

Background Paper

**TRADE AND INVESTMENT BETWEEN
LAOS AND INDIA: PAST, PRESENT AND FUTURE
PROSPECTS**

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TRADE AND INVESTMENT BETWEEN LAOS AND INDIA: PAST, PRESENT AND PROSPECTS

INTRODUCTION

India and Laos signed a contract on economy and trade cooperation on November 9, 2000, and the contract has been in effect since December 21, 2001¹. The relationship on trade between India and Laos in the past has shown that some businessmen of India propose sales of some products, namely agricultural machinery, electronic equipment, medicine, computer, office appliances, and others. India also shows interest on purchasing some products from Laos, such as phosphate, precious stones, wood products, (namman yang), and etc. Besides, there are some interests on establishing weaving factory, cement factory, and vegetable oil factory in the Lao P.D.R. The products that Laos currently export to India is very limited, only some mineral. The total export from Laos in 2002 was 60,219 US dollars while the import from India was 40,219 US dollars, and export value was US \$18,000

Trade relationship between Laos and India has not been expanded as it should have been. This is due to the fact that there is difficulty in transportation; the product of India has not yet been widely known in Lao market; and the communication between Lao and Indian businessmen has not been well-cooperated.

This paper will first present a brief overview of Lao economy. Secondly, it will raise foreign trade, trade policy and export issues. Then, the foreign direct policy environment in Laos will be discussed followed by India and Lao trade relations and conclusion.

1. AN OVERVIEW OF LAO ECONOMY

The economic reform² from a centralized, planned economy toward an open, liberalized, market-oriented economic system was launched in 1986. This reform had led to strong revival of economic growth, rapid increase in employment, reduction in poverty, a boom in exports and a decline in inflation. Reforms of the external sector, and the consequent achievements on the balance of payments front, have played a key role in the turnaround in the growth of GDP, employment and social indicators. The country's external debt situation has improved markedly in the past few years. The growth of external debt between 1991 and 1995 averaged US\$ 2.2 billion per annum, compared to the much higher average annual increase of US\$ 4.9 billion a year, between end-March 1986 and end-March 1991.

The economy is dominated by subsistence agriculture, with a low level of monetization. Agricultural output is limited by weak infrastructure and unsophisticated production

¹ Minutes of the Fourth Meetings of India-Laos Joint Commission on Trade, Economics, Scientific and Technological Cooperation held in New Delhi on 22-23 July, 2002

² Lao Economic Reform "New Mechanism" adoption 1986 and Laws on the Promotion and Management of Foreign Investment

methods, and is vulnerable to weather conditions. The agriculture sector employs over 80 percent of the population, and contributes 53 percent of GDP.

Considerable progress has been made since 1986 in the shift from centrally planning toward market-oriented economic structure. The economy has continually expanded (albeit from a very small base). A market-based price system is in place for most products, the currency has been floated and a fledgling private sector is growing in confidence. A number of banking and state enterprise reforms are gradually being introduced, with assistance from the World Bank and Asian Development Bank (ADB). However current high levels of debt in the financial sector continue to hamper macroeconomic stability. A privatization program was initiated in the 1990s with the aim of improving economic efficiency and freeing state coffers from propping up inefficient state enterprises. This latter process has slowed in recent years, and numerous enterprises remain in government hands.

The industry and service sector now account for almost half of GDP growth, with key economic activity focused in electricity production, handicrafts, foodstuffs, chemical production and mining. Tourist numbers increased significantly in the late 1990s, with the Lao National Tourism Authority anticipating around 747,000 tourist arrivals in 2004, making tourism one of Lao biggest sources of foreign exchange.

The current account deficit is forecasted to be 3.2 percent of GDP in 2004. Gross international reserves have been increasing steadily and, according to the International Monetary Fund (IMF), are expected to reach US\$228 million by 2004, equivalent to approximately 4 months of imports.

By mid-2000, the Lao economy had largely recovered from the triple-digit inflation levels and drastic currency devaluation that occurred in the late 1990s. This was partly as a result of the imposition of stringent fiscal measures, as well as downward pressure on food prices resulting from good rice harvests. Average inflation, which reached 128 percent in 1999, was reduced to single figures by 2002, but climbed to almost 18 percent between March and May 2003. It is expected to fall again to 12.3 percent in 2004.

The introduction of more attractive foreign investment legislation has led to increased foreign investment inflows, particularly in the hydroelectricity and mining sectors. One private sector consortium is planning to develop a large hydropower project, Nam Theun II worth about US\$1.1 billion but a number of issues are yet to be resolved. Lao foreign investment regulations are among the more opening in the region and tariffs are relatively low. However, trade and investment are heavily regulated, including through import and export licensing.

The small size of the Lao economy makes it particularly vulnerable to internal policy settings and external shocks. Significant structure impediments to further economic development include inadequate physical infrastructure, and underdeveloped human processes are increasing as institutional capacity is stretched to its limits in specific areas required by government.

By 2001, the Lao GDP growth rate stood at 5.5%. Since the late 1980s, the government's economic policy has been to rapidly move from a centralized, planned economy toward an open, liberalized, market-oriented economic system. The foreign exchange markets have been opened and the kip floats freely based on supply and demand in relationship to the exchange rate in the "parallel market". Formal exchange controls have been lifted.

In 1995, the Lao currency (kip) started to devalue. The value of kip against US dollar fell from 726 kip per 1USD in 1994 to 936 kip per 1 USD in 1995. In August 1999, kip reached its lowest point, being traded at a market price of 9,705 per 1 USD. After critical point, the value of kip began to increase and stabilize. From January to October 2000, the exchange rate of kip against USD was bouncing in a narrow margin with an average rate of 7,894.4 kip per 1 USD.

By April 2003, the exchange rate was 10,660 kip 1 USD. The average consumer price index in Laos from 1988 to 1997 was 20,447%. After the Asian financial crisis erupted, the value of kip fell sharply. As a result, inflation rate rapidly increased. In 1998, the inflation began to ease. According to the Bank of Lao PDR, the average inflation rate of the year 2000 was 30%. In 2001, consumer price inflation was at 7.8%.

