

CHAPTER III

OUTLINE OF ECONOMIC DEVELOPMENT

3.1 Economic Development in Lao PDR

Since the fourteenth century, Laos has experienced long periods of warfare, which resulted in the waste or expropriation of any surplus that the economy could generate. Colonial rule between the end of the nineteenth century (1898-1945) and 1945, when the country became independent, provided peace and political stability, but Laos saw little economic growth and limited investment in infrastructure and social services. Between 1954 and 1975, the country again suffered from a period of war, which divided the country and produced not only physical destruction but also immense structural distortions to the predominantly agricultural economy. The warfare drove hundreds of thousands of people in rural areas off the land, mainly into Vientiane, whose artificially inflated economy was sustained by military and military-related expenditures.

The creation of Lao PDR in December 1975, replacing the earlier monarchy, represented the establishment of the first unified central government since the country's independence, and presented the opportunity for a cohesive attempt to set in train the long-term development of the country. However, the immediate priority of the new regime was to establish political and administrative control and make emergency arrangements for feeding and resettling the population, rather than attempt to deal with the long-term obstacles to development in the rural region. It was not until 1977 that long-term development could become the central concern of the government. During the first period of the new regime, the politicians together with their citizens considered themselves as the poor or labor class.

To address the problems, the first task of the government was to establish control over the economy. To affect that, planning structure was gradually put in place, while socialist institutions were created. It was during the Interim Three-Year Development Plan (1978-80) and the First Five-Year Plan (1981-1985) that a system of centralized

physical planning was adopted. Its main characteristics were that farm output, material allocation, employment, investment, exports, and imports were determined by the central government, and the principal plan targets were established in physical term independently of the system of incentives provided by prices, wages, and exchange rates.¹

Although some private sector activity was maintained, the economic system was highly regulated. Farm-gate prices and trade in agricultural products were administratively determined. Trade among provinces was restricted, and food coupons for public employees were usable only in state shops. In addition, the industrial sector – producing less than 15 per cent of GDP – was largely composed of state-owned enterprises under the state planning system.

The results were disappointing. Domestic price controls and tight restriction on foreign trade led to the emergence of parallel markets for goods and foreign exchange. Meanwhile, a distorted incentive structure created supply shortages. Moreover, a lax monetary policy, which accommodated borrowing requirements of the state enterprises, fueled rapid inflation.

In sum, the system was developed in three stages with the third stage currently underway.

- 1975-1985, the Lao Government emphasized centralized economic planning policy.
- 1985-1990 marked the change in Lao economic policy. The market mechanism was the principle focus of the economic development of the country.
- 1993-2000, the long-term economic development plan will put into place government policy for preparing the country for the 21st century.²

¹ Seiji Finch Naya and Joseph L.H. Tan, Asian Transitional Economies: Challenges and Prospects for Reform and Transformation (Singapore: Institute of Southeast Asian Studies, 1995), p. 154-155.

² http://www.business-in-asia.com/countries/laos_economic.html#2

The long-term economic development plan clearly identifies three regions to focus development: the north, the centre and the south. In the north, Xiengkhuang and Luangprabang provinces are indicated as investment promotion areas for husbandry and tourism. Vientiane in the central region focuses on tourism and industry, whereas Khammuane focuses on electricity and processing industries. Savannakhet and Champasack in the south are areas focused on trading, agriculture and tourism.

The Lao PDR Government has embarked on a comprehensive program of policy reforms, labeled the "New Economic Mechanism" (NEM), since 1985. The NEM is aimed at transitioning the Lao economy from centrally planned to market-base. Initially the reform process was confined to improving the structure and performance of state-owned enterprise (SOEs) and deregulating agricultural marketing arrangements. Since 1988 the Lao Government has taken serious measures to drastically reduce direct intervention in the economy, including divestment of state enterprises.

Domestically, the NEM has provided the context for the Lao government to orchestrate a smooth but gradual transition from a centrally planned system to an emerging market system. The government has avoided taking draconian measures to reduce the size of the public sector, which would have had extremely adverse effects on those losing their sources of livelihood. Nevertheless, since 1989 the state has sold off a large proportion of its enterprises through various divestment procedures. Even the national telecommunications company is now a joint venture with foreign corporations. Such joint ventures are among the most remarkable results of the opening up of Laos to increased foreign direct investment, aid, and tourism. This reversal of the country's ingrained isolation from the West was one of the main features of the NEM, particularly at the beginning of the 1990s, when the government began to anticipate that the country could no longer depend on the Soviet Union or its former allies in central and Eastern Europe, for large-scale development assistance.³

NEM consisted of a wide array of reforms affecting economic system, including measures aimed to deregulate, stabilize, and improve the performance of the economy. These reforms were necessitated by the fact that the central planning system had created

deficiencies in the functioning of the country's administration and the performance of its economy.⁴

NEM was first initiated on an experimental basis in 1985 with the granting of managerial autonomy to selected state enterprises. After this change of policy course was endorsed by the Lao Revolutionary Party Congress in 1986, the experiment was turned into a comprehensive set of reforms, cutting across the whole spectrum of economic activities. The new system translated, among others, into a complete decentralization of economic decision-making, the granting of financial autonomy to most economic agent, the promoting of private sector participation, and the liberalization of most price (except for public utilities) and the exchange rate. In contrast to other socialist countries' previous attempts at moving toward market systems, Lao PDR did not adopt a phased and gradual approach but boldly decided to achieve this major overhaul in a matter of months.⁵ These bold and sweeping measures demonstrated the determination of the Government to foster a more rapid economic development of the country, by setting the appropriate framework for the efficient allocation of resources.

Despite severe external shocks, this policy has already shown signs of success in revitalizing economic activities. Real growth recovered in 1988 and 1989 to satisfactory rates of 5 and 9 per cent, respectively. This recovery was driven primarily by private sector expenditure, but it was still fragile.

