

**The Foreign Direct Investment (FDI) Promotion Policies and
Tourism Development
A case study in Luang Prabang Province Lao People's Democratic
Republic**

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Certification

I, BOUNVILAY Chanphet confirm that this report is my own idea. And has not been submitted in any form for another degree or diploma at any university. All data and information come from the relevant official agencies and other researchers who distribute their research, and are referenced in the bibliography.

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List of Abbreviation

AFTA	= ASEAN Free Trade Area
ASEAN	= Association of Southeast Asian Nations
BOL	= Bank of the Lao
EU	= European Union
FDI	= Foreign Direct Investment
FTA	= Free Trade Area
GMS	= Greater Mekong Sub-Region
GSP	= Generalized System of Preferences
Lao PDR	= Lao People's Democratic Republic
LDC	= Least Developed Country
MNE	= Multinational Enterprises
NEM	= New Economic Mechanism
NGOs	= Non-Governmental Organizations
M&As	= Mergers and Acquisitions
OLI	= ownership, location, internalization
OECD	= Organization for Economic Co-operation and Development
UNESCO	=United Nations Educational, Scientific and Cultural Organization
UNCTAD	=United Nations Conference on Trade and Development
UNWTO	= World Tourism Organization
SOE	= State Owned Enterprise

SMEs	= Small and Medium-sized Enterprises
TNC	= Transnational Corporation
WTO	= World Trade Organization

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Abstracts

Foreign direct Investment (FDI) is the key factor to socio-economic development of the Lao economy from 1986 until now. The government has attracted more foreign investors to invest in many sectors of the economy. This paper will study foreign capital inflows into Lao P.D.R, related to FDI promotion policies and describes investment contributions by sector. The influences of FDI on the tourism development in different provinces were observed from tourism related sectors such as number of tourist arrivals, hotels, and travel agencies. In order to investigate these topics, there are a few important questions that need to find answers particularly on the implemented government policies. What were the government policies on FDI flow into Lao P.D.R, what the relationship between FDI and tourism is, and why FDI in tourism development is successful? Through the analysis of FDI inflow into Lao P.D.R, FDI inflow into the tourism sector, and management policies between central government and local level, the last part of the paper will summarize some recommendations concerning the improvement of FDI in tourism development in the future.

Keywords: Lao P.D.R, foreign direct investment, policy, economic development, tourism.

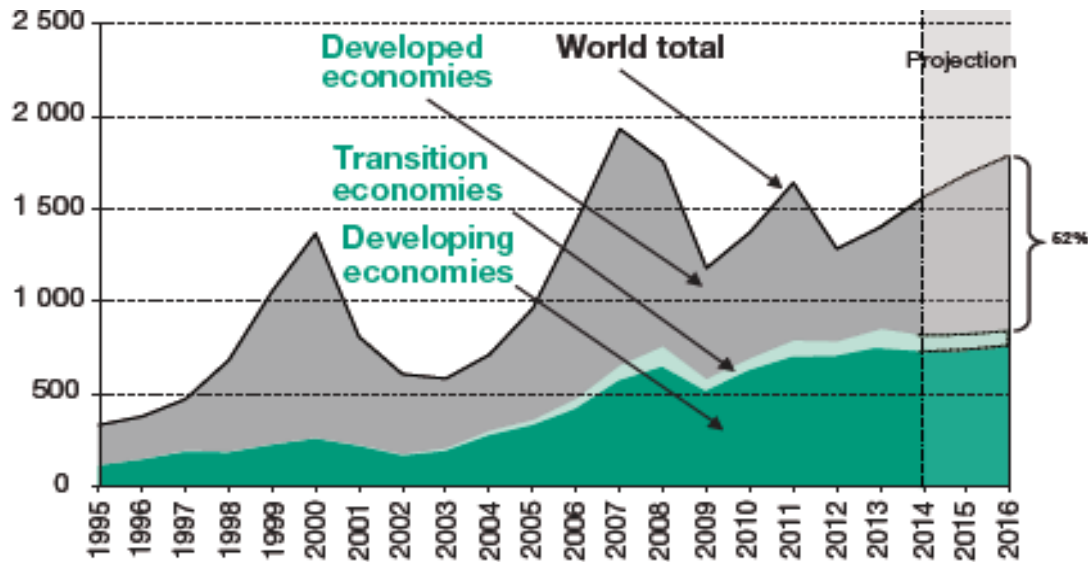
Chapter 1. Introduction

1.1 Overview

Foreign direct investment (FDI) is a tool of foreign companies to get the highest profit for their investment through capital, knowledge, or technology. Companies invest where economic and political conditions allow them to reduce the costs of operation, and increase production and profits. In general, FDI occurs in two forms: Greenfield and mergers and acquisitions (M&A). FDI also concerns the direct control of a facility or equipment, and the infrastructure to build or expand their business operation.

In 2013, FDI flows increased 9 percent from 2012, equal to \$ 1.45 trillion. FDI grew in all developed, transition, and developing economies. According to estimates by the United Nations Conference on Trade and Development (UNCTAD) investment flows in the world may rise to \$1.6 trillion in 2014, \$1.75 trillion in 2015, and \$1.85 trillion in 2016. The increase globally will be driven by economic development in order to recover economically from the financial crisis of 2009. Instability in markets and risks related to policy uncertainty and conflict in the region can affect to FDI. From estimates FDI will grow in developed countries and the distribution of investment globally may lead other countries to develop (UNCTAD, 2014).

Figure1.1. FDI Inflows, global and by group of economics 1995-2013 and projections, 2014-2016 (Bill.Dollars)



Source: UNCTAD, World Investment Report 2014.

According to the ASEAN Investment Report (AIR) the trends and developments in foreign direct investment (FDI) in the Southeast Asia also make significant contributions to the economic integration of ASEAN and the transformation of the region to an investment destination.

ASEAN, investment in 2011 has reached US\$114.1 billion, a figure that rose 24 percent compared to 2010. Likewise, 2010 figures were up 97 percent compared to 2009. Investment grew for two consecutive years despite the global economic depression, demonstrating the resilience of investment in ASEAN. It should also be

recognized that investment growth in ASEAN has gone through significant changes over the past decade, because of the dynamically changing environment of business. These changes, among others, including growth initially seek strong investment. There has been an increase of investment companies and foreign investors in the form of the M&A; the influence of multinational companies strategic actions have increased regional integration through increased activity in regional production networks and regional supply chains. These changes create a new image for regional investment policies and have resulted in development cooperation. ASEAN pursued to further integrate economically through new investment policies. ASEAN urged the continuance of the satisfaction guarantee investment policy as it continued to be relevant and effective in support of the sustainability and growth of investment into ASEAN.

The flow of investment into ASEAN in 2011 rose to \$11.4 billion compared to 2010. FDI flows in the region in 2011 increased 24%, or \$1.14 billion, compared to 2010. These investment flows are influenced by global economic conditions. Moreover, the flow of investment in 2010 was up 97% compared to 2009, which was the first time investment had grown by such a large percentage.