Table 1: GDP growth and volume of Merchandise Trade, 1992 – 2001

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|------|------|------|-------|------|-------|--------|-------|-------|------|
| Real GDP growth % | 7.0 | 5.9 | 8.1 | 7.0 | 6.8 | 6.9 | 4.0 | 7.3 | 5.7 | 5.5 |
| Average inflation % | 6.00 | 8.94 | 6.78 | 25.66 | 7.28 | 26.60 | 141.97 | 86.46 | 30.00 | 7.8 |
| Yearly average exchange rate (kip/US\$) | 725 | 722 | 722 | 936 | 938 | 1321 | 3422 | 7438 | 7809 | n/a |

Laos joined ASEAN in 1997 and is a member country of the World Bank, the Asian Development Bank (ADB), and the International Monetary Fund (IMF), and is in the process of applying to join the World Trade Organization (WTO). Tariffs in Laos are below the average rate of the ASEAN countries. Over 60% of recorded imports enter the country under some form of incentive duty reduction scheme. There are no price controls in Laos, although there is government supervision in pricing of petroleum products and electricity and telecommunications rates. Imports still exceed exports while exports have more rapidly expanded.

CONTRIBUTION OF GDP BY SECTORS

GDP structure at constant price in 2000 consisted of 51.8% shared by agriculture, 22.6% shares by industry and 25% share by service. There was a downward trend in agriculture sector share, despite of an increase in its output of 3.8% in 2001, 4% in 2002, and 2.2% in 2003. The agricultural sector shared to GDP decreased to 50.8%, 49.9% and 48.2% in 2001, 2002, and 2003 respectively. Industrial sector, in contrast, continuously increased, to 23.5% in 2001, 24.4% in 2002, and 25.7% in 2003. There were minor changes in service sector, with the share of 25% in 2001, 24.9% in 2002, and 25.3% in 2003. In industrial sector, the major contributor is processing industry, whose share constantly increased in the past three years, from 16.8% in 2000, to 17.8% in 2001, 18.8% in 2002, and 19% in 2003.

Table 2: Balance of Trade and Current Account

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|------|------|
| Export US\$ million fob | 123.6 | 247.9 | 305.4 | 346.2 | 321.0 | 317.0 | 341.0 | 310.9 | 393 | 425 |
| Imports US\$ million | 253 | 431.9 | 564.1 | 588.8 | 690.0 | 648.0 | 553.0 | 524.6 | 591 | n/a |

Source: Bank of Laos (Various issues)

2. FOREIGN TRADE, TRADE POLICY AND EXPORT INCENTIVES

2.1. COMMERCE AND TRADE

Since 1986, when the Government of the Lao PDR (GOL) adopted its new economic policy, commercial relations with foreign countries have been widely expanded in line with government policy to open up the country.

Laos has trade relations with more than 30 nations around the world. Trade volume has increased in each year by average of 18.7%. Even so, the foreign trade deficit still increases by an average of 15.4% per year. However, trade is active as it can be seen from the trend towards the balance of export and import goods for general use consumption. The difficulty arises from imports for the construction of a basic national economic infrastructure for the development of the economy, and especially for the export.

The important trading partners of the Lao PDR are mainly Asia and Pacific nations, such as Thailand, Vietnam, Japan, China, Singapore, Hong Kong and some European nations like France, Germany, Italy, the United States of America, Russia and others. Lao exports goods are mainly timber products, electricity, gypsum, rattan products, coffee, cardamom, sesame, non-timber forest products, garments and handicraft items.

The goods imported into Laos are mainly foods, fabrics, garments, equipment and machinery for construction work and agriculture, electrical goods, machines, fuels and consumer goods.

2.2. STRUCTURE OF EXPORT AND IMPORT

Lao export structure is increasing and diversifying, and improving the quality of exported products are among the main objectives of the government. A number of new items in the manufacturing and processing sectors have been introduced. The volume of exports had increased substantially from US\$247 million in 1994 to US\$374 million in 2004.

The structure of exported goods had changed over a decade from 1994 to 2004. While wood and wood products, garments and electricity are still important components in total export, their significance had been fluctuated. While garment decreased from 28.6% in 1994 to 19.1% in 2004, Electricity increased dramatically at average increase of 22.1%. Garment had remained one of the most import exports. It had fluctuated at around 29.37% from 1994 to 2004. Gold for export increased sharply from only 2003 to 2004 at 16%.

Commodity Composition of Exports (%) 1995 - 2004

| Major exportation items | 1995/96 | 1996/97 | 1997/98 | 7998/99 | 1999/2000 | 2000/2001 | 2001/2002 | 2002/2003 | 2003/2004 |
|------------------------------------|---------|---------|---------|---------|-----------|-----------|-----------|-----------|-----------|
| Wood and Wood Products | 28.6% | 19.1% | 16.2% | 23.0% | 22.0% | 24.7% | 23.2% | 19.8% | 19.1% |
| Rattan and Bamboo | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 1.0% | 0.0% | 0.3% |
| Coffee | 10.1% | 11.2% | 19.6% | 11.5% | 9.0% | 4.7% | 3.0% | 3.1% | 3.5% |
| Gypsum and other mineral | 0.2% | 0.2% | 0.2% | 0.3% | 1.8% | 1.5% | 1.2% | 13.2% | 1.7% |
| Gold | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 16.3% |
| Benzoin | 0.3% | 0.3% | 0.4% | 0.4% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| Cardamom | 0.1% | 0.1% | 0.1% | 0.1% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| Non Forestry Produced | 0.6% | 1.3% | 0.7% | 0.4% | 1.3% | 2.0% | 2.5% | 1.6% | 0.9% |
| Maize | 0.9% | 1.3% | 1.0% | 0.6% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| Animal/Agricultural | 7.2% | 4.7% | 5.9% | 3.5% | 1.6% | 1.8% | 2.4% | 3.2% | 4.6% |
| Handicrafts | 0.0% | 0.2% | 0.7% | 1.1% | 1.6% | 1.2% | 0.8% | 3.5% | 0.5% |
| Garment | 25.9% | 36.1% | 30.6% | 29.7% | 29.1% | 30.8% | 31.0% | 24.7% | 26.5% |
| Electricity | 12.0% | 12.5% | 13.0% | 21.1% | 33.0% | 28.1% | 28.7% | 27.6% | 23.1% |
| Other products/Industrial Products | 14.1% | 13.2% | 11.5% | 8.3% | 0.6% | 5.2% | 5.3% | 2.0% | 2.9% |
| Others | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.9% | 1.2% | 0.7% |
| Grand Total | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