The expansion of production in 1989 owed much to a bumper crop after two years of protracted drought. Transforming this rebound into long-term growth would require, above and beyond the maintenance of supportive incentive framework, a fresh effort at developing the country's human and physical capital. It would also require a continued commitment to macroeconomic stability.

⁴ Seiji Finch Naya and Joseph L.H. Tan, Asian Transitional Economies: Challenges and Prospects for Reform and Transformation (Singapore: Institute of Southeast Asian Studies, 1995) p. 154-165.

⁵ World Bank, Lao People's Democratic Republic: (Asia Region: Report No. 8532-Lao, August 10, 1990), p. 1.

Economic tensions have unfortunately accumulated in 1989 as revealed by the acceleration of inflation from an average 7 per cent in 1987-88 to about 50 per cent in 1989; due to difficulties in tax collection, and the deterioration of the trade balance. These difficulties originated in a sharp decline in public savings and have been aggravated by the lack of coordination between domestic and external policies.

Many of the recent difficulties have their origin in the rapid reform process. They indicated moreover that the reform process must undergo consolidation, chiefly with respect to the role of the public sector in the economy.⁶

The reform program called for an opening up of the economy to foreign investment, and the use of price and other market mechanisms rather than state planning. In these respects, it was clearly related both to restructuring (*perestroika*) then being attempted in the Soviet Union and to the similar "new structure" (*doi moi*) program being formulated in Vietnam around the same time. Like the ruling parties in those countries, the Lao party had recognized that rigid planning would not result in needed improvements in the economic welfare of the people.

The impact of the reforms on the services sector has been more pronounced. During the years 1990, 1991, and 1992, there had been remarkable increases in the number of small private commercial enterprises operating in major cities of Laos. In particular, a number of new enterprises have been established which were capable of supplying vehicles, machinery, computer equipment, spare parts, and consumer goods that previously had to be ordered from Thailand. A number of private enterprises providing agricultural, engineering, legal, financial, and medical services have also been established. A number of hotels have reopened and there has been significant growth in the transport of goods between Thailand and neighboring countries.

Despite these favorable recent economic developments, the agricultural sector continues to dominate the Lao economy and provides employment for about 85 per cent of the labor force. The impact of the reforms has been less visible in the rural areas, but

⁶ Ibid., p. 1.

there are indications of more intensive use of inputs to increase production of cash crops.⁷

The Lao economy has grown by more than 7%, driven by foreign investment in the development of the hydro-electric power industry, fast expanding gold and copper mining activity, and a rapidly growing tourism industry. Since 2001, the Lao economy has grown at an average annual rate of 6.5%. Official development assistance and aid still contributed largely to the national budget, but merchandise trade was increasing as a driver of growth, up from 45.8% of GDP in 2005 to nearly 61% in 2006, according to World Bank statistics. Growing garment, horticultural and timber sectors have improved Laos' economic performance and helped to narrow external debt. The signs of increased economic activity were visibly apparent in Vientiane and urban areas around the country, where formerly pot-holed, dusty streets are now clean, paved and full of traffic. New shops sell imported consumer wares, new motorcycles and cars zoom through once sleepy streets, and the city boasts a bevy of Internet cafes frequented not only by foreign tourists and aid workers but locals as well.

The Lao government has in fits and starts promoted the transition from subsistence agriculture towards a more trade- and investment-driven economy. Although the communist government maintains socialist rhetoric and vestiges of the old central planning regime, for all practical sakes and purposes Laos is now in the main a market economy. That represents a significant turn for Laos, which in recent years has undertaken significant structural reforms in trade, private sector development and public financial management. Economic analysts say the country has taken lessons from China and Vietnam's capitalist transformations, albeit at a slower, more cautious pace.

First launched in 1990, the reform transformation from a centrally planned to market economy has allowed Laos to diversify from its traditional reliance on China and Vietnam for its economic sustenance and assert more economic sovereignty over the country's vast bounty of natural resources.

⁷ Seiji Finch Naya and Joseph L.H. Tan, Asian Transitional Economies: Challenges and Prospects for Reform and Transformation (Singapore: Institute of Southeast Asian Studies, 1995), p. 175-177.

According to the government's poverty reduction plans, Laos, which now has a per capital gross national income (GNI) of about US\$500, should at present economic growth rates graduate by 2020 from so-called Least Developed Country status - reserved for states with a per capita income over a three-year average of less than \$750 - and join the ranks of the world's middle-income nations. GNI per capita is up from \$290 in 1992, when the economy was still largely closed to the outside world.

As late as in 1999, statistics from the Lao state planning committee showed that "remittances from abroad" were the single most important source of income in the Vientiane valley, then representing 28% of all household earnings, compared with 25% from agriculture, 22% from wages and 18% from businesses.⁸

Despite the progress achieved so far, several structural bottlenecks continue to hamper the full development of the country's economic potential.

First, because of the low domestic resource mobilization, the country is still heavily dependent on external assistance. Second, the narrow production and export base – with export earnings depending mainly on electricity, garments, and timber and wood products – make the economy vulnerable to external shocks and limits development prospects. Third, acute absorptive capacity problem delay the buildup of social and physical infrastructure. Forth, the early fruits of economic development have remained concentrated in urban centers and have not reached the rural areas, where poverty is still pervasive.⁹

3.1.1 Economic Development in Savannakhet

Savannakhet is the homeland of the late President Kaisone Phomvihane, the most powerful in Lao People Revolutionary Party during 1955 to 1992 – The province has thus been developed gradually under the guidance of the Party and Government of the

⁸ http://www.atimes.com/atimes/Southeast_Asia/JA10Ae01.html

⁹ Ichiro Otani and Chi Do Pham, The Lao People's Democratic Republic: Systemic Transformation and Adjustment (Washington, D.C: International Monetary Fund, 1996) p. 1- 4.