Investment was strong in 2011 and contributed to many factors, including a surge in of M&A, increased investment in ASEAN, and increased investment source markets, such as China. Additionally, the investment during this period was

widespread, and included both the manufacturing and services sectors. To further improve the environment for investment, policy measures at the regional and national level must be improved. The share of FDI in the ASEAN economy exceeded \$1 trillion for the first time in 2011. The growth of the last few years, especially 2010-2011, has contributed to the quick growth of the region, of which investment was more than \$1.1 billion in 2011, compared with 26.6 billion in 2000, and occurred in little more than a decade. This growth has contributed to the rapidly changing landscape of investment in the region. Furthermore, ASEAN's share of global investment flows have increased further. Investment in ASEAN and regional economic development has increased. In 2010-2011, the region received 74% of investors worldwide and 161% of the economic development compared with 27% and 11% respectively in the first decade (2000-2003).

The changing attitudes toward FDI in ASEAN is an important factor in regional development. These changes included pursuing higher levels of investment, sources of new investment, and increased M&A. These new attitudes toward FDI and integration in the region, led to changing investor attitudes as well. These included decisions to invest and MNE's increase in strategic performance through network production in the region, and an increase in regional supply chain. These changes are creating a new FDI landscape with consequences for regional policy (ASEAN Secretariat, 2012)

The tourism industry has now become one of the leading industries in many countries. The tourism sector contributes significantly to foreign exchange, national income and creating employment opportunities. Tourism is related to many economic activities of the country. For instance, in the period 1995 to 2010, international tourist arrivals increased from 541 million to 935 million, increasing by an average of 3.7% per year. Total income from tourism during the same period increased from \$410.7 billion to \$935 billion (UNWTO, 2011)¹, where growth averaged about 5.5% per year. These figures show that the tourism industry has grown internationally and is involved in the export of services worldwide. The rapid growth in this industry has led to the development of tourist destinations, especially in developing countries which have been developing their tourism industries very practically.

According to the UNWTO reported in 2014, the number of international tourists in 2013, grew 5% in, reaching a figure of 1.087 billion visitors worldwide, which increased from 1.035 billion in 2012, which marked for the first time in history this figure reached more than 1 billion. Despite the global economic recession, demand in international tourism reached beyond expectations, and increased by 52 million tourists internationally in 2013.

¹ For more information, please see: www.unwto.org/pub

The EU led growth in tourism, receiving 29 million foreign tourists in 2013, an increase by approximately 563 million people. The rate of growth, 5%, was double the regional average during 2005-2012 of 2.5% per year. Asia and the Pacific recorded growing fastest across all regions according to UNWTO, increasing by 6%, or about 14 million more than in 2012. Africa saw an increase by 5%, which equated to an increase of 3 million visitors, reaching 56 million people. In America, international tourist arrivals increased by 3% to reach 168 million, up by five million people. Middle East (0%) are not finished to growing, even some destinations perform well.

Growth is expected to continue in 2014 at a rate of 4 % to 4.5% worldwide. By region, UNWTO expectations for 2014 are strong in Asia and the Pacific, 5% to 6%, Africa, 4% to 6%, followed by Europe and America both at 3% to 4%. The Middle East 0% to 5% expected to change positively (UNWTO, 2014).

1.2 Tourism in Lao PDR

The Lao People's Democratic Republic (Lao PDR) is located in the centre of the Indochina Peninsula in Southeast Asia, with a population of 6,256,197; and an area of 236,800 square kilometres. Lao P.D.R consists of three ethnic groups. People who live in the mountainous areas are called Lao sung or Hmong. People living in the midlands are called Lao Theung or Khmu and those living in the lowlands are called Lao Loum. Lao P.D.R shares borders with China to the north, Myanmar to the

northwest, Thailand to the west, Cambodia to the south, and Vietnam to the east.

There are two highlands; the Xieng Khouang plateau is in the north and Bolaven plateau is in the south. The geographical conditions are rich with mountains and humid weather conditions. The country has two seasons. The rainy season is from May to November and the dry season is from December to April. The capital of Lao P.D.R is Vientiane. Other major cities include Luang Prabang, Savannakhet and Pakse. The geographical land of the country is divided into 1 capital and 17 provinces. Further the provinces are divided into districts than KhumBan (groups of villages) and then villages.

In the year 1353, King Fa Ngum connected all cities in order to create the Kingdom of Lane Xang. During his period he built many historical sites and temples. After he died the Lane Xang kingdom was not sustained because it was not strong. It was easy for foreigners to attack the country. In 1893 Lao PDR became a French colony. To come out of that regime, local people started fighting under the leadership of the communist party founded in 1930. In 1975, Lao P.D.R won independence together with Vietnam and Cambodia. The Lao People's Democratic Republic was established on 2 December 1975

Since independence, the Lao economy has depended on agriculture products. About 80% of the population works on fields and upland cultivation. In 1986, the Lao

government changed its policy from a centrally-driven, planned economy to a market economy. The main objective of the new policy is to promote economic growth, reduce poverty, and upgrade its current status as a least developed country (LDC) by 2020. (MPI, 2004) Therefore Lao P.D.R's government was under the instruction of the World Bank (WB) and International Monetary Fund (IMF). There are many economic and financial changes needed including policies on tax reforms, financial and trade, investment, tourism, approval of foreign direct investment, and the privatization of state owned companies. Under these new policy changes there was good opportunity for tourism development, such as acceptance of foreign direct investment (FDI) (Phommavong, 2011) and support for the private sector to own and operate business with state enterprises such as hotels and tour companies.

In the year 1991, the National Assembly accepted a new constitution to guarantee a new open policy for trade, investment and tourism sectors. These sectors promote private investments both domestic and foreign. The tourism sector is one of the sectors that is very important for social economic development in the world, especially in developing countries. Tourism can create jobs and income for people in urban and rural areas. It is also related directly and indirectly with other economic sectors. The tourism industry plays an important role in economic development of the country and reduces poverty. The tourism sector in the Lao P.D.R. is the second largest income earner, the first being the mining sector. The tourism sector was up to \$514 million in revenue in 2012, and 3.7 million tourists visited Lao P.D.R in 2013

and the country earned about \$600 million. Lao P.D.R won the world best tourism destination which awarded by European Council on Tourism in 2013.

To enhance, promote and support more facilities on trade, investment and tourism the Lao government has invested and developed transportation and telecommunications to support trade, investment and tourism (MPI, 2004). The beneficiaries are air and land transportation such as three major international airports are Wattay, Luang Prabang and Pakse. Connection with neighbours such as, Bangkok, Hanoi, Khummimg, Phanom Phenh, Singapore, Taipei and Korea is possible from Vientiane. In the future, the Lao government plans to extend these connections and cooperate with other countries including Japan. Lao Airlines is a Lao state owned enterprise (SOE). Other services airline of the country includes Bangkok Airways, Vietnam Airlines, Thai Airways International, and China Eastern Airlines. Lao P.D.R is connected with Thailand in Vientiane by the Lao-Thai Friendship Bridge. The main roads connecting the major urban cities are national Route No. 13 link from north to south of Lao P.D.R, and Route R3 from Borten (China) border via Bokeo Province to Thailand and route 9 from Savannakhet Province to Vietnam. These roads have been significantly upgraded in recent years, but villages in the rural area far from main roads are difficult to accesses during the rainy season.