Commodity Composition of Imports (%) 1995 - 2004

| Major exportation items | 1995/96 | 1996/97 | 1997/98 | 7998/99 | 1999/2000 | 2000/2001 | 2001/2002 | 2002/2003 | 2003/2004 |
|--------------------------------------|---------|---------|---------|---------|-----------|-----------|-----------|-----------|-----------|
| Agriculture & animal equipment | 4.8% | 5.0% | 4.5% | 4.5% | 4.6% | 3.4% | 1.6% | 3.1% | 1.9% |
| Office and sport equipment | 1.4% | 1.4% | 1.4% | 1.3% | 1.3% | 0.4% | 0.8% | 0.7% | 0.1% |
| Commodities (food. Vegetables) | 9.0% | 9.9% | 8.4% | 7.2% | 3.7% | 3.2% | 3.1% | 4.1% | 3.3% |
| Clothes (garment stuff) | 16.0% | 13.1% | 4.7% | 9.8% | 3.2% | 2.0% | 2.5% | 2.5% | 2.8% |
| Electronic and spare part Equipment | 14.4% | 15.4% | 10.9% | 12.3% | 1.3% | 0.5% | 0.6% | 0.7% | 0.7% |
| Construction equipment | 24.0% | 21.8% | 28.2% | 17.3% | 5.7% | 5.7% | 5.3% | 3.9% | 4.4% |
| Fuel and gas | 10.2% | 10.2% | 15.0% | 14.0% | 14.3% | 18.7% | 14.9% | 19.4% | 18.0% |
| Medicine and equipment | 2.7% | 2.9% | 3.4% | 6.6% | 0.6% | 0.8% | 0.5% | 0.3% | 0.6% |
| Vehicles and spare part | 14.6% | 17.8% | 20.4% | 22.4% | 3.9% | 3.7% | 3.5% | 5.2% | 6.4% |
| Luxury products | 0.8% | 1.1% | 1.1% | 1.4% | 0.6% | 0.1% | 0.3% | 0.8% | 0.9% |
| Import of Electricity | 2.1% | 1.5% | 1.9% | 3.1% | 1.5% | 0.8% | 1.3% | 1.4% | 1.7% |
| Other products | 0.0% | 0.0% | 0.0% | 0.0% | 0.9% | 3.4% | 2.6% | 1.3% | 0.7% |
| Import of Garment Raw material | 0.0% | 0.0% | 0.0% | 0.0% | 16.1% | 15.2% | 13.8% | 10.1% | 14.8% |
| Informal Trade | 0.0% | 0.0% | 0.0% | 0.0% | 8.3% | 14.5% | 15.0% | 3.9% | 3.5% |
| Goods for Exhibition | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.4% | 0.0% |
| Industrial goods | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 7.8% | 5.9% |
| Total Import | 0.0% | 0.0% | 0.0% | 0.0% | 66.0% | 72.3% | 65.9% | 65.3% | 65.6% |
| Import of Foreign Investment Project | 0.0% | 0.0% | 0.0% | 0.0% | 34.0% | 27.7% | 34.1% | 34.7% | 34.4% |
| Grand Total Import of Lao PDR | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

However, Lao important imported goods are fuel and gas, garment raw material and foreign investment project machinery. There was a continuous increase in importing of fuel and gas from 1995 to 2004 whereas garment materials and foreign investment project machinery only started from 1999 to 2004. There was a slightly decrease of garment materials from 1995 to 2004 while foreign investment project machinery remained stable at the same time period.

2.3. CHANGE IN TRADE POLICY MEASURES / TRADE POLICY REFORM

Trade policy prior to the introduction of the New Economic Mechanism had been highly restrictive, revolving around the centralized allocation of goods for export. In 1988, however, in line with the New Economic Mechanism, the government began to progressively decentralize some of its trade-oriented responsibilities, including planning and arranging trade contracts with foreign suppliers. Trade, controlled by the ministries of trade and finance, is conducted by about twenty-four state trading companies and some provincial trading companies. Several measures promulgated in March 1988 modified trade policy. According to Decree 16, the government became the sole exporter through state import-export organizations. Under Decree 13, the State Committee for Foreign Economic Relations and Trade, provincial administrative committee, and municipality are empowered to supervise the management and control of import and export activities. The decree also authorizes the trade agents at Lao PDR embassies worldwide to make direct trade contacts.

Decree 18 identifies a number of 'strategic' goods, including coffee, tobacco, wood products such as a timber, sawn wood, pressed wood, and rattan, other forestry product such as benzoin and sticklac, and mineral, for which the state has an export monopoly: in short, all the major export commodities. Only the central government import-export organisation, the Lao Import-Export Company and certain provincial and state enterprises are permitted to export these goods to fulfill national trade agreements with the non-convertible currency area. All importing units are required to submit plans for their trading operations to the State Committee for Foreign Economic Relations and Trade in order to formulate the national import export plan. However, importers are permitted to trade in all commodities not on the strategic or restricted lists. Under Decree 18, export businesses are permitted to export goods on the strategic list directly, after national requirements have been met. The decree thus considerably liberalises trade regulations. The main reason for the restriction on trade in strategic goods is that the government has to plan its supply of export goods to coincide with its multiyear trade arrangements with the non-convertible currency area countries. After 1990, however, this issue was smoot because as trade volume with theses countries dropped to a negligible amount.

The import of certain items, including automobiles and military vehicles, fertilizers, drugs, and 'decadent cultural products and pictures,' is subject to quotas and other restrictions. In addition, trade in certain goods is entirely prohibited, including poisons, weapons, and other goods related to national security.