Lao PDR. Now Savannakhet province as a whole, and in particular, Kaisone Phomvihhan district, attracts a number of investors to the province to do businesses. This gains momentum following the pursuance by the Lao government of the open-up policy for foreign relations and investment in the country.

In addition, Savannakhet province is rife with potential in economy, agriculture and forestry, and transition services in combination with tourism in the province. The province is also blessed with mineral potentials such as gypsum, gold, copper, natural gas, and oil, among others. All these potential are valuable resources of Savannakhet province, which are attractive to investors from many countries as a means to extract, develop and generate enormous revenues for people of all ethnic groups in the region. This will be used to boost the ambitious program of poverty eradication in the country and drag it out of the list of least developed countries by 2020, according to the target set by the Party and Government.

Savannakhet, sandwiched between the more developed Mukdaharn on the Thai side and Quang Tri on the Vietnamese side, at all times is ready to open its arms wide to create opportunities for interested business people to make a feasibility study for investment in development and construction, to create employment and generate income for investors simultaneously with the creation of more jobs for local ethnic people so as to develop the economy to prosperity.¹⁰

Furthermore, Savannakhet houses the national highway Route 9, which is considered as the strategic East-West highway of the region. It stretches to the east from the Lao-Vietnam border through Vietnam to the South China Sea, giving access to China, Hong Kong, Taiwan, Indonesia, the Philippines, Korea, Japan and North and South America. To the west across the new bridge at Savannakhet/Mukdaharn, the highway provides access to Thailand, Myanmar, Malaysia, and Singapore and via the Andaman Sea to India, Africa, the Middle East and Europe. Apart from the transportation assets, the economic infrastructure - such as electricity and water supplies, communications and human resource - is being developed gradually and

¹⁰ Savannakhet: The Charming Golden Land (Investment and Tourism Magazine No. 1, October, 2007), p. 3-4.

effectively in this province. In addition, following Vientiane capital, Savannakhet is also known as the industrial base of Laos, housing 198 factories employing 6,738 workers.¹¹ Finally, it is rich in tourist sites such as temples and religious monuments, ancient Khmer structures and dinosaur fossil, and has ecotourism potential.

There are two international checkpoints in Savannakhet, to Vietnam through Lao Bao-Dansavanh and to Thailand through Mukdaharn-Khaisone Phomvihan. From this advantage point, Savannakhet is a thriving hub of trade and services in the Greater Mekong Sub-region (GMS). The province is located along the East-West Economic Corridor (EWEC) linking Myanmar, Thailand, Lao PDR, and Vietnam via Road No.9. The completion of the new bridge has made Route No. 9 Southeast Asia's strategic highway connecting the East with West and will not only improve transport and communication but also boost trade and expansion of markets in the region.

The road network in Savannakhet province is fairly good, with a total length of 5,000 kilometers, the highest in the Lao PDR. In addition, Route No. 9 is a high standard tarred road suitable for rapid transport of goods. Not only does Route No. 9 ease communication from border to border, but it is also connected with the high standard national highway Route 13, which will facilitate transport of goods from this area to northern and southern provinces. With such a complete network, goods from this area could easily travel to other markets both nationally and internationally with great efficiency and effectiveness. In the future, there is possibility that a new international airport may be constructed in Savannakhet, serving both domestic and international airlines, with the aim of becoming an aviation hub for the region.

The completion and inauguration of the second Lao-Thai Friendship Bridge in 2006 has sparked interest among investors since the bridge is connecting and facilitating the East-West Economic Corridor. Obviously, Savannakhet now sees more and more projects of foreign investment. Since the completion of the bridge, the number of tourists has rapidly increased from around 200,000 people in 2006 to more than 300,000 visitors in just the first eight months of 2007. The bridge serves as a link not only

¹¹ K.A.S. Murshid, The Cross Border Economies of Cambodia, Laos, Thailand and Vietnam (Development Analysis Network), 2005, p. 87.

between the Lao and Thailand but also with other countries in the region, especially Vietnam.¹²

At the hub of this emerging web of roadways lies Laos, one of the poorest countries in the GMS, which hopes to exploit its central location in the sub-region to foster much needed trade and investments. Strongly committed to integration in the regional and global trade system, the Lao government has its eye on turning Laos "from a landlocked to a land-linked country" through the corridors crossing its territory.

One attribute that could turn Savannakhet government's dream into reality is the East West Economic Corridor (EWEC) - the US\$200 million project by the Manila-based Asian Development Bank (ADB). Since its inception in 1992 as part of the Greater Mekong Sub-region, it has in effect helped four countries to synergize their economic development and resources.

The EWEC, one of the five economic Corridors initiated by the ADB in the GMS, is a road link of approximately 1,450 km long, running across four GMS countries. It is the artery between GMS and the economic opening to Ganges River, India, hence, shortening the distance and reducing costs for the development of economic exchanges between the Pacific Ocean and Indian Ocean.¹³

A EWEC is to make Savannakhet province become the dry port for transportation of cargo in the Greater Mekong Sub-region (GMS), which is also the cross road and centre for the transport service. With the liberalization of trader and investment this will be an important advantage creating favorable conditions for the development of foreign economic relations for Savannakhet.

Mr Bouasone Bouphavanh, the Prime Minister of Lao PDR notes that in the region along with the EWEC, the Second international bridge over the Mekong River plays thus an important role in upgrading Laos (a land locked country) to be able to compete for potential for service on transition, transportation, trade and tourism among

¹² Vientiane times, November 26, 2007.

¹³ Ibid..

the GMS countries. This will provide an advantage creating favorable conditions for the development of its country and the ASEAN region, as well.¹⁴

Mr. Vilayvanh Phomkhe, the Governor of Savannakhet province notes that having EWEC will make Laos PDR as well as Savannakhet become a crossroad to the Pacific Ocean for the landlocked countries in the region. Meanwhile, the completion of the 2nd friendship bridge crossing over the Mekong River will be a dry port for the transportation of containers of products.¹⁵ EWEC will not only offer an unprecedented opportunity for countries of the region to promote business investment and to accelerate regional cooperation and raise living standards but also provide business with better access to the raw materials, service market, capital, technology, labor etc to diversify economic activities and exports.

