rates exceeding 7% for four consecutive years from 2005, and is assumed to have reached 7.2% in 2008. However, although the global financial crisis did not directly impact the country, the indirect impacts of the crisis have had a large effect on the country's economy. Tourism income has dropped, export and resource revenues have fallen due to the drop in prices for natural resources, and overseas direct investments have been postponed. The deterioration of the country's finances and international trade balance appears inevitable. The country's budget deficit for fiscal 2008-09 is expected to correspond to about 6.7% of GDP due to a shortfall in revenue and the extrabudgetary expenditure by the Central Bank of Laos in the face of the financial crisis. The deficit for fiscal 2009-10 is expected to be about 4.4% of GDP. Of these expected budget deficits, the Laotian government has no prospect of procuring funds for about 60 to 70 million USD worth of the deficit for fiscal 2008-09. While it is considering a wide range of measures on both the expenditure and revenue sides, domestic means for fund procurement are limited, and overseas bond issuance is difficult in terms of credit capability. Thus, Laos has little choice but to depend on donor assistance to bridge its financial gaps.

(2) Development Policies in Lao PDR and the Priority of the Project

In the Sixth National Socio-Economic Development Plan (NSEDP) for the five years from 2006 to 2010, the Laotian government established policies for a number of priority issues, including improvement of the investment and business climate, development of small and medium enterprises, trade expansion and integration into global economy, financial sector reforms, and administrative reforms. NSEDP 2006-2010 was formulated based on the national goal of graduating from LDC status by 2020, which was adopted by the government at the Sixth Party Congress held in 1996. The World Bank and the International Monetary Fund (IMF) have acknowledged the NSEDP as providing a basis for a Poverty Reduction Strategy Paper (PRSP), and have launched the Poverty Reduction Support Operation (PRSO) with an emphasis on ① sustainable growth, proper management of natural resources and trade promotion based on improvement of the investment climate, and ② institutional reforms for improved public finance management systems and public services. This loan project aims to support the implementation of these important policy reforms.

(3) Japan and JICA's Policy and Operations

The Laotian Ministry of Finance introduced a new budget law and a new accounting system in 2005, and is implementing reforms relating to public finance management, including the centralization of tax services, tariffs, and national treasury. Its main focus is to build capacities in the central and local governments to operate the new systems once the reforms are completed. In the investment area, various issues still need to be addressed before investors can be offered an attractive investment climate, such as the improvement of opaque and complicated investment procedures and the further development of the existing system which remains undeveloped in many respects. Given this situation, Japan's Country Assistance Program for Laos focuses on "improvement of administrative capacity and institutional building" and "institutional building and human resource development for strengthening the private sector" as Japan's priority areas of assistance. In response to this policy, JICA has formulated its own Country Assistance Program for Laos, which identifies "administrative and financial reforms and public finance management" and "development of investment and export promotion environments" as two main development issues in its assistance for the capacity building of the central and local governments in Laos. This project therefore fundamentally conforms to Japan and JICA's assistance policies.

(Major achievements)

- Technical cooperation projects: Project on Support to Trade Promotion (FY2008-2011); Capacity Building Project for Public Investment Management Program (FY2005-2007); Project for Enhancing Capacity on PIP Management (FY2007-2010); Project for Capacity Building for Public Financial Management Strengthening Program (FY2008-2011), etc.
- ODA loans: PRSO2 (loan agreement for 500 million Yen, FY2006); PRSO3 (loan agreement for 500 million Yen, FY2007)

(4) Other Donors' Activity

Comprehensive programs for enhancing public finance management are being implemented by the World Bank, EC, ADB, SIDA, and France and JICA is implementing its cooperation in line with these programs. The World Bank, EC, and AusAid are also providing assistance through the PRSO.

(5) Necessity of the Project

The project aims to bridge the financial gap that has occurred accompanying the decrease in tax revenues due to the economic crisis, and to contribute to the sustainable development of Laos by supporting the implementation of the PRSO and other administrative and financial reforms that are being pursued by the Laotian government based on the NSEDP. As there are concerns about the impacts of the financial and economic crisis on the country's economy, JICA's support of the project is both highly necessary and relevant.

3. Project Description

(1) Project Objective

The objective of the project is to help Laos achieve sustainable economic growth and reduce poverty by working together with the World Bank and other donors in supporting the policy aspects of the Laotian government, which suffers a revenue-expenditure imbalance as a result of the global financial and economic crisis, and by promoting the various policy and institutional reforms that are being pursued by the government based on the NSEDP (administrative and financial reforms, improvement of the investment and business climate, trade expansion and integration into global economy, financial sector reforms, etc.), through direct support of the country's finances.

(2) Project Site/Target Area

The entire country of Laos

(3) Project Components

In accordance with the PRSO Phase 2 (PRSO4-7) matrix which was formulated based on the NSEDP, the project will promote the following eight reform areas with the aim of ①promoting sustainable growth and trade through improvement of the investment climate and ②enhancing public finance management systems and public services: ① improvement of the business climate and investment attraction; ② implementation of international/regional trade agreements; ③ the performance and monitoring of state-owned enterprises (SOEs); ④ transparency and commercial viability of state-owned commercial banks; ⑤budget planning and budget reports; ⑥ budget hearings and budget use; ⑦ implementation of a financial auditing system; and ⑧ provision of public services (healthcare, education).