At the end of the 1980s, the authority of the Lao Import-Export Company had begun to diminish, because import-export licenses were being granted to increasing numbers of private organisations. By 1991, the national trade company was slated for privatization.

2.4. MAJOR TRADING PARTNERS

Lao foreign trade is mainly with other Asian countries. Japan, Singapore, Thailand, China and Vietnam are its trading partners. Regionally, the European Unions ranks second importance. With the change in the pattern of trade, the direction of trade may be changed.

Table 8: Major Trading Partners of Lao PDR (Export) unit in USD

| No. | Countries in ASEAN | 1999-00 | 2000-01 | 2001-02 | 2002-03 | Average growth rate (%) |
|--------------|--------------------|--------------------|--------------------|--------------------|--------------------|-------------------------|
| 1 | Cambodia | 17,623 | - | 53,949 | 118,752 | 0.40 |
| 2 | Indonesia | 1,015,830 | 43,858 | - | 123,746 | 2.39 |
| 3 | Malaysia | 90,710 | 112,412 | 44,678 | 170,688 | 0.61 |
| 4 | Myanmar | 258,377 | - | 17,990 | 241,740 | 0.54 |
| 5 | Philippines | - | 0 | 15,120 | 62,589 | 0.31 |
| 6 | Singapore | 932,922 | 1,034,033 | 145,745 | 161,472,747 | 4.24 |
| 7 | Thailand | 162,995,387 | 146,733,757 | 171,247,058 | 161,472,747 | 0.99 |
| 8 | Vietnam | 23,291,404 | 19,483,447 | 27,040,724 | 21,212,648 | 1.07 |
| Total | | 188,602,253 | 167,407,507 | 198,565,263 | 183,535,174 | 1.01 |

3. INDUSTRY SITUATION IN THE COUNTRY

3.1. INDUSTRY

Reports of the industrial sector's contribution to GDP vary, but most sources find it to be slow increasing, from about 10 percent in 1984 to about 17 percent in 1993. The World Bank estimated the sector's contribution at 14 percent in 1989. Most sources also indicated an increase in the percentage of the labour force employed in the sector from 5 percent in 1970 to 7 percent in 1980. However, World Bank figures available in mid-1993 indicated that the sector employed only just over 2 percent of the labour force in 1986. All sources agree that the growth of the industrial sector had increased throughout the 1980s. The World Bank estimated an average annual growth rate of 3.4 percent between 1980 and 1989, despite negative growth in the drought years of 1987 and 1988 during which exports of hydroelectricity were substantially lowered. By 1990, the growth rate had leveled off, from a surge of nearly 32.0 percent in 1989 to about 12.7 percent in 1992. The virtual end of the command economy fueled the 1989 industrial boom and supported steady growth for at least the medium term. Principal activities in the industrial sector include manufacturing, construction, mining, processing agricultural and forestry goods, and producing hydroelectricity.

3.2. MANUFACTURING

There is a paucity of any real industry in Laos outside of timber harvesting and electricity generation. Nonetheless, manufacturing represents about half of all industrial activity. Other manufacturing activities includes the production of agricultural tools, animal feed, bricks, cigarettes, detergents, handicrafts, insecticides, matches, oxygen, plastics, rubber, footwear, salt, soft drinks and beer, textiles and clothing, and veterinary products. Manufacturing employed only approximately 2 percent of labour force in 1991. A few factories in Vientiane Capital area have been rehabilitated since mid-1980s. As of 1994, the garment industry was booming with investment from China, France, Taiwan, and Thailand. There were more than forty garment factories in Vientiane Capital area.

The manufacturing sub-sector was composed of over 600 factories and plants of which one-third were state-owned in 1991. Most manufacturing is for domestic consumption and is centered in Vientiane Capital area. As of mid-1994, there was little manufacturing in or near Laotian towns. In 1989 and 1990, there was a rapid increase in cottage industries such as cotton spinning and weaving, traditional village crafts, basket-weaving, and the production of alcoholic beverages. As part of the internal business sector, however, cottage industries are not covered by national statistics.

Between 1980s and 1990s, over 80 percent of manufacturing was in the production of clothing, food and beverages, metal products, tobacco products, and wood products. Industrial round wood production increased 71 percent between 1975 to late 1980s to an annual average of 330,000 cubic meters and then declined to 309,400 cubic meters in 1990. Sources differ over the growth trend for lumber production; the UN reported a decrease in production of 61 percent between 1980 and 1988, and the Asian Development Bank showed an increase of nearly 40 an increase of nearly 400 percent in the same period.

3.3. MANUFACTURING AND HANDICRAFT INDUSTRIES

The number of manufacturing and handicraft factories run by small enterprises increased dramatically from 1995 to 2000 compared 10,826 to 21,558. That was an increase of 96%. This causes a rise at 56% in GDP contributed by the overall industrial sectors which came from joint venture at 69.4%, State enterprises at 20.4% and 10.2% from private sectors.

3.4. ENERGY INDUSTRY

Lao energy industry is based upon natural resource. During the last two decades, from 1980 to 2000, with the change of government policy toward foreign investment and businesses, the energy industry has been remarkably increased in hydropower electricity construction. Energy industry has served greatly to the country export, and contributed mainly to the GDP. The hydropower electricity production rose from 33 MW in 1975 to 644 MW in 2000. Electricity of low, medium and high voltages has been expanded to countryside with the total consumption of 35% of electricity production.

3.5. MINING

Assessments of mineral reserves are imprecise, because by 1991 most of the country had not been geologically surveyed in a detailed manner. According to 1991 estimates, deposits of gemstones, gold, gypsum, iron, lead, potash, silver, tin, and zinc have relatively high commercial development potential, but mining activity is on an extremely small scale. In addition, Laos has small deposits of aluminum, antimony, chromium, coal and manganese, as well as potential for oil and natural gas. In 1989 exploration agreements for oil and gas were signed with British, French, and the United States companies.