For Savannakhet province, economic reforms in Laos have paved the way for market-determined prices, liberalization of trade, elimination of subsidies, free-market exchange rates, private sector involvement in the production and distribution of goods and services, and liberal policies towards FDI.¹⁶ Savannakhet government plans to develop the province into the supply chain for the East and West and go for eco-tourism, the province now is actively attracting foreign investors who are interested in rubber, peanuts and corn, among other products. Thai agro-industry companies such as Charoen Phokphand and Mitr Phol have already invested in the province.

Savannakhet now has to increase exports, promote tourism and rural development, entice its shifting cultivators into stationary jobs, reform its financial system, encourage more investment from abroad, and introduce extensive administrative and legal reforms, in order to make the economy and the investment climate more transparent. While Savannakhet government seeks to promote economic growth, the government is also seeking to address the problems of uneven development related to the region's poor physical infrastructure; this is because the government lacks

¹⁴ Savannakhet Province, Potentials and Investment Opportunities (Department for Planning and Investment of Savannakhet Province, August, 2007), p. 12-13.

¹⁵ *Ibid.*, p. 15.

¹⁶ Seiji Finch Naya and Joseph L.H. Tan, Asian Transitional Economies: Challenges and Prospects for Reform and Transformation (Singapore: Institute of Southeast Asian Studies, 1995), p. 58.

of capital. Savannakhet also needs to restore the confidence of foreign investors in order to revive and then increase the flow of foreign direct investment, particularly, in those industries that will best facilitate an increase in foreign exchange earnings. With economic recovery gathering pace in Asia, Thailand, Malaysia, and South Korea may well become important sources of finance once again, while China also represents a potential source of large-scale investment, particularly in energy, trade, tourism and other services.

Attracting investments from abroad would be made easier if the government's reform program could be accelerated. Many of the enterprises that remain in the hands of the state have not yet felt the effects of the NEM. And there is persistent weakness in the financial sector, which is burdened with nonperforming loans.

In relation to foreign investment and domestic infrastructure alike, Savannakhet also needs to maintain its focus on developing the skills and talents of its people. This goal represents a major challenge in itself, given the region's remarkable ethnic diversity and the remoteness of many of its rural communities. In an economy that is increasingly oriented to private sector development, the government sector will need to do even more than in the past to enhance the quality of people's lives, to provide greater opportunities for women, to improve productivity and competitiveness, and thus continue to attract foreign investment.

From 2004 to 2007 the total of 20 companies are licensed by the Government to invest USD 445,630,370, including registered capital of USD 153,160,000 in the projects in the agricultural sector of Savannakhet province. Eight companies already signed contracts with the Government, 10 companies directly promote the people to plant trees. At present, there is 206,560 ha concession area, 11,764 ha are cleared, trees are planted on 3,689 ha and people are promoted to grow trees on 653 ha.¹⁷

Mr Somvang Vongvath, Head of the Industry and Commercial Department of Savannakhet provinces said: "The province wants the foreign businessmen to invest in our land, to expand our products and to further develop local labor skills. In the past, timber and raw wood were the main exported goods from the province. To day, this

¹⁷ Ibid., p. 40-42.

activity is strictly prohibited while the processed wood products and furniture are being exported instead. But we are encountering difficulties in regards to upgrading this sector due to the lack of skilled workers, which creates a sensitive dilemma, if we can not maintain the needed level of production; we face a serious risk of trading deficit.”¹⁸

Province's macro-economic development for the past five years under the 5th socio-economic plan has brought increased stability to the region. Furthermore, Savannakhet government confidence that the stability will continue throughout the 6th plan which is being implemented, and that economic growth will average 7.5 - 8%, which will translate into a per capita income of around \$800 by 2020.¹⁹ In 2004-2005 Savannakhet's GDP reach 3,470,720 billion Kip (8%), GDP per capita per year USD 402 with increase rate of 5.51%.

Savannakhet province has similarity to other provinces located along the Mekong River in Lao PDR. Their current economic structure, which is primarily agrarian, rural, and typified by low-level technology, is the product of centuries of isolation and economic domination by its neighboring countries.

During 2006-2007, the agricultural and forestry growth contributed to the GDP of the province at the amount of 2,292 billion Kips equal to 47.89%. The average rate of the agricultural growth stands at 7.31%, so it helps GDP per capital of Savannakhet province to attain USD 587. It is projected that the rice production will reach 594,491 tons, an average 782 kgs per person. By calculations, in 2007 the province will have 200,000 tons of rice in surplus. The province is able to produce 26,200 tons of meat, 9,890 tons of fish and 1,100 tons of eggs. By calculations, all meat, fish and eggs are in surplus.

The existing industries in Savannakhet comprise 4 types of industries as follows: The Large-size industry has as many as 35 manufacturers which are comprised of the food processing industry, handicraft industry, power plant, and mining industry, and employ 5,410 employees. The Medium-size and small-size are comprised of food

¹⁸ Ibid.

¹⁹ Interview with informant number 15, 10 January 2006.

processing industry, handicraft industry and mining industry, and household industries including the butcher shop industry and ice industry, numbering 45,119 and 101 respectively. The number of laborers employed by the medium, small and household industries is 79, 3,352, and 880 respectively. The total number of manufacturers in Savannakhet is 300. And the total employee employed by the mentioned manufacturers is 10,621 people compared with the total workforce in Savannakhet, around 200,000 people.²⁰

Table 3.1 Number of industry and workforce in Savannakhet province, 2005

Type of Industry	Number of Industry	Number of Workforce
Large Industry	35	5,410
Medium Industry	45	979
Small Industry	119	3,352
Household Industry	101	880
Total	300	10,621

Source: Savannakhet Industry and Handicraft Office 2005

Necessity of FDI considered as one of the priority development strategy for Laos government which is now being implementing by Savannakhet province

²⁰ Industrial Estate Authority of Thailand, The Feasibility Study on the Establishment of Savan-Seno Special Economic Zone, Lao PDR. (Panya-Src-CMCL, 2006), p. 4.