(4) Estimated Project Cost (Loan Amount)

Total donor assistance for PRSO5: approx. 40 million USD (planned) (including ODA loans worth 1,500 million Yen)

(5) Schedule

The loan is planned for execution in December 2009. The project period corresponds to the period covered by PRSO5, from April 2008 to the end of March 2009 (12 months). It shall be completed with the completion of the loan procedure in December 2009.

(6) Project Implementation Structure

1) Borrower: The Government of Lao People's Democratic Republic
2) Executing Agency: Ministry of Finance
3) Operation and Maintenance System: The Ministry of Finance will be responsible for monitoring and reporting on the progress of the reforms.

(7) Environmental and Social Consideration/Poverty Reduction/Social Development

1) Environmental and Social Consideration

① Category: C

② Reason for Categorization

The project is classified as Category C, because it applies (provides financial assistance) to a sector in which no particular environmental impact is expected, and because it does not have characteristics that are liable to cause adverse impacts nor is it located in a sensitive area as defined in the "JBIC Guidelines for Confirmation of Environmental and Social Considerations" (April 2002).

2) Promotion of Poverty Reduction

The project contributes to poverty reduction by securing a proper budget for the education and health sectors.

3) Promotion of Social Development (e.g. Gender Perspective, Measure for Infectious Diseases including HIV/AIDS, Participatory Development, Consideration for the Handicapped, etc.)

None

(8) Collaboration with Other Donors

The loan will be provided as a joint financing with the World Bank, EU and AusAid, and future actions will be monitored also in cooperation with these donors.

(9) Other Important Issues

None

4. Targeted Outcomes

(1) Performance Indicators (Operation and Effect Indicator)

In consideration of the Japanese government's sectors of interest, targets that are strongly relevant to JICA's assistance projects and studies and their indicators will be established as indicators of operation and effectiveness, as shown below.

Indicator	Baseline (Actual Value in 2006)	Target (2011) [Expected Value at Completion of PRSO7]
1. Improvement of the business climate, investment attraction		
No. of days required to establish a company	163	70
Company registration rate (percentage of new registrations to the total)	NA	10% increase/year
2. Implementation of international/regional trade agreements		
No. of days required to export/import goods	Export: 66 Import: 78	Export: 32 Import: 33
No. of documents required to export/import goods	Export: 12 Import: 16	Export: 7 Import: 8
Ratio of total trade to GDP (%)	69%	78%
3. Performance and monitoring of state-owned enterprises (SOEs)		
No. of deficit-ridden SOEs (primary to tertiary)	13	Reduction by half
Profit-loss ratio of deficit-ridden SOEs	42%	20%
Amount of unpaid electricity charges to be paid to EDL by the Laotian government	113 billion Kip	0
4. Transparency and commercial viability of state-owned commercial banks		
Total ratio of nonperforming loans in the state-owned bank system	21.2%	< 5%
Total loans to the private sector	71.6%	Maintain at 80% or higher
5. Provision of public services (healthcare, education)		
Total primary school enrolment rate in the 47 priority districts	28.4%	Increase to a rate over 28.4%
Ratio of ordinary healthcare budget expenditure to total ordinary budget expenditure	3.9%	Increase to a rate over 3.9%

(2) Internal Rate of Return: Not applicable

5. External Factors and Risk Control

Delays beyond the control of the administrative body may occur particularly in policy and institutional improvements that accompany legislative procedures, and may affect the progress of the project as a whole.

6. Lessons Learned from Past Projects

The Laotian government and the World Bank have assessed the overall effectiveness of the previous first series of PRSO (PRSO1-3) in 2007, and have verified that it has contributed significantly to improving policy systems in Laos, such as by enhancing public expenditure management capacity and finance management capacity, including the centralization of fiscal revenue, and by promoting investment through the revision of company laws and foreign investment laws.

At the same time, however, past PRSO schemes were not without problems. For example, a discrepancy emerged between the new company law and foreign investment promotion law, and the lack of a proper network among customs authorities impeded the actual enforcement of regulations relating to customs and tax authorities which had come into force. This experience underscored the need to assess the mutual compatibility of different laws and the implementation capacity of customs authorities through TA. Therefore, this project will not only identify triggers and assess the achievement of actions, but will also heed derived issues and consider potential needs to dispatch experts.

Joint financing projects in the form of financial support schemes like the PRSO tend to involve many players. Therefore, careful consideration is needed to ensure effective communication among all relevant parties on both the donor side and the host government side, and to consistently share a common understanding of all matters concerning the project. Based on this awareness, the project will continue to be implemented through consultations with the Laotian government, the World Bank and other donors in the process of monitoring and assessing reform items, and efforts will be made to share information, adjust program details as necessary, and maintain a consensus. Furthermore, the monitoring framework will be strengthened by dispatching experts as appropriate.

7. Plan for Future Evaluation

(1) Indicators to be Used

1) Reduced number of days required to establish a company
2) Company registration rate (percentage of new registrations to the total)
3) Reduced number of days required to import/export goods
4) Reduced number of documents required to import/export goods
5) Total trade to GDP (%)
6) Number of deficit-ridden SOEs
7) Total annual loss of deficit-ridden SOEs

8) Amount of unpaid electricity charges by the government
9) Total ratio of nonperforming loans in the state-owned bank system
10) Loans to the private sector
11) Total primary school enrolment rate in the 47 priority districts
12) Ratio of ordinary healthcare budget expenditure to total ordinary budget expenditure

(2) Timing

Upon completion of PRSO7 (to be implemented in conjunction with the evaluation process by the World Bank)