Mining operations are carried out by state mining enterprises, and supervised by the Department of Geology and Mines and small scale miners. Production of tin, the principal mineral export, decreased 50 percent between 1975 and 1988, to about 240 tons. Gypsum production increased 167 percent between 1980 and 1988 to about 80,000 tons. Salt production increased 233 percent between 1992 and 1988 to eleven tons. Coal production increased more than 600 percent 1982 and 1988 to about 800 tons.

From late 1980s to 1990s, the survey of mineral reserved has been made. By the year 2000, the government has identified 20 different kinds in 50 mining reserves. Over 10 of the mining operations have been tested and utilized such as: Charcoal, iron, ore, emerald, limes, ceramics for cement production, barite stone, zinc, phosphorus, wet coal, salt, construction stone and sapphires. The mining operation has been conducted by local and international investors. 110 activities of survey, exploration and testing were approved in 2000.

The survey has estimated 655 million tons of coals, 1.5 million tons of wet coal, 57.7 million of zinc, 1 million tone of bronze, 0.7 million tons of pyrite, 92,546 million tons of salt (nitrate, galimyra), 20.6 million tons of ceramic, 1,180 million tons of lime for ceramic production, 55 million tons of sand for bricks production, 8 million tons of sand glass, 100 tons of gold, 0.55 million tons of phosphorus, 0.15 million tons of balid, 0.3 million tons of micon, 32.3 million tons of karats of sapphire and other unexplored minerals.

3.6. TECHNOLOGY AND EQUIPMENT

The technological use in industrial production in Lao PDR has not been developed. This is due to the storage in personnel in many areas concerned. However, by 2000, Laos introduced technology in its productivity in order to efficiently and effectively produce its products. This includes timber processing industry, hydropower electricity. Thus, the research in technological and machinery used in productivity has been very little success.

3.7. LABOUR IN INDUSTRY

There was an increase in laborer working for industrial jobs from 56,635 people in 1995 to 83,240 people in 2000, which was growth at 3.8%. 58% of this kind of workers is females working in textile factories. Nearly all these workers are young and low-educated.

3.8. INVESTMENT

By implementing the national policy on the expansion of electricity to all over the country, the government has mainly invested on electricity industry at around 80% to 90% while invested in mineral and manufacturing sector at around 10% to 20%. The number of private sector investment has considerably increased from 268.4 billion kip to 1,019.9 billion kip from 1999 to 2000. However, there was still a little growth investment in industrial sector. Hence, the contribution to economic development has improved gradually.

3.9. FOREIGN INVESTMENT

Foreign investment in the hotel and tourism sector has increased significantly in recent years. Over the period from 1988 there were 34 tourism projects and foreign investment amounted to US\$605 million, representing 8.8 percent of total foreign investment in the Lao PDR. To date, foreign investment accounts for 83 percent of total investment in the Lao PDR.

4. INVESTMENT OPPORTUNITIES

The Lao law on the promotion of foreign investment has been clearly defined its stages on investment. The reduction of duties on machinery equipments and materials to 0%, profit tax definition at 20%, 15% and 10% for certain period, one-stopped service for license approval provide a good opportunity for investors to invest in mining, hydropower, tourism and agro-forest processing.

4.1. TOURISM

International tourism received a boost when the country was opened to international tourists in October 1989. Since then, other measures such as the relaxation of visa requirements for visitors have aided the expansion of the tourism sector. The importance of tourism's potential contribution to social and economic development in Lao PDR was underscored when, 1995, the Lao National Assembly identified the tourism industry as one of the nation's eight priority development areas.

Since 1991, revenue from the tourism industry has increased dramatically, which has become a major export industry of the Lao PDR. Tourism activities earned US\$73.3 million in 1997, was the nation's third largest source of export revenue. The growing importance of tourism is clearly reflected, for instance, in the growth of the hotel and restaurant sub-sector which expanded by 62.8% in 1995, the largest increase by far of any major sector in the Lao economy. The number of accommodation establishments, hotels and guesthouses, has more than tripled between 1992 and 1997, and the number of room has doubled during the same time period.

The number of tourist arrivals, especially among regional tourists, has been increasing dramatically. The average length of stay for international tourists is five days and for regional tourists it is one day. Fifty-five percent of tourism industry revenue during the 1997 was derived from international tourists who accounted for 19.2 percent of total tourist arrivals. The majority of arrivals are tourists in 1997 of 70 percent of international tourists and 78 percent of regional tourists visited Lao PDR for tourism or leisure purposes. The number of tourist arrivals doubled up from 463,200 in 1997 to 894,806 in

2004. That was an increase from US\$73 million to US\$119 million. These tourists were mainly from Asia and Pacific and Europe.

Table 9: Tourist Arrivals to Laos

| Year | No. Tourist Arrivals | Income from Tourism in USD |
|------|----------------------|----------------------------|
| 1997 | 463,200 | 73,276,904 |
| 1998 | 500,200 | 79,960,145 |
| 1999 | 614,278 | 97,265,324 |
| 2000 | 737,208 | 113,898,285 |
| 2001 | 673,823 | 103,786,323 |
| 2002 | 735,662 | 113,409,883 |
| 2003 | 636,361 | 87,302,412 |
| 2004 | 894,806 | 118,947,707 |

4.2. AGRICULTURE

At least 5 million hectares of Laos's total area of 23,680,000 km² are suitable for cultivation; however, just 17 percent of the land area, between 850,000 and 900,000 hectares is cultivated, less than 4 percent of the total area. Rice accounted for about 80 percent of cultivated land during the 1989 to 1990 growing season, including 422,000 hectares of lowland wet rice and 223,000 hectares of upland rice, clearly demonstrating that although there is interplanting of upland crops and fish are found in fields, irrigated rice agriculture remains basically a monoculture system despite government efforts to encourage crop diversification. Cultivated land area had increased by about 6 percent from 1975 to 1977 but in 1987 only provided citizens with less than one-fourth of a hectare, each given a population of approximately 3.72 million in 1986. In addition to land under cultivation, about 800,000 hectares are used for pastureland or contain ponds for raising fish. Pastureland is rotated, and its use is not fixed over a long time period.