To accommodate trade and investment in the province, Savannakhet has arranged 3 important locations such as: Savan-Seno Special Economic Zone (site A and B) located in Kaisone Phomvihan conserves of 305 ha, and site B located in Outhomphone (Seno) with 20 ha. Dansavanh Border Trading Zone is to accommodate trade and investment along the East-West Economic Corridor as Special Economic Zone. Its location is at the Lao-Vietnam Border which has total area of 3,310 ha. Kengkabao industrial Zone is considered as medium, big scale factories which may affected the environment. This industrial zone is about 50 km far from Savannakhet town to the Northwest. The 800 ha area has been conserved. The existing factories running there are Chemical and Bio Fertilizer factory and steel factory.

Apart from these 3 locations mentioned above, Savannakhet has one more New Trade and Investment location which groups of investors from Malaysia, China, Singapore and Taiwan which are now studying and constructing infrastructure in the 200 ha site. This location belong to Kaisone Phomvihan district at kilometer 10 (Route 9) called: Trade and Investment Savan Park. First factory will be constructed in January 2008.²¹

The Savan-Seno Special Economic Zone is also a project of the province, which is a major potential attraction of investment to businessmen from neighboring countries like Thailand, Malaysia, Singapore, and Japan, among others. In particular, the unloading point at Seno is the most important site on the East-West Economic Corridor, which is built under a corporation program between a Japanese company and Laos, in facilitation of goods transportation along the corridor. The Seno point is dubbed by the Japanese as the "dry port" of Laos, which is not connected to the sea, but plays an important role similar to other seaports elsewhere in the world.

Special Economic Zone is one of the first priority programs of the socio-economic plan of the Lao Government. It was established by the Prime Minister Decree No. 148/PM dated September 29th, 2003 in order to develop areas along the East-West Economic Corridor based on economic cooperative projects among countries of Greater

²¹ Savannakhet Province, Potentials and Investment Opportunities (Department for Planning and Investment of Savannakhet Province, August, 2007), p. 12-13.

Mekong Sub-region. Objective of the cooperation are enhancing economic strength, reducing international economic gaps, promoting efficiency in sharing natural resources as well as strengthening bilateral cooperative activities through developing economic zones.

The development concept is to establish a free economic zone supporting the private sector to conduct their business activities in trade, service, manufacturing and tourism bases on the potential and competitive advantage of each site. The final objective of the development of Special Economic Zone is to transform the zone into a trade and service hub of the EWEC.

3.1.1.1 Objective of establishment Special Economic Zone

- To develop the province to be the hub for trade, investment, and services of the region by encouraging investments upon utilization a strategic location;
- To develop province as a foundation for industrialization and modernization of Lao PDR;
- To transfer capital, technology, and know-how;
- To create jobs and generate income for localities;
- To benefit from such physical infrastructures;
- Boosting economic and growth including domestic private sector;
- Promote export.

3.1.1.2 Development strategy of Savannakhet

- Ensure Social and Politic Stability.
- Poverty eradication.

- Develop the province to be the service center of the country and region.
- Develop human resource to serve the program shifting from subsistence agriculture to industrialization.
- Provide accessibility to education, especially for rural people.\
- Improve public health service.
- Promote culture.
- Improve basic infrastructure such as road connect to rural, electricity improvement.
- Financial management, and promote export.
- Attract and promote foreign and domestic investment in order to reduce poverty.²²

3.2 Economic development in Thailand

3.2.1 Review of national development from the first plan to seventh plan (1961-1996)

National development during the First and Second Plan periods emphasized the acceleration of economic growth through the diversification of investment in infrastructure projects, including road, electricity, and water supply networks. Despite achieving an impressive record of annual economic growth, income distribution and quality of life of the people in the rural areas deteriorated. Hence, the Third Plan began to focus more attention on social development, the reduction of the population growth rate, and income distribution, in addition to the traditional focus on economic growth. During the Fourth period, political uncertainty and an energy crisis ensure, bringing

²²2001-2006 Socio-Economic Development Plan, Savannakhet Province

about severe balance of trade and current account deficits. In light of these circumstances, the Fifth and Six Plans emphasize economic stability, economic structural adjustment, as well as poverty eradication. A worldwide economic recovery, however, brought about rapid expansion of the economy, causing it to overheat and exceeding the absorptive capacity of economic fundamentals. The Seven Plan subsequently began the shift to a sustainable development paradigm. This paradigm emphasizes maintaining a sustainable level of economic growth, and stability, improving income distribution, developing human resources, and enhancing the quality of life and the environment.

A review of the national development over the past seven plans period shows that Thailand has achieved an impressive record of economic growth, averaging 7% per annum. The Kingdom's average per capital income at current market price increased from 2,100 Bath in 1961 to 7,700 Bath in 1996, which repositioned Thailand from being a poor county to joining the ranks of developing countries. At the same time, the number of people living in absolute poverty has dropped substantially from 57 % to 11.4 % of the population.

However, the country's impressive rate of economic growth has been based on unbalanced development, evident in a widening income gap and an unequal distribution of development benefits between rural and urban areas as well as among the various social groups. Rapid economic growth has also lowered aspects of the quality of life of Thai people and brought about many other social problems such as drug addiction, and public safety issues. At the same time, natural resource depletion, as a result of commercial exploitation, has led to social conflicts and the serious deterioration of environmental conditions. The foregoing suggests that past development, despite achieving high levels of economic growth, has not been sufficiently balanced. Many social problems still remain and the development is unsustainable.²³

The Thai past in rural communities had very little engagement with the world beyond the confines of the village and its field.