Lao P.D.R has 22 international checkpoints, and 18 checkpoints can issue visas to tourists on arrival for a 30 day period. Visas also can be obtained at a

consulate or embassy overseas. In the past, a visa extension was available only in Vientiane, but now it is possible in every province. The government has committed to continue to develop the facilities and the services needed to attract more foreign tourists. The results promote and encourage the making of foreign direct investments (FDI) in business services. Foreign Direct Investment (FDI) for the country was mainly in natural resources, energy and service sectors. According to reports from the Ministry of Planning and Investment in 2010, the amount of total investment of FDI was on 1,022 projects and it worth \$ 11.01 billion. The following table shows the investments of each sector. The largest investments came from China, Vietnam and Thailand.

Table 1. 1. Foreign Direct Investment (FDI) into Lao P.D.R

Sector	Investment (billion dollars)*	Percentage
Electricity	3.44	31.24%
Mining Industry	2.88	25.82%
Services sector	1.48	13.44%
Other sectors	3.21	29.15%

Source: MPI, 2011

Note: * Approved data

The Lao government and private sectors have tried to promote the tourism of the nation and create tourism activity. For instance, in the 1999-2000 was the first Lao tourism openness year, called “Visit Lao Year” and the second was in 2011-2012 “Simply Beautiful”. Lao PDR has many tourism sites and has become a popular place

for tourists due to its relaxed style of living.

The Lao's government supports the private sector and international organizations including foreign investors to develop facilities to meet the needs of locals and tourists. In recent years the major attraction for tourists is Luang Prabang province, especially the Buddhist Culture and Colonial architecture. Muang Ngoi district and Vang Vieng city is famous for eco-tourism. Ancient temples are famous in Vientiane capital, wildlife such tigers in the Nam Et-Phou Louey protected area of Huaphanh provinces, trekking and visiting hill tribes in Phongsaly and Luang Namtha, Nang ann's caves and waterfalls near Thakhek Khammounce province and Khone Phapheng water fall at Si Phan Don are also famous tourist attractions. Bolaven Plateau is famous for coffee production and the ancient temple Wat Phu, which has become a world heritage site.

Lao's government has recommended the development of eco-tourism and conservation. These emphasize capacity building management and use resources sustainably, respecting the culture and natural environment in these areas. The government has established projects under cooperation with international partners such as United Nations Educational, Scientific and Cultural Organization (UNESCO). Eco-tourism projects in areas such as Nam Kan and Nam Nga are among these projects (David Harrison & Steven Schipani, 2007). Lao P.D.R's tourism sector grew rapidly in 1990. The tourist arrivals at that time were about 0.8 million. In 2010 this

number increased to 1.876 million tourists (MPI, 2011). The number of tourists increased since the government launch the “Visit Lao P.D.R Year” campaign in 1999-2000 (NATA, 2005). The government plans to develop infrastructure at tourist attractions and support doing business in tourism to increase the appeal to visitors. The government's effort in promotion and advertising has gained international recognition and resulted in many tourists. In addition, the government is improving and developing personnel in the tourism industry, and training entrepreneurs conducting private business. These things may improve the capacity of workers in the tourism industry and quality of services. Lao P.D.R is a destination for tourism and investment from abroad. The main reasons behind this are: the beauty of Lao P.D.R’ natural environment, traditional rich culture and stable political situation. The country has become a linking point of the region, by upgraded roads and bridges across the Mekong River.

1.3 Research Objectives

The aim of this study is to analyse the policy framework which is attracting FDI to promote tourism activities and to support and facilitate economic activity in LuangPrabang province. The results of this research can explain the contribution of foreign direct investment (FDI) to tourism development. Also this study will provide necessary information to policy makers in the Lao P.D.R government and other tourism stakeholders especially in Luang Prabang province. This study will allow governing authorities to have a better understanding about the nature of tourism and

FDI in the region. Therefore they could set a long-term tourism strategy and appropriate planning for development in the future. Additionally, a review of the existing literature of FDI to identify the factors that affect the FDI inflow, legal and regulatory framework, central and local government involvement will be conducted in this study.

1.4 Research Questions

In order to achieve the above objectives this study will answer the following research questions:

1. What are Lao policies for inbound FDI?
 - What is the relationship between FDI and tourism development?
 - How is FDI in tourism successful in terms of tourism development?

1.5 Significance of the Research.

The main aim of the research project is to identify key factors of FDI influence or consequences to develop tourism sectors in Luang Prabang province in Lao P.D.R. This study will encourage policy improvement in the tourism sector and lead to more sustainable tourism. Research results expected from this study are important factors for investors to invest in the tourism sector. The findings will enable stakeholders in the tourism sector understanding, especially those in marketing, and tourism development planning. The increase in foreign direct investment can be used wisely. The research will contribute to stimulate and strengthen investment in the tourism

sector for foreign direct investment. The research could also help other provinces in the country to attract more foreign direct investment in the tourism industry for future planning and develop tourism related development. As such, this research will be an appropriate study especially for foreign investors. This study will contribute both academically and practically to tourism and FDI. Luang Prabang city is the first World Heritage Site in Lao PDR. This work is related to social economic development in the province. The final reason is Luang Prabang city has been a popular tourist destination in Lao PDR.

1.6 Methodology and Data collection

This study was conducted in the Luang Prabang province, Lao PDR, a case study. The reason this province was selected as a sample model for the whole country, was because, in general, the tourism sector plays an important role in the Lao economy and national development. In this study; the author used both quantitative and qualitative research methods. Including government policies regarding business operations. Secondary data and information was used for this study, such as information available on government websites, books, and journals related to the research topic. Most of the secondary data was taken from the Lao Ministries of Information, Culture and Tourism; Planning and Investment; along with the Luang Prabang provincial Department of Information, Culture and Tourism; and Department of Planning and Investment such as:

- Number of visitors, tourist arrivals, hotel, resorts, restaurants, tour

companies in operation,

- Total of FDI in the whole country and Luang Prabang province by sector.

1.7 Scope and Limitations of the study

During the process of data collection there were some limitations. First, data from related government organisations was not available via online means. Second, this study did not include interviews with stakeholders related to the approval of FDI, and foreign investors or managers. Therefore, it was not possible to collect their perspective, problems, and advices. Finally, this study focused on Luang Prabang province as a sample, and was not able to study as a whole of Lao P.D.R.