In the early 1990s, agriculture remains the foundation of the economy. Although a slight downward trend in the sector's contribution to gross domestic product, GDP was evident throughout the 1980s and early 1990s from about 65 percent of GDP in 1980s to about 61 percent in 1989 and further decreasing to between 53 and 57 percent in 1991.

In June 1988, in line with policies by the New Economic Mechanism, the government passed a resolution to reform the agricultural sector. As announced at the Fourth Party Congress in 1986, the principal goal was to reorient the sector toward a market economy. The abolition of the much hated agricultural tax as well as the socialist restrictions on marketing helped to create necessary incentives for farmers.

The major change was in the pricing policy. The practice of setting low producer prices for a wide range of crops was ended, boosting incomes in rural areas.

Other changes were also implemented. Restrictions on internal trade of agricultural products were removed allowing free market to operate, at least for important crops such as rice. Laws also were enacted to guarantee farmers' rights to private ownership of land,

including the right to use, transfer commercially, and bequeath. Tax exemptions for specified periods also were decreed.

The reforms emphasize the government's belief that further increasing and diversifying agricultural production requires the participation encouragement of the private sector. Food security, as always, remains a key objective, but the focus of the new agricultural policy is on the production of cash crops that can be processed to increase their value and then exported. This means for reaching that goal include the popular 1989 measure of abandoning the poorly developed attempts at establishing the socialist infrastructure of agriculture to a cooperative farming system.

In fishing, for many Laotians, freshwater fish are the principal source of protein; per capita consumption average 5.1 kilograms annually. Fishpond culture had begun in the mid-1960s, and production mainly carp raised in small home lots-grew an average 30 percent annually thereafter, the highest rate in Asia between 1975 and 1985. The Mekong River districts in the south have especially high potential for greater increases in fish production. In the 1982 – 1984 periods, the average annual catch was 20,000 tons, all of which was consumed domestically.

4.3. THE BANKING SYSTEM

In March 1988, Decree 11 on the reform of the banking system was passed, separating commercial bank functions from central bank functions. The Vientiane branch of the old State Bank, the Banque d'Etat de la Republique Democratique Populaire du Laos (RDPL), became the central monetary agency. In June 1990, the Central Banking Law was passed, establishing the Bank of the Lao People's Democratic Republic, or Central Bank to replace the State Bank. Under this law, the Central Bank assumes responsibility for regulation and supervision of commercial and regional banks; maintenance of foreign exchange reserves; issuance and supervision of money for circulation; licensing, supervision, and regulation of financial services; and management of the monetary and credit system. The Central Bank has about ninety regional branches; as of 1991, the government was considering separating these branches into three regional banks, serving the southern, northern, and central regions.

Other branches of the former State Bank were transformed into autonomous commercial banks to promote private investment. These banks are responsible for accepting savings deposits from enterprises, government departments, and individuals, and for granting credit to state entities, joint ventures, and individuals for capital investment and business start-ups or expansion. Commercial banks are restricted from granting credit to economic units experiencing deficits and losses. These banks do not receive subsidies, although they do render 60 percent of their profits to the government.

By 1991 Laos had seven commercial banks, including the Joint Development Bank, a Lao-Thai joint venture, and six wholly state owned banks. Government policy encourages privatization of these six banks. However, in part because of the absence of laws governing banking activities and in part of because of the relatively small size of the economy, foreign bankers do not express much interest in these ventures.

The Foreign Trade Bank, Banque pour le Commerce Exterieur Lao (BCEL), a subsidiary of the Central Bank, is the country's foreign exchange and foreign trade bank. By Decree 48 of July 1989, the Central Bank is assigned sole responsibility for setting and managing the exchange rate. BCEL was granted autonomy in November 1989 and was charged with handling foreign exchange transactions relating to trade; as of 1991, BCEL had arrangements with sixty-four banks internationally. However, a Foreign Exchange Decree was scheduled to go into effect soon after 1991, allowing all commercial banks already authorized to deal in foreign exchange to carry out foreign exchange transactions themselves, thus removing BCEL's monopoly on such activities. Information on the status of this decree was unavailable.

4.4. DOMESTIC FUNDS

Around 90% of GDP has been utilized for development of infrastructure throughout the country. The national budget is deficit. Funding generation mechanism of the financial system has not yet been developed. The National development requires sufficient funds in terms of loans, grants and private investment.

5. FDI POLICY ENVIRONMENT IN LAOS

5.1. FDI INFLOWS

Foreign Investment Law of Lao PDR was promulgated in 1988. This law seeks to encourage foreign investment as a means of facilitating economic development as called for by the New Economic Mechanism. Foreign investment law allows investors to enter into three type of investment arrangement. In early 1989, Decree 27 established the Foreign Investment Management Committee to centralize foreign approval procedures, thus enabling the Foreign Investment Law to be implemented. The clear provision of the law and the reduction of steps of investment assist in attracting new business ventures and build their confidence to invest in Lao PDR.

In 1995, the approval of foreign investment license was the amount of US\$1.218 million and up till then the total amount of foreign investment accounted for US\$7.126 billion, which consists of 618 projects. Of the amount, US\$1 billion is resulted from local investment. Foreign investment came from more than 30 countries such as: United States, Hong Kong, Russia, United Kingdom, Singapore, Japan, Germany, Canada, Italy, New Zealand and others.

Projects approved in 1995 included those engaged in agricultural, industrial and service sectors, of which the biggest contribution of foreign investment comprises of energy sector activity.

Table 10: Foreign Investment by sectors (1996)

| No. | Sectors | Amount in US\$ | Percent |
|-----|-----------------------------------|----------------|---------|
| 1 | Agriculture | 55,700,000 | 0.78 |
| 2 | Textile and Garments | 69,268,000 | 0.97 |
| 3 | Processing Industry & Handicrafts | 176,056,000 | 2.47 |
| 4 | Wood processing | 71,393,000 | 1.00 |
| 5 | Mining | 312,336,000 | 4.38 |
| 6 | Trade | 54,474,000 | 0.76 |
| 7 | Hotel, Tourism | 604,944,000 | 8.49 |
| 8 | Bank and Insurance | 73,800,000 | 1.04 |
| 9 | Consultant Service | 7,232,000 | 0.10 |
| 10 | Other Services | 24,811,000 | 0.35 |

The Government of the Lao PDR (GOL) has approved nearly US\$18 billion worth of foreign investment projects since 1988. Hydropower schemes account for more than 65 percent of that amount, including the \$1.2 billion Nam Theun-2 hydro-electronic dam. The value of approvals for new investment licenses declined by more than 90 percent from 1996 to 1998, while foreign direct investment fell by nearly 75 percent over the same period. Foreign direct investment figures provided by the Bank of Lao PDR are given below.