²³ National Economic and Social Development Board, Office of the Prime Minister: The Ninth National Economic and Social Development Plan 2002-2006 (Thailand: Kurusapa Press, Bangkok, 2002), p. 3-4.

The Thai village economy in the past was a subsistence economy. Production for food and for own use persisted and could be reproduced without reliance on the outside world. Bonds within the village were strong. Control of land was mediated by membership of the community. Corporative exchange labor was used in production. Individual families were self-sufficient. Agriculture and artisan work – that is, rice cultivation and weaving – were combined in the same household. There was no class conflict in the village.

This view have been influential not only in academia, but also more widely – and, in many ways, more importantly – in the non-government organization (NGO) community. Even the King of Thailand, in the wake of the economic crisis of 1997, called for Thais to create s ‘self-sufficient economy’ based on integrated agricultural. In the King’s seventieth birthday address in December 1997 he said:

Being a [economic] tiger is not important. What is important is to have enough to eat and to live, and to have an economy which provides enough to eat and live....If we can change back to a self-sufficient economy, not complete, even not as much as half, perhaps just a quarter, we can survive... We need to move backwards in order to move forwards.²⁴

This ‘localism discourse’ refocuses development on the village as a community, not as a mere site for the operation of global economic forces. During the 1997 crisis, ‘communities are the heart and the answer [to the economic malaise]. If they are strong, the country will survive’.²⁵

The economic crisis which took place during the first year of the Eighth Plan’s implementation had a lot of repercussions for Thai people. Hence, there was a need to revise the plan in order to solve the national crisis, with more attention given to economic stabilization, provision of social protection, economic structural adjustment, as well as the improvement of management for national economic and social consolidation.

²⁴ Quoted in Pasuak Phongpaichit and Baker, Christopher, Thailand’s Crisis. Singapore: Institute of Southeast Asian Studies, 2000), p. 193.

²⁵ Jonathan Rigg, Living with Transition In Laos: Market integration in Southeast Asia, (London and New York: Routledge, 2005), p. 48-49.

The global economic crisis has seriously affected macro economic conditions. On going attempts by various governments to solve the problem, both on short and medium term bases, has brought about a gradual recovery of the economy. A certain degree of economic stability has been achieved. By 2000, the economy was growing at a rate of 4.4 per cent as compared with the historic contraction of 10.2 per cent in 1998. But problems still remained in financial and property sectors, and the growing public debt and budget deficits will be a major constraint for future resource allocation. Moreover, similar to Laos, the Thai economy is still dependent on foreign technology, has weak production base, and is unable to absorb rapid changes in external conditions. The economic environment, in general, is not conduct to local innovations or the efficient transfer of technology to enhance the national development.

The economic crisis has generated many negative impacts on the quality of life of Thai people. Poverty and income disparities have worsened. Absolute poverty, which had been continually reduced prior to the crisis, increased from 11.4 per cent of the total population, or 6.8 million people, in 1996 to 15.9 per cent of the total population, or 9.9 million people, in 1999. Income distribution also worsened. The combined income of the bottom 20 per cent of GDP, with the top 20 per cent of households saw their combined income rise from 56.5 per cent to 58.5 per cent of GDP. In addition, the number of unemployed also increased from the period preceding the crisis by almost 1 million people. The rapid deterioration of natural resources and the environment has also given rise to more social conflict.²⁶

The economic management, political, and bureaucratic systems in Thailand are highly centralized and dominated by the public sector. The government sector is weak, inefficient, unable to respond to changes in a flexible and timely manner, and unable to fully support economic development. It impedes development in the business sector. At the same time, local administrative organizations have limited capacities. Decentralization of power to local community organizations and local communities is still at the initial stages and the results are still limited. Hence, the people generally have

²⁶ National Economic and Social Development Board, Office of the Prime Minister, The Ninth National Economic and Social Development Plan 2002-2006 (Thailand: Kurusapa Press, Bangkok, 2002), p 5-6.

not been given sufficient opportunity to participate in the formulation of national economic development directions. The legal framework, rules and regulations are out of date and in need of an overhaul to cope with the changing situation and to support development more efficiently.

Corruption and malpractice in public, political and private sectors are chronic problems that have been eroding national development for a long period of time, while corruption prevention and control mechanisms are only at a nascent stage. The public and political will to solve these problems is still inadequate. This, coupled with importance in Thai society of the patronage system and the respect shown to those with power and money, have contributed to serious corruption problems which erode people's confidence in the management of both the public and the private sector. Corruption increases the cost of national economic development and impedes the creation of good governance in Thai society.

Thai society is moving more and more towards increasing materialism and consumerism, with grater consideration given to individual rather than social benefits. This shift in values is one of the major factors that contributed to the severity of the economic crisis. Many Thai people have not been sufficiently selective and prudent about adopting or adapting to foreign cultures that have been transferred to the country, through various information technologies and media entertainment. Cultural domination by Western and industrial countries, and increasing consumerist behavior among the young generation, has caused rapid change in the Thai way of life. Adoption of superficial and materialistic lifestyles has led to declining morality and other social problems. Hence, there is need for the government to empower all stakeholders in the society to play a grater role in human development, so that the Thai people will have necessary skills, knowledge and readiness to adjust to rapidly changing condition in more appropriate ways.