1.8 The Structure of the Report

This report consists of five chapters. Chapter 1 provides a general overview of global foreign direct investment (FDI) trends. For instance from developed countries to developing countries, and a historical overview of the developments of the opening up of the Lao economy and related policies as they pertain to foreign direct investment and tourism development. Chapter 2 reviews the existing literature and overall patterns of FDI flows in terms of openness and geographical distribution. Chapter 3 focuses on the theoretical background mainly on foreign direct investment flows into Lao P.D.R in general, the structure of Lao economy and also The FDI by sector, policies an investment management between central and local level. The last part there are some constraint for FDI in the current. Chapter 4 offers a discussion on

FDI in the tourism sector as well as tourism policies in Lao P.D.R. The role of FDI in tourism development in Luang Prabang Province. And the Chapter 5 summarizes my findings and some final conclusions concerning the research questions, which hopefully may prove useful for further research.

Chapter 2. Literature review

According to ASEAN Economic Community Blueprint, investment policies in the ASEAN member states have furthered regional economic integration and implementation agreements. One of these policies has been to strengthen the investment environment of the region in 2011-2012, the other has been to create a more attractive investment environment as a means of facilitating ASEAN's continued growth.

Over the last two years regional action plans have lead individual states to improve the investment atmosphere in ASEAN. These measures have begun to lay the groundwork for possible creation of the ASEAN Economic Community (AEC). ASEAN collaboration in terms of trade in goods and services contributed to the increasing attractiveness for investment in the region. Increased investment in ASEAN is the main policy objective in building economic integration in the region. Each ASEAN member country has taken action individually to further improve the investment environment of their communities. Between 2009 and 2012, individual states took steps to open their investment regimes, improve and simplify the process of investment, provide incentives to encourage investment from newly industrialized countries as partners, reduce the tax rate of firms established in the new special economic zones, strengthen the capacity of institutions with broad promotion

authority, and outline of processes to reduce the cost of doing business, including facilitating investment.

These ASEAN regional agreements are economically important to improve the environment for investment in the region. These agreements intend to increase the competitiveness of the region and make it more attractive for investment in general business terms, production, and trade. From the viewpoint of investors, these agreements increase their ability to manage and expand their investments in an increased number of industries, providing a market size considerably larger than before, and facilitating the easy transfer of capital for business production across the region. Through the implementation of these policies, ASEAN has achieved 98.6% of the 88,152 items identified in the policies for tariff exemption. ASEAN Comprehensive Investment Agreement (ACIA) was put in force on 29 March 2012, with ratification by all member states.

ASEAN has methods and procedures to improve the investment system in the region, and also continue to work on investment freely to facilitate and promote entrepreneurship through providing information to increase more transparency. Efforts were initiated in 2012 to improve and shorten the procedure of application for investment approval, and concluded in an improved process for licensing in business in Cambodia-Lao P.D.R-Myanmar-Vietnam (CLMV) as the main key elements of ASEAN Economic Community (ASEAN Secretariat, 2011):

The ASEAN Economic Community (AEC) as the end goal of the full economic integration in the region by year end 2015. The AEC deepens and broadens the economic integration of Member States based on the principles of an open, outward-looking, inclusive and market-driven economy consistent with multilateral rules and adherence to rules-based systems.

The AEC will ensuing key appearances and foundations:

- *A single market and production base, which promotes a free flow of goods, services, investment, skilled labor and a freer flow of capital.*
- *A highly competitive economic region, that supports and facilitates competition policy, consumer protection, intellectual property rights, infrastructure development, bilateral agreements on avoidance of double taxation and e-commerce.*
- *A region of equitable economic development, involving SME development and initiatives for ASEAN integration to narrow the development gap within and outside the region.*
- *A region fully integrated into the global economy, by making ASEAN a more dynamic and stronger segment of global supply chains, and by ensuring that the region remains attractive for foreign investment. It also entails adopting a coherent approach towards external economic relations. Many specific programmes and measures have been and are being implemented.*

Source: ASEAN Secretariat (2011).

2.1. Characterization of Foreign Direct Investment (FDI)

In last three decades, the amount of foreign direct investment increased rapidly, especially in transition economies such as China, Hong Kong, Korea, Taiwan, Thailand, and Vietnam. Those countries were considered attractive foreign direct investment destinations for their source of socio-economic development, which created jobs and income for the country. There are several studies that have proven that the foreign direct investment plays an important role in promoting and supporting trade, investment and tourism of the host country. In addition, FDI promotes exports and foreign exchange, brings tools and technologies, including knowledge transfer skills to the host country.

According to the Dunning paradigm of ownership, location, and internalization (OLI), general factors, which determine FDI inflows, are the characteristics of the host country that provide the investor with the benefit by ownership (1988). Dunning (1988) pointed out that “...*multinational enterprises (MNEs) are companies which undertake productive, i.e. value adding, activities outside the country in which are incorporated. They are, by definition, also companies which are internationally involved. The extent to which they engage in foreign production will depend on their comparative advantage vis-à-vis host country firms, and the comparative endowments of home and foreign countries*”

Currently financial conditions of countries are affected by the balance of payments and the amount of reserves they hold, but they also have a source of savings through the inflow of investment or the export of resources and capital for private investment. Many developing countries, because they are non-oil exporting, are limited in their sources of capital. Now foreign investment or flow of foreign investment is an important financial strategy for development. These requirements are extended by the action plan for resource targets in sectors important for investment and strategy for poverty reduction. The flow of capital between countries, there are three main forms as Stephen C. Smith (2012) clarified as below:

- (1) private foreign direct and portfolio investment, consisting of (a) foreign “direct” investment by large multinational (or transnational) corporations, usually with headquarters in the developed nations, and (b) foreign portfolio investment (e.g., stocks, bonds and notes) in developing countries’ credit and equity markets by private institutions (banks, mutual funds, corporations) and individuals;*
- (2) remittances of earnings by international migrants; and*
- (3) public and private development assistance (foreign aid), from (a) individual national governments and multinational donor agencies and, increasingly, (b) private nongovernmental organizations (NGOs)*

OECD also gives the definition of the foreign direct investment (FDI) as:

FDI is a key element in this rapidly evolving international economic integration, also referred to as globalisation. FDI provides a means for creating direct, stable and long-lasting links between economies. Under the right policy environment, it can serve as an important vehicle for local enterprise development, and it may also help improve the competitive position of both the recipient (“host”) and the investing (“home”) economy. In particular, FDI encourages the transfer of technology and know-how between economies. It also provides an opportunity for the host economy to promote its products more widely in international markets. FDI, in addition to its positive effect on the development of international trade, is an important source of capital for a range of host and home economies (OECD, 2008)

The direct investor's has influence over their investment. They do not need to obtain 100% ownership. These investments can be made practical by the owner of 100% of the capital. The reason for this is that all or part of the investment company formation can be done by borrowing from financial institutions in the host country. Although there is no an agreement on what constitutes a controlling share, economists agree at least 10 percent allows foreign investors to qualify for the policy decision of the administration (Fry, 1993). Some researchers disagree about the 10% figure, as ownership of 10% in some cases may not affect decision management significantly enough.

2.2 The Theory of Foreign Direct Investment.

Researchers have shown that there are many factors that determine the competitiveness of the companies involved in FDI, starting from resources such as natural materials and cheap labor, to more complex resources such as public transport, infrastructure, and efficient market (Majocchi, A. and Strange, R., 2007).