Table 11: Foreign Investment in Laos in millions of US dollars

| 1998 | 1999 | 2000 | 2001 | 2002-2003 |
|------|------|------|--------|-----------|
| 122 | 86.6 | 21.7 | 1154.3 | 277.7 |

Table 12: Foreign Investment Licenses Granted in Laos in Million of US Dollars

| 1998 | 1999 | 2000 | 2001 | 2002 |
|------|------|------|------|------|
| 68 | 53 | 36 | 68 | 43 |

Foreign Investment licensed in Lao PDR by sector from December 1988 through February 1999 in US dollars (Source: Foreign Investment Management Cabinet)

Table 13: Number of Projects

| Sector | No of Projects | Amount (\$) |
|--------------------|----------------|----------------------|
| Elec. Power | 7 | 4,500,820,000 |
| Telecom, Transport | 16 | 637,655,997 |
| Hotel/Tourism | 34 | 605,288,232 |
| Handicrafts | 126 | 463,875,048 |
| Wood Industry | 37 | 168,022,632 |
| Mining, Oil | 30 | 130,992,764 |
| Garments | 78 | 75,753,130 |
| Banking, Insurance | 11 | 73,800,000 |
| Agribusiness | 76 | 68,679,221 |
| Trading | 106 | 64,766,611 |
| Construction | 37 | 61,733,566 |
| Services | 129 | 58,263,054 |
| Consultancy | 31 | 5,998,540 |
| Total | 718 | 6,915,648,795 |

The table below shows official Government of Laos figures on foreign investment. However, these figures reflect the value of investment licenses granted rather than actual foreign direct investment flows. Accurate data on how many of these licenses have been implemented is difficult to obtain.

Table 14: Foreign Direct Investment in Lao PDR by countries

Rank Country Number of Projects Capital

| No | Country | No of Licenses | Value in US\$ |
|----|---------------|----------------|---------------|
| 1 | Thailand | 248 | 2,926,062,468 |
| 2 | USA | 41 | 1,489,599,019 |
| 3 | South Korea | 29 | 630,440,507 |
| 4 | Malaysia | 19 | 293,329,547 |
| 5 | Taiwan | 34 | 68,195,836 |
| 6 | China | 67 | 62,700,031 |
| 7 | Australia | 44 | 41,841,034 |
| 8 | France | 82 | 36,992,998 |
| 9 | U.K. | 17 | 27,535,200 |
| 10 | Hong Kong | 20 | 26,033,100 |
| 11 | Singapore | 15 | 20,044,384 |
| 12 | Russia | 15 | 18,928,705 |
| 13 | Japan | 26 | 17,466,585 |
| 14 | Indonesia | 1 | 5,000,000 |
| 15 | Vietnam | 14 | 4,641,916 |
| 16 | North Korea | 1 | 3,300,000 |
| 17 | Italy | 5 | 2,709,880 |
| 18 | Germany | 8 | 2,672,900 |
| 19 | Belgium | 5 | 2,628,952 |
| 20 | Macau | 1 | 2,534,856 |
| 21 | Canada | 11 | 2,452,366 |
| 22 | Switzerland | 3 | 1,080,000 |
| 23 | Sweden | 7 | 904,675 |
| 24 | Norway | 3 | 900,000 |
| 25 | Holland | 3 | 670,000 |
| 26 | Finland | 1 | 504,000 |
| 27 | Denmark | 6 | 477,000 |
| 28 | India | 2 | 469,600 |
| 29 | Austria | 3 | 212,000 |
| 30 | Luxembourg | 1 | 200,000 |
| 31 | Ukraine | 1 | 200,000 |
| 32 | Bangladesh | 2 | 150,000 |
| 33 | New Zealand | 2 | 118,500 |
| 34 | International | 1 | 100,000 |
| 35 | Cambodia | 1 | 100,000 |
| 36 | Burma | 1 | 50,000 |

Foreign investment licensed in Lao PDR by country of origin, from December 1988 through February 1999, in US Dollars. (Source: Foreign Investment Management Cabinet)

Since 1988, with the advent of the policy of New Thinking, the nation's economic development has steadily been liberalized and is moving towards a market economy. Due to the natural expansion of the economy, Laos achieved a growth rate of 7.2% in 1997, compared with 6.9%, and 7% in 1995.

5.2. FDI POLICY ENVIRONMENT

Since 1986, the Lao Government has introduced an open-door policy and has taken a number of measures to achieve a market economy by reforming its administrative structure and policy accordingly. The government policy has emphasized both revenue raising and expenditure containing measures. Meanwhile, structural reforms have accentuated, notably in creating an atmosphere for investment, privatization, decentralization, and the initiation of an appropriate regulatory framework to meet the immediate needs of the emerging private sector. Following the open-door policy, in 1988, the Government of Lao PDR adopted a code for foreign direct investment (FDI) in order to generate revenue and job opportunities created in the country.

In early 1989, Decree 27 established the foreign investment Management Committee to centralize foreign investment approval procedures, thus enabling the Foreign Investment Law to be implemented. The Lao Chamber of Commerce was established in 1990 to assist in attracting new business ventures. Private domestic and foreign investments have been encouraged by the gradual improvement of the legal environment, including the passage of laws regarding property rights (1990), contractual obligation (1990), crime (1990), civil procedure (1990), and labour (1991). The 1991 approval of the constitution, which protects the right to private ownership, is also an important factor in encouraging foreign investment. Also, as of late 1993, an arbitration law was being drafted that provided a legal mechanism for the settlement of disputes.

