ABSTRACT

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The propose of this study is to examine the structure of the financial and fiscal systems in Lao P.D.R. to arrive at a better understanding about the execution of monetary and fiscal policy in this country.

The study found that prior to 1975, Lao P.D.R. economy was seriously degenerate as the country was in the civil war period when the Left-wing government had to concentrate on joining force with the people to fight for independence from foreign power while having limited capacity to implement any monetary and fiscal policies to stabilize its economy. After 1975 when the Left-wing government had won the war, the economy of Laos was transformed into a centralized system under the leadership of Lao's People Revolutionary Party. The government then merged all banks operating in the war time period into a mono-bank system. However, the Central Bank did not exercise any monetary policy but functioned mainly to provide lending to the public sector to implement the National Social and Development Plan and give loans to state owned enterprises (SOEs).

For the reasons that the country was newly liberalized and the people were scatteringly settled, the government then adopted a decentralized public finance system in which provincial governments had their own autonomy in revenue collection and administration, and would generally send a share to the central government and keep the rest for local expenditure. This system, however, set a limit for the central government's control over domestic budget spending. Moreover, most government revenue was from SOEs transfer, which did not stimulate those enterprises to attempt for more profits, but instead sought more credit from the Central Bank.

As the result of the above policies, the country experienced so slow growth and development that the government had to made a review and sought alternative solutions. Consequently, the Lao P.D.R. has been transformed into a market oriented system beginning in 1986. Under the new economic mechanisms, fiscal and financial reform was implemented. The bank system was changed into a two-tier system and the number of commercial banks had continued to increase. In 1999, seven state owned commercial banks (SOCBs) were merged into three in order to strengthen the internal financial system. The Central Bank, therefore, has become the key body functioning to ensure economic stability by fully and actively implementing the monetary policy directed to the objectives of economic growth, inflation control, maintaining balance of payment and stabilization of exchange rate, by using major monetary instruments including inter-bank rate, credit ceiling control, issuance of government bonds and BOL bonds. Furthermore, the Central Bank also has to provide loans to the public sector to deal with government budget deficit problem in time of need and for strategic public investment projects. In the fiscal side, the government had reformed its system into a single national budget system by changing the revenue base from SOEs capital transfer to tax base revenue. Meanwhile, annual budget expenditure has to be allocated according to the five year public investment plan for financial control and inspection.

In conclusion, the results of this study have exhibited that economy has been subjected to a series of economic system transformation and reform including its financial and fiscal structure, the monetary and fiscal policy management, under the intention of its governments to turn the country from an underdeveloped one into a developed nation in the near future.