The research by Koojaroenprasit look at impacts of foreign direct investment (FDI) on economic growth in South Korea by using secondary data from 1980-2009. The study attempts to determine the actual impact of FDI on the economy of South Korea by using macro-economic data such as, annual FDI trends, local investments, labor employment, exports, and human resources, which are considered a variable for economic growth. The study found that FDI was a strength and had a positive impact on investment and economic growth in South Korea. Furthermore, the study suggests that human resources, employment and exports have positive effects on economic growth, while local investment in the South Korea had no significant impact on economic growth (Koojaroenprasit, 2012)

Agrawal studies the impact of investment on economic growth in China and India. From 1993-2009. The study built a model of economic growth at basic level. This model includes factors such as GDP, human resources, labor, FDI and overall development. After testing, Agrawal found that a 1% increase in FDI will have increased to 0.07% GDP of China and 0.02% of GDP grew of India. He also found

that the growth of China is affected by FDI growth more than in India. Investors from abroad prefer to invest in China over India because China has a larger market than India, and also easier to access export markets, government policies that are more attractive, developed infrastructure, is more cost effective, and has a more stable macro-economic environment (Agrawal, 2011).

One reason analysis is performed on the direction of the relationship between economic variables, is to identify a cause. This kind of causal analysis in development economics studies variables such as FDI, technology transfer, trade and tourism. Below were previous studies that discuss the relationship between several variables including tourism, FDI, and economic growth with varying results. For example, research done by Borenstztein et al. (1998) employed a set of FDI flow data from industrial countries to 69 developing countries. Results of the study show that FDI allows the transfer of technology and higher economic growth, however, only when there is a low cost of human resources and high productivity (Borensztein, E., Gregorio, J.D & Lee, 1998). In the tourism sector, studied by Contractor and Kundu, it was found that the rate of growth of the economy was effected by business travellers who identify key FDI opportunities for hotels in the international arena (1995). Also Michael's research on the relationship of tourism in Mexico and economic growth for over 30 years, starting 1970 to 1999, found that several factors may increase tourism in Mexico including the presence of large multinational hotel chains. Foreign investors and tourists are encouraged to involve the private sector in

the support of the local economy. (Michael., 1999)

Kulendran and Wilson research on the nature of tourism and trade. They use a Granger model to test the relationship between tourism and trade. They suggested that this subject needs further discussion. Meanwhile, research that links the development of the tourism industry and FDI in general is still limited (Kulendran, N. & Wilson, K., 2000). Tang researched the relationship between the development of the tourism industry and FDI in China using quarterly data (2007). From 1985 to 2003 the study showed that there was a one direction causal relationship from FDI to tourism describing the rapid growth of tourism in last decades.

2.3 Foreign Direct Investment in Tourism

In reality, FDI in tourism is low compared to other industries; however, the amount of real Trans National Cooperate (TNC) in tourism may be unnoticed. The reasons are that many countries lack the data required for investment in tourism, and a part of the activities in the tourist sector will take place through modes of inequality. Some support activities that foreign brand companies provide for smaller private enterprises in Lao P.D.R do not show up in the investment statistics. These support activities consist of a wide variety of services, for instance administration, management, technology and knowledge transfer and access to market. Investment funds from the foreign brand companies can be made with the intention to provide FDI in a small amount or practical support that is not recognized as official FDI. A

joint venture entity can also be formed between two or more parties to conduct business activities together. The exchange between the foreign and the local companies contribute to balancing and sharing costs and managing the enterprise. Forms of non-equity investments include leases, management agreements, franchise agreements and selling agreements.

FDI in service sector of the tourism industry usually manifests itself by merger and acquisitions (M & A) in hotels in developed countries, although investment in Greenfield manifests itself everywhere, especially to develop resorts. Joint ventures with local partners are used in the formation of new attractions and providing services. Through this arrangement, foreign TNC can take advantage of market knowledge and business partner network in the host country (UNCTAD, 2010).

According to the UNCTAD (2010) let us know that an often-used theoretical approach is applied, and said that a foreign firm will invest only in the foreign country (ies) together with three factors, known as the “OLI” (ownership, location, internalization) paradigm.

1. *Ownership*: The company possesses ownership-specific advantages which allow it to compete effectively with local companies
2. *Location*: There are benefits to locating in the host country (such as a large market, cheap labour, a rich cultural heritage or a pleasant climate); and
3. *Internalization*: There are benefits from directly controlling the business

activity in the host country rather than hiring a local firm to provide it.

This framework also emphasizes that the first condition (ownership) and the third condition (benefits of internalization) determine whether or not FDI is an attractive strategy in the first place from the firm's perspective. The second condition (location) has a crucial influence on which countries will be selected by TNCs. And the internalization factor, in particular, occurs much less in tourism than it does in other economic activities, and separation of ownership and control is common. Table 2 applies the OLI approach to the four tourism-related activities in which FDI is most likely to occur (UNCTAD, 2010)

The tourism sector is a strategic priority in the economic development of developing countries. International tourism activities are linked to growing trade and international investment. FDI plays an important role in providing services to the tourism sector in the control and open policy of the host country to adopt investment in related sectors by using FDI as a key element. Because of the growth of the tourism industry, the government must put effort into attracting more foreign direct investment. Although the tourism industry is the largest industry in the world, it still appears smaller compared to other industry sectors worldwide. As opposed to investment in general, investment in the tourism sector is still very low comparatively. FDI in tourism related activities represents only a small portion related to the management of tourism for example hotel and restaurants and rental

cars. FDI has invested in a few activities that are attractive and important for tourism like airlines and reservation systems (Endo, 2006).

FDI in the tourism sector mostly takes place in developed countries. Approximately 85-90 percent of hotels are TNC in developing countries and recent trends in tourism-related FDI in developing countries show that it is increasing. This growth can be expected to continue over the next five years, according to the survey of UNCTAD that shows that almost all FDI in tourism appears like a small amount for the economic development in a developed country (UNCTAD, 2007).

Tourism industries are one of the economic activities that have grown fast in the world in the last four decade. Tourism industry acts as an important part in economy, conservation and social-cultural development (Hall, C. M., & Jenkins, J. M. , 1995). According to Richter's studies, tourism is "a highly political phenomenon" in Asia and the Pacific region. The result of studies recommend that the government has a role to control internal tourism development (Richter, 1989). The study by Peck and Lepie found that tourism is almost always the product of political and economic aspects (Peck, J., & Lepie, A., 1989).

In reality, a policy analysis of the tourism industry as a way to enhance the effectiveness of its industry. The purpose is to determine the role and policy of the government to attract FDI in tourism and eventually we can know that the role of FDI

in the tourism industry. The study found that large investments are focused on the tourism industry of China. To develop tourism industry and business-related activities, the government's policy is to not levy tax on investments in hotels for foreign investors in 1980s. Previously, this field of services was operated by government (Zhang, H., Chong, K. & Ap, J, 1999)

The researchers made a review of the tourism industry in Vietnam during the last century and the contribution of FDI to develop tourism. Because of the change in the nature of tourism and domestic policies of the government, the trends suggest a slowdown in the growth rate. The decrease in investment is a result of internal and external factors including the Asia financial crisis in the 1990s. In the future governments should consider such obstacles to achieve the objectives set in their policy. The findings suggest challenges arising in future are new destinations in emerging economies that seek to develop tourism and some limited amount of FDI. (Muhammad, A & Joan, C, 2001).