5.3. TAX INCENTIVES

Tax incentives are used to encourage foreign investment. In order to qualify for the reduction, a foreign investment project has to meet three of the following criteria: the project will export more than 70 percent of the goods it produce; will obtain domestically more than 70 percent of the raw materials it uses; will use advanced technology; will aim to overcome unfavorable natural or socioeconomic conditions; will contribute to national economic growth; allows foreign investors to remit profits to the countries of their choice; in addition, it prohibits the nationalization of their capital and property.

6. INDIA – LAOS TRADE RELATIONS

India and Laos has a long history of cooperation, yet the economic cooperation is growing very slowly. The trade and investment data and information is very limited. Below is the available information that can be obtained so far regarding trade and investment cooperation.

India and Laos signed a contract on economy and trade cooperation on November 9, 2000, and the contract was in effect since December 21, 2001. The relationship on trade between India and Laos in the past has shown that some businessmen of India propose sales of some products, namely agricultural machinery, electronic equipment, medicine, computer, office appliances, and others. India also shows interest on purchasing some products from Laos, such as phosphate, precious stones, wood products, (namman yang), and etc. Besides, there are some interests on establishing weaving factory, cement factory, and vegetable oil factory in the Lao P.D.R. The products that Laos currently export to India is very limited, namely some mineral. The total export from Laos in 2002 was 60,219 US dollars while the import from India was 40,219 US dollars, and export value was US \$18,000.

Table 15
Value of Trade between Laos and India

(Unit: USD).

| Fiscal year | Export | Import | Total |
|-------------|---------|---------|---------|
| 1999-2000 | 11,317 | - | 11,317 |
| 2000-2001 | 297,593 | 34,719 | 332,312 |
| 2001-2002 | 19,410 | 42,219 | 61,629 |
| 2002-2003 | 112,626 | 563,542 | 676,168 |
| 2003-2004 | 32,799 | 117,416 | 150,215 |

Source: Department of statistics and planning, Ministry of Commerce

6.1. COOPERATION IN AGRICULTURE AND OTHER RELATED AREAS

In November 2000, India and Laos worked out the work plan in agriculture and related areas in which India would continue to provide for an exchange of scientists and experts, the training for Lao personnel in irrigation development projects, consultancy services in management of large irrigation projects and other join/collaborative projects. Whereas, Laos would be pleased to have Indian expert to study the agriculture extension system in the country and to share the Indian experience with Lao side.

6.2. CREDIT

The Government of India gave credit of US\$2 million to Lao PDR. Juguar Overseas Limited has already supplied agricultural farm machinery and equipment worth US\$0.833 million while Tata International Limited was in the completion stage of setting up of foundry at the cost of US\$1.17 million. In addition to this, the Government of India provided soft loan of US\$5 million for Laos to be utilized for upgrading the irrigation management system.

6.3. COOPERATION IN TRADE AND INVESTMENT

India and Laos signed the Agreement on Trade and Economic Cooperation on 9th November 2000 and has come in force on 21 December 2001. India and Laos agreed to

make concerted efforts to expand and increase the bilateral trade turnover and agreed to explore trade promotion measures such as participation in trade fairs, dissemination of commercial information, exchange of business delegations and setting up of joint ventures.

The India is interested in importing of items such as timber, phosphates, rough gemstones and pulses from Laos, and in exporting items such capital goods, agricultural implements and equipment, telecom equipment, solar energy systems, dairy and food processing equipment and pharmaceuticals to Laos.

6.4. MINING AND INDUSTRY

In mining and industry, India is interested in participating in pre-exploration or mining of materials in Laos, and it s readiness to send an expert team to carry out pre-exploratory studies.

6.5. TRANSPORT AND TOURISM

India offered expertise consultancy in the infrastructure sector and involved of some Indian private companies in road consultancy work in Lao PDR, and that this expertise can be effectively utilized for future projects. Rail India Technical and Economic Service is interested in participating in inland container depot project proposed to be set up in Vientiane as consultant project manager.

6.6. COOPERATION IN EDUCATION AND CULTURE

Cultural Exchange Programme (CEP) for 1999 – 2001, India and Laos agreed upon organizing book and photo exhibitions, visit of cultural troupes, film festivals and providing scholarships for Lao Buddhist monks in India. From 2002 – 2003, India offered at least 70 slots to Lao candidates for training civilians which include 60 short and medium term (under ITEC and Colombo Plan) and 10 long term training courses (under ICCR and UGC). India encouraged Laos to fully avail of the training opportunities in diverse areas.

6.7. SCIENCE AND TECHNOLOGY

It was agreed to explore new possibility of cooperation in science and technology of mutual interest by organizing exchange visits of scientists and join seminars or workshop. India is ready to set up an Information Technology Centre in Vientiane. India offered to send one IT expert to explore feasibility of setting up the IT Centre, for which Laos would provide office space, domestic transport and support staff.

CONCLUSION

The ASEAN Free Trade Area (AFTA) was established in 1993. It now comprises the ten countries of ASEAN: Brunei, Burma, Cambodia, Indonesia, Laos, Malaysia, the Philippines, Singapore, Thailand and Vietnam. AFTA's primary goals are to:

- increase ASEAN's competitive edge as a production base in the world market through the elimination, within ASEAN, of tariffs and non-tariff barriers; and
- attract more foreign direct investment to ASEAN.

The primary mechanism for achieving these goals is the Common Effective Preferential Tariff (CEPT) scheme, which established phased tariff reductions within ASEAN, while leaving members free to set their own tariff levels against non-members.

With ASEAN –India relations have been strengthened after the ASEAN Summit organized in Vientiane, there is a reasonably good potential for trade and investment between Laos and India. In the past, the relationship of trade and investment between Laos and India was growing at a very slow pace, in spite of good long term relation both culturally and politically, between the two countries. There are much potential for the relation of trade and investment if more concerted effort has been put into the trade and investment promotion. With the reform of Lao government policy in market oriented economy policy and a new direction of development targeting on industrialization and modernization as well as integration into the regional and global development, India – Lao trade and economic relations will be growing and has good prospect as trading partners in the future.

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