Thailand's economic capacity and international competitive position have been continuously and rapidly eroding. Due to backwardness in science and technology, production efficiency has been slow to improve. Thailand's economy is highly dependent on foreign markets and imports of foreign raw material, capital, and technology. The majority of the Thai labor forces has received only a lower secondary

education, and has not been continuously retrained to upgrade their knowledge and skills to be consistent with changing production systems.²⁷

Thailand is an open country in terms of trade policy, development cooperation and investment. The government supports free trade and is committed to multilateral liberalization, especially in agriculture. As an APEC member, Thailand is also committed to “open regionalism” as a means of achieving free and open trade and investment by 2020. It also engages in regional trade liberalization and, in addition to the ASEAN Free Trade Area, is now actively seeking to negotiate a network of bilateral preferential trading arrangements. Thailand is also pursuing greater regional trade links within ASEAN.²⁸

Rapid economic growth and industrialization since World War II have changed the structure of the Thai economy in terms of the importance of agriculture in the GDP and the relative wealth and income of the city and village. Up until about 1960, Thai society was primarily based on an agricultural economy, with about 90 per cent of the work force engaged in agriculture and contributing about half of the national income. Rice production dominated, with over 80 per cent of cultivated land used to cultivate rice. Under the military dictatorship of Sarit Thanarat (prime minister from 1958 to 1963) the government set the country on a path of industrialization and economic growth.

Sarit began promoting development (*kanphatthana*) as “both an economic goal to be pursued and an ideology on which the legitimacy of the government was based”. The shift towards a greater development effort in regions. Thailand was largely motivated by concerns of the political leaders that the relative underdevelopment and poverty in rural areas, particularly the Northeast, would become a source of rebellion and a threat to the security of the state. Following the advice of the World Bank, Sarit’s government began investing large amounts in public infrastructure and promoting private sector investment in manufacturing. The extension of economic infrastructure

²⁷ Ibid., p. 9-11.

²⁸ K.A.S. Murshid, The Cross Border Economies of Cambodia, Laos, Thailand and Vietnam (Development Analysis Network, 2005), p. 149.

and the provision of schools, health centers, and administrative structures served to incorporate regional populations into the nation-state and capitalist economy, but also enabled the exploitation by the center of the profits of rural production and “the transfer of wealth from the countryside to the city”.

From 1961 development policy was officially guided by a series of National Economic and Social Development Plans drawn up by the National Economic and Social Development Board in the Prime Minister’s Office. Industrialization was encouraged with import substitution policies during the 1960s, followed by a turn towards promotion of export-oriented manufacturing from the early 1970s. These policies led to a period of rapid economic growth and industrialization from the mid-1980s that continued until the economic downturn and crisis that struck in 1997.

During the 1960s, economic growth, albeit highly inequitable, rapidly changed the structure of Thai society, while political power remained concentrated in the hands of the top echelons of the military and civil bureaucracy, in collusion with small economic elite.

Development policies, however, favored Bangkok at the expense of the rural sector, and large-scale agricultural industry at the expense of small-scale farmers and peasants. While economic and industrial development brought about a declining poverty incidence overall, inequality in income distribution grew. While there was an overall decline in poverty during the period of economic development, by 1988, 21.2 per cent of the population still lived in poverty, and 89 percent of those lived in rural villages and were mainly farmers or farm laborers. By 1990, whereas agriculture’s share of GDP had dropped to about 11 per cent, it still engaged over 60 per cent of the work force. While rice and agricultural production continued to grow in absolute terms, the agricultural sector declined relative to manufacturing, and rural production actually helped finance industrial investment and economic growth in Bangkok. Although agriculture remained the foundation of economic growth until about 1980, the rice premium, a form of taxation, kept the domestic price artificially low and hence “depressed the income of rice farmers, kept the cost of living down for urban dwellers (and thereby the cost of labor)”. Rice was finally freed from government intervention with the lifting of the rice export tax in 1990.

The result has been increasing economic inequalities between urban and rural Thailand. Large-scale commercial rice production for the international market expanded in the Central Plains. There, and in the North, peasant landlessness and tenancy increases. Isan, as the Northeast region is called, has suffered the greatest relative deprivation, remaining the poorest region with the greatest incidences of poverty.

Structural changes in the economy, industrial development has resulted in a growing demand for natural resources. While the economic profits of agricultural expansion and concomitant deforestation mainly went to fund economic growth and industrialization in Bangkok, rural Thailand has been left with the ecological costs of deforestation, soil degradation, and industrial pollution.²⁹

It is in this context of economic development, structural change, and environmental degradation that the recent history of rural resistance and organized opposition needs to be seen. The brief review of the economic and environmental impact of the development era on rural villagers is not meant to imply that village life and livelihood were any easier before that time. Rural society and economy in Thailand have always been based on inequality and exploitation of the labor and agricultural production of poor peasants. The era of economic development and industrialization, however, has brought new forms of inequality and exploitation, and hence new forms of grievances to motivate collective resistance.³⁰

Thailand has the long process of regional economic development, faced many economic development issues and met many challenges. Very soon, Thai Government vision of economic development will become a newly industrialized country and again will face new development issues and challenges.

3.2.2 Economic Development in Mukdaharn

²⁹ Bruce D. Missingham, The Assembly of the Poor in Thailand: From Local Struggle to National Protest Movement (Silkworm Book, 2003) p. 16-18.

³⁰ Ibid., p. 20.

Mukdaharn with the modern technology, knowledge, skilled, well developed market, infrastructure and advantage in term of capital compare to Savannakhet, the province is certainly interested in greater market access for its exports, especially of processed goods. It is keenly interested in developing market clusters where neighboring markets are closely linked to its raw material, technology and investment. It is also aware of the increasing need to be able to shift sunset industries to cheaper or lower (labor) cost centers. Mukdaharn is also positioning itself to emerge as a new regional economic hub, at the center of a dynamic region consisting of Myanmar, Laos and Vietnam.

Mukdaharn population's GDP per capita is 28,944 bath/year, Gross Province Product value 10,313.18 millions Bath (2001). The main income of the province come from service sector which cover 30.26%. While trade cover 17.28%, agriculture 15.38% and other 37.08%. In 2006, the service and tourism sector has growing gradually; this is because of the completion of the Second Mekong Bridge.