The case study analyzed the determinants of inflow of tourism in Lao P.D.R. The tourism industry in Lao P.D.R has increased impressively since 1990, becoming a major contributor to income and employment. Furthermore, tourism contributes directly to reducing poverty by diversifying employment opportunities and income increased in urban and rural areas. However, international tourism is important to the economy of Lao P.D.R (Latsany.Ph and Kim.D, 2007)

Table 2. 1. The mode of FDI in tourism

Industry/ activity	Ownership advantages	Locational advantages	Internalization factors: (+) encourages FDI; (-) encourages other modes
Hotels	<ul style="list-style-type: none"> • Experience in home countries in supplying upmarket services • Experience in training key personnel • Quality control systems (e.g. management, procurement) • Referral system (GDS) • Economies of geographical specialization, access to inputs 	<ul style="list-style-type: none"> • Location-bound when selling a foreign service • Exports through tourists/ business people visiting home or host country 	<p>When selling a foreign service, Exports through tourists/ business people visit home or host country</p> <ul style="list-style-type: none"> • Investment in hotels is capital-intensive (+) • Quality control can be ensured through non- equity forms (-) • Governments prefer non-equity forms (-) • Referral systems are centrally coordinated without equity control (-) • Growing brand recognition for new TNCs from the South (+) • Lack of managerial expertise in host country (-)
Restaurants and car rentals	<ul style="list-style-type: none"> • Brand name and image • Reputation and experience • Referral system (GDS) • Economies of scale and scope • Tie-up deals with airlines and hotel 	<ul style="list-style-type: none"> • Location-bound • Foreign earnings through tourists and business people visiting exporting countries 	<ul style="list-style-type: none"> • Franchising can protect quality (-)
Tour operators/	<ul style="list-style-type: none"> • Reputation of providing satisfactory 	<ul style="list-style-type: none"> • Need for local tour agents and support facilities 	<ul style="list-style-type: none"> • Coordination of itineraries, packaging of services, need for

travel agents	<ul style="list-style-type: none"> experience Economies of scope (travel portfolio offered) Bargaining power Quality of deals made with airlines, hotels, cruise companies and other associated services 	<ul style="list-style-type: none"> Customers initially originate from home country? Costs of supplying local facilities usually lower Fiscal incentives and infrastructure facilities 	<ul style="list-style-type: none"> quality control of ancillary services for tourists (-) Economies of transaction costs from vertical integration (+) Growth in e-commerce and increasing role of local tour operators (-)
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Source: UNCTAD (2007a), expanding on Dunning J. (1989)

However, tourism industry activities require financing, infrastructure, knowledge, access to marketing and distribution in the global chain. Therefore, the provision of financial resources is the key to achieving development in the tourism industry and further economic growth. That investment will play a key role in the development of the tourism industry, particularly among developing countries that need funding to improve infrastructure such as the international airport, highways, hotels and modern technology which are key for the development of tourism. Therefore, governments in many countries, especially in developing countries, make attracting more FDI their policy priority in order to foster growth of tourism and economic growth for the future.

On the other hand, the tourism usually needs to provide goods and services such as housing, food, anything that facilitates transportation and entertainment in the

host country. In many developing countries, to accommodate the increased demand, the current level of production needs to increase correspondingly. In addition, the shortage of places for accommodation and infrastructure in the country need financing as well. FDI is considered a channel for support, knowledge, and technology that can lead to the growth of the overall economy. The government wants to attract more investment to expand domestic production. However, recognizing the existence of investment in tourism can have consequences for the development of marketing tourism by adopting different policy decisions.

Chapter 3. The foreign direct investment (FDI) inflow to Lao P.D.R

3.1 The Structure of Lao P.D.R's Economy

Since Lao P.D.R government opened policies known as the New Economic Mechanism (NEM) in 1986, the Lao P.D.R economy has been in transition from a centrally planned economy to a market based economy. The Lao economy was affected by the Asian financial crisis in 1997. Lao economic development in the past shows that it achieved a reasonably high rate of economic growth, with low inflation. The economic growth rate was around 6.53% from 2001-2010. Inflation and exchange rate average was maintained in the single digits during 2001-2010. The main methods of furthering economic growth during this period was the flow of funds from overseas, such as foreign direct investment (FDI) in the mining and hydro powers sector and export mining production (Kyophilavong, P & Toyoda,T, 2008). Although the economy's ability to keep growing at high rates, low inflation, and maintain exchange rate stability, it also has serious problems with macroeconomics. First, Lao P.D.R faces deficits in international trade and government spending for public services. During 2001-2010 the average of budget deficit equalled 4.4% of GDP. The average ratio of the current account deficit to GDP was 9.24% during the same period (IMF, 2011). These deficits were funded mainly by aid programs through official development assistance (ODA), foreign direct investment (FDI), and remittances. Budget problems were worse in the country. If the deficit budget continues to grow, it may cause inflation and devaluation of national currency, and

can lead to instability of the economy (Kyophilavong, 2012). According to the IMF in 2010 Lao P.D.R also faced the burden of external debt. The accumulated external debt was more than 50% of GDP in 2010 (IMF, 2011). If the economy is still relying on foreign aid, especially to meet debt requirements, it is likely to cause a debt crisis and also may lead to instable macroeconomic conditions of the nation.

Lao's faces a trade deficit in goods imported from abroad, such as basic consumer goods, investment goods and fuel. In the period 2001-2010, the three core imports were machinery and electrical equipment, oil and minerals, and transportation tools. In the same period, the country's main export products were, mining, electricity, and agricultural products. ASEAN countries were the main trading partner of Lao P.D.R, worth more than 50% of exports and 70% of imports (IMF, 2011) In ASEAN, Thailand accounted for the highest proportion of total exports and imports.

Lao P.D.R joined the Association of Southeast Asian Nations (ASEAN) and applied to join the WTO in 1997. The Lao government has improved legislation, regulations and policies related to attracting foreign direct investment. Lao P.D.R, to further integrate into the regional and world economy, has reformed investment, trade and tourism policies regarding foreign direct investment (Sisombat, 2008). Now FDI has become a source of growth for the economic and socio-economic development of Lao P.D.R. FDI in Lao P.D.R in recent years mainly occurs in the natural resources,

energy, electricity and mining, services and construction, and agricultural sectors. However, the continued growth and development of the mining industry in Lao P.D.R may quickly affect the growth of economy.

3.2 FDI Influence to National Economic Growth

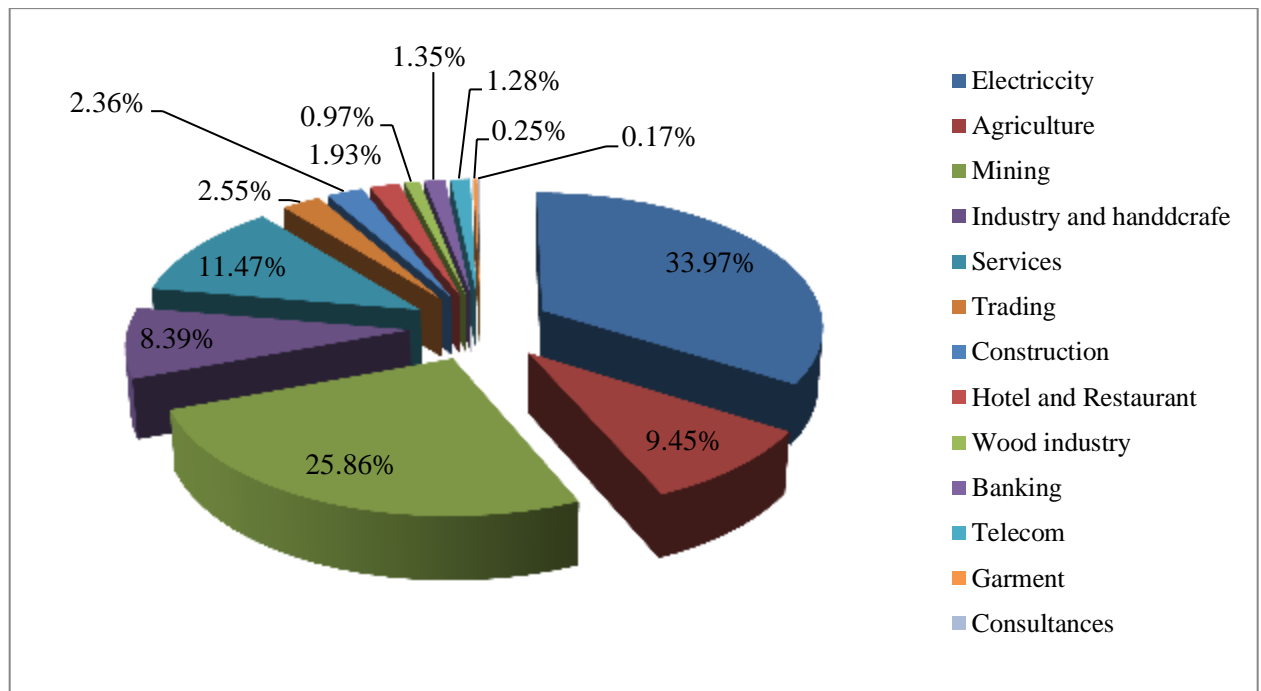
In the early period the Lao government acted on a Soviet model regarding development economics. All investments belonged to state own enterprise (SOE). The investments were in agriculture, handicraft and re-habitation from the war. Foreign investors were not permitted to take part of any economic activities. Throughout that period, Lao P.D.R' economy hurt from little development and a small growth rate. Nevertheless, the government of Lao P.D.R has opened the economy to foreign investment since the mid-1980s. Therefore, the investment policy scheme has been transformed to the private sector and promotes the expansion of investment and competition. The main key component used in economic reforms is the encouragement of FDI. Since 2009, the Lao government has enacted policies on the way to promote FDI. In early 2010s, the economic policies were categorised in the new regulations to set up Special Economic Zones (SEZs), which meant the government gave a huge area to the private sector for a long term concession of 99 years (National Assembly, 2009). In 2014, there were more than 10 SEZs, most of them were Chinese investors in businesses such as Casinos, to attract more tourists, and some of them were in industries to promote manufacturing. These zones are free to import and to operate their business and have the right to foreign exchange. Lao

government had supportive policies to increase FDI inflow in the early 2000s and it developed more of these policies in the early 2010s.

3.4 Foreign Direct Investment Distribution by sectors

According to the Ministry of Planning and Investment (2014), during 2001-2010 the investment in Lao P.D.R was focused on hydropower which covers 33.97 %, Mining 25.86%, agriculture 9.45%, industry and handicrafts 8.39%, services sector 11.47%, trading 2.55%, construction 2.36%, Hotels and restaurants 1.93%, wood industry 0.97%, Banking 1.35%, telecommunications 1.28%, garment 0.25 % and consultancies 0.17%. Although investment in the mining sector represented 25.86% of the total investment in Lao P.D.R, it appears that the actual investments in mining had grown rapidly since the early 2000s, Chinese investors were the largest investor in the mining sector in Lao P.D.R. Chinese investment in the mining industry in Lao P.D.R has grown rapidly, especially over the past year. The present data of investment for period 2001-2010. Overall, the majority of investments were in energy, hydropower, handicrafts, wood industry, telecommunications and mining sector. This figure shows the annual investment by sector during 2001-2010.

Figure 3. 1. FDI by sector



Source; Ministry of Planning and Investment, 2014

The investment in Lao P.D.R for the fiscal year 10/2013 to 09/2014 totalled, from both domestic and foreign investors, about 1,150 projects worth total \$3,383,248,937. This figure includes approved projects from 3 government agencies as following: from Ministry of Planning and Investment can attract domestic and foreign investors. 29 of the projects (covering 4 sectors: mining, electricity, agriculture and services related to the concession activities) are valued at \$953,322,140. From industry and commerce there were 1,088 projects worth \$2,080,570,547. From special economic zones there were 33 projects worth \$349,356,250 (MPI, 2014).

China investment in Lao P.D.R became more important since the 2000s after China gave official development assistance (ODA) to the Lao government to recover from the impact of the Asian financial crisis. The Chinese government encouraged private investors to invest in Lao P.D.R during the 2000s. Investment from China in agriculture still remains small, while Chinese investment is mainly in the mining and hydro power sectors. For instance, the year 2013 saw China become the largest investor in Lao P.D.R. The total investment from China has reached approximately \$5 billion, making it the largest investor in the country, according to statistics. China is followed by Vietnam and Thailand. The value of investment from Vietnam is \$4.8 billion and Thailand, \$4.3 billion, according to the Ministry of Planning and Investment. Trade between Lao P.D.R and China reached \$2.03 billion in 2013, up nearly 29.6% in 2012. That same year, China's export products worth more than \$1,227 billion, an increase of 46.41% from the previous year. China also imports products from Lao P.D.R worth about \$800 million, representing an increase of 10.29% from the previous year. In 2010, the volume of trade between the two countries reached a \$1.04 billion increase, or 46% compared to 2009. In the year 2011 it had climbed to 22.72% to value \$1.28 billion. By 2012 it increased 32.8% up to \$1,728 billion (MPI, 2014).

3.3 Lao P.D.R Foreign Direct Investment Inflow

Foreign Direct investment is one of the most important contributing factors to the implementation of the seventh national socio-economic development plan (2011-2015). The plan set a target GDP, which would represent an increase by an average of 8% per year, which will be driven by investment from the private sector, both domestic and foreign. This will at least average \$1,700 million per year, for the period 2014-2015 to reach \$2.1 billion, or 83% of total investment.

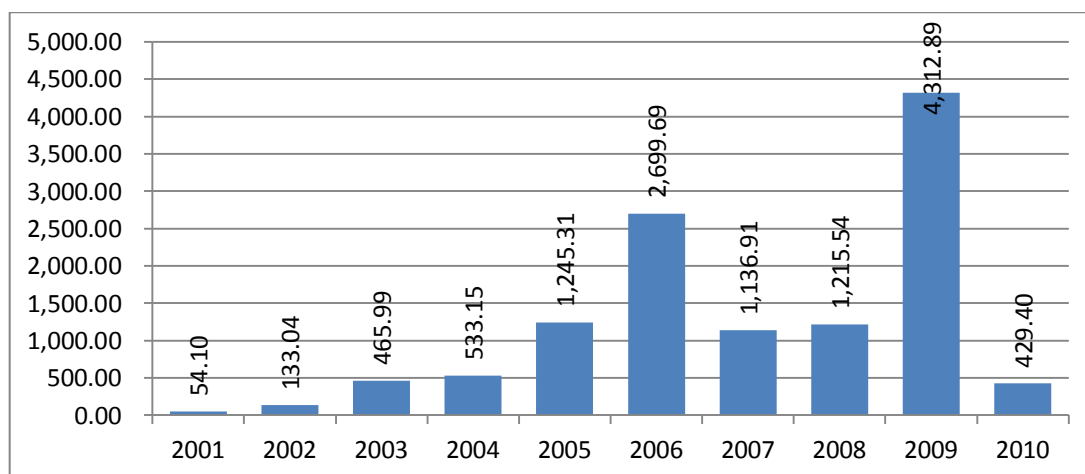
The FDI inflow into Lao P.D.R from early 2000s saw continuous growth, according to information about investment from Ministry of Planning and Investment (MPI) from 2000 to 2010. According to data from MPI (2014), the flow of investment to Lao P.D.R was about \$54 million in 2001. The FDI in Lao P.D.R from 2000-2010 increased in the early 2000 continuously. By 2006, investment in Lao P.D.R totaled \$2,699 billion. The actual investment amount increased from the year 2000-2006 when Lao P.D.R' government amended the investment law in the 2004. The increased value of investment in Lao P.D.R is associated with the growing global economy and increased FDI worldwide. The Asian financial crisis has made a direct impact on investment in Asian countries including Lao P.D.R.

In late 2009, the government had allowed foreign investment in Lao P.D.R worth around \$4,312 billion (MPI, 2014). The investment attraction efforts were focused in sectors such as hydro power, mining, forestry, telecommunications, hotels, industrial timber, tourism, oil and textiles industrial. The early investments prior to 2001 were mostly through joint ventures, as this form of investment is recommended for foreign investment in Lao P.D.R. In mid of 2001, most FDI enterprises were a 100% own.

During 2001-2010, the FDI inflow increased with the total amount of \$12.23 billion, which started from only \$54 million in 2001. This significant increasing was due to the economic situation in the region improved and also Lao P.D.R made

additional efforts which were helpful to investors and made investing easier than before. An example of these efforts include the amendment of the process for considering the approval of documentation. In addition, duty on imports were at 0% for investment related items such as machinery, and the period of investment was extended for up to 99 years (National Assembly, 2009). Before 2004, the period of investment was only allowed for 75 years. During 2001-2010 there were many investors interested and invested in Lao P.D.R. This can be seen in the country's FDI attraction over the past decade. Moreover, Lao cooperation with ASEAN countries and participation in multilateral trade has also contributed to increased investment. Investment actually increased by approximately 20% per year during the period from 2004-2005, the investment totaled approximately \$533.15 million, while investment approvals rose to \$1,245 billion during the same period.

Figure 3. 2. FDI Inflow from 2001 – 2010 (Mill.USD)



Source: Ministry of Planning and Investment, 2014

Investment among ASEAN countries in Lao P.D.R increased significantly during 2000 to 2006. Investors from ASEAN have become the biggest investors in Lao P.D.R, mainly due to Lao P.D.R becoming a place favorable to investment and its shared link to Asian culture. European investment in Lao P.D.R showed a downward trend over the years, replaced by the new industrial economies such as China, Thailand, Vietnam, South Korea, and Malaysia. The economic growth in ASEAN and China have made new investments in Lao P.D.R feasible, and became significant during the period 2001-2010. These trends show the importance of the integration of the Lao economy into the Southeast Asian and global economies. Thailand was a major investor in Lao P.D.R in the early 2000s. Thailand became the largest investor because Lao P.D.R and Thailand share a border and have a similar culture and language. France is one of the largest EU investors in Lao P.D.R because Lao P.D.R was once a French colony. Lao P.D.R has become an attractive destination for investment for EU companies because Lao P.D.R has special permission from the Generalized System of Preferences (GSP) for export to Europe.

3.5 The Investment Management between Local and Central Government

The new investment promotion law was amended in 2009. This law gave more power to local authorities, for example the provincial level can approve investments in sectors not otherwise identified by the central government. The Central government issues and manages activities related to national strategy and sectors that use high technology, for instance finance, insurance, telecom, transportation,

aviation, energy, minerals, water, fuel, gas. In these instances the central government provides initial approvals and the local authority then manages any necessary administration.

Lao P.D.R government has promoted FDI and tried to make a more attractive investment climate through amending regulations related to FDI. The first FDI Law in 1988 was revised three times. The first revision was in 1994, the second in 2004, and the current using is in 2009. These revisions combined two laws, foreign direct investment law and domestic law. The aim was to encourage investment and make it easier and more effective to do business, whether as a domestic or foreign investor. These revisions included: shorter process to take establish a new business; no limit on investment promotion activities; promoting investment in education and health sector as a priority; foreign investors can access local financial sources; foreign investment companies can own land for the construction of housing; foreigners can invest in the real estate industry; also promoting the development of the SEZ and industry park (National Assembly, 2009)

3.6 Constraints for FDI

Lao P.D.R has promoted FDI since the New Economic Mechanism (NEM) was established in the early 1990s, along with improving the legal system to meet the needs of development. Even though the government has taken appropriate steps to make it easier for foreign investors to run a business in Lao P.D.R, the regulations at

present lack consistent performance, and lack transparency in the practice. These cause an increasing cost of doing business.

Some of the obstacles to legal investment include issues with the enforcement of laws and regulations, specifically: Lao government faces challenges in environmental investment since legislation and regulations are not clear; low infrastructure and services in finance remain limited; the promotion Law is only basic; the legal system lacks consistent rules and practices; and FDI data is not clear or is incorrect. Regarding the FDI data in particular, the figures show only approval not actual investment, and the real investment is hard to evaluate. The real number of foreign investment is perhaps higher than official estimates.

Other problems include government issues combating corruption, which has not been entirely effective. Office of the anti-corruption government organization is responsible for fighting corruption. There are