In 2002, there were 713,684 visitors came to Mukdaharn, 220, 682 of whom are tourists (30.92%), 493,002 of whom are for travelling (69.08%), 672,553 of whom are Thais (94.24%) and 41,131 are foreigners (5.76%), there are more 40 tourist sites in Mukdaharn.³¹

There are 493 villages (95.54%) can access to electricity in Mukdaharn, Mekong River is a major source of water supply for the province. Thai businessmen are now very interested in logistics investment along the route No. 9 linking the four countries, because land transport will play a more critical role than shipping in the future. Some Thai investors have already invested in logistics development at Mukdaharn.

Mukdaharn government expects that the completion of the infrastructure development projects of countries in the GMS will result in more access to the markets, promote economic activities among countries in the region, particularly transportation of goods, cross border trade and investment.

³¹ Mukdaharn Administration Office.

The EWEC resulted in more investment and commercial service centre of Mukdaharn fastly communication network. This will have a positive impact on growth and revenue flows to the budget. In light of these potentials, the objective is to develop infrastructure with a more advanced transit system to renew the role of Mukdaharn as a transit point in the region. This policy also aims to increase economic, political and cultural cooperation with countries in the region in order to integrate the region into the regional and international economy step by step.

3.2.2.1 Development strategy of Mukdaharn

- Poverty eradication.
- Quality Development of human resource and social.
- Economic structure development for equality and competition.
- Natural resource and environment management.
- Economic Development Corporation with neighboring countries.
- Good governance structural development.
- Promote democracy and community movement.
- Security.

Mukdaharn province along with Nakhonpanom, Sakonnakone and Kalasin provinces agreed to promote strategy of human resource development, border trade, ecology tourism and, industry under the regional strategy called “ Happiness Provinces”.

Mukdaharn consider herself as a gateway to Indochina, Thai government plan to develop the province to become the special economic region for industrial production and marketing base for GMS countries which has population more than 380 million people, thus, Mukdaharn plan to establish distribution center. The province is also one of community allies in Northeast area linking Sakonnakorn, Mukdaharn and Nakornpamom by four lanes road. In order to reduce development gap, Twin cities of Mukdaharn and Savannakhet has been established under two governments.

Furthermore, Mukdaharn is a connection point of communication in the region (North-South Esan) and has a role of an economic and tourism gate way as well as a trade and investment key for the GMS. Mukdaharn government expects that the completion of the infrastructure development projects of GMS countries will result in more access to the markets, increase economic activities among countries in the region, particularly transportation of goods, cross border trade and investment. Currently, Mukdaharn promoting night resting camp areas for Indochina countries and within Thailand in order to generation income to local people.

One of the most important policies of Mukdaharn governments is attracting labour-intensive agro-industries and investment activities. Toward this purpose, the governments are approaching bilateral assistance agencies such as ACMEC.

3.3 Conclusion

Economic growth of Savanakheth and Mukdaharn has increased substantially since the end of Cold War and latter formally opened its border in the late 1980s. The level of economic interdependency between these two provinces was further boosted in 1992 when Lao and Thailand, and other countries of the Greater Mekong Sub-region embarked on a program of economic cooperation (known as the GMS Program) to promote development through closer economic linkages; and in 1997 when Lao PDR became a full member of the Association of Southeast Asian Nations (ASEAN).³²

Savannakheth and Mukdaharn, the sister provinces can be viewed as strategic gateways and thriving hub of trade and services in the Greater Mekong Sub-region, it is also one of the river based cooperation and sub-regional economic cooperation in Southeast Asia. Both provinces are located along the East-West Economic Corridor (EWEC) linking Myanmar, Thailand, Lao PDR, and Vietnam via road No. 9. EWEC is a key connects people and also serves economic interest, by facilitating the flow of goods, capital, and people, especially is will link the two provinces to the increasingly

³² Diokno Maria Serena .I and Nguyen Van Chinh, The Mekong Arrange & Rearranged. Thailand: (Mekong Press, Chiang Mai 2006), p. 63.

important market in this region, particularly it can enlarge the bilateral trade in goods, as well as enhance tourism under ASEAN, GMS and ACMEC.³³

From a good geographical viewpoint and potentials, both provinces have an advantage in terms of access to foreign markets and attracting investment. The completion of the second Lao-Thai Friendship Bridge in 2006 has sparked interest among local and foreign investors since the bridge is connecting and facilitating the East-West Economic Corridor. Apart from the transportation assets, the economic infrastructure – such as electricity and water supplies, communication and human resource is being developed gradually and effectively in these two provinces in order to serve the rapid economic growth in this region.

Regional economic developments of Savannakhet and Mukdaharn have been promoted under Lao and Thai's economic policy and the framework of the government's land-linked development strategy within the context of regional integration and globalization. The general objectives of economic development are to promote economic growth and reduce poverty, and thus entered into several regional trade and cooperation agreement such as ASEAN, Greater Mekong Sub-region and ACMEC.

During 1990-2006, Mukdaharn and Savannakhet governments have implemented many development projects including mega projects such as Special Economic Zone in Savannakhet and Distribution Center in Mukdaharn, those project using huge natural resource and budget in order to improve infrastructure and human resource, the goal is to reduce poverty. Both FDI and domestic investment activities have contribute and increasingly subsequent improvement of living standard of the people, local population can benefit from employment opportunity, offering some benefits to those working in the projects, as well as participating in certain facilities made available by the projects, etc. The serious indictment is that investment generates profits, but these profits largely remain unshared by the people and numbers of people

³³ Murshid K.A.S, The Cross Border Economies of Cambodia, Laos, Thailand and Vietnam. (Development Analysis Network, 2005), p. 39.

living in poverty are still high. However, both Foreign direct investment and domestic investment appear not very successful on reduce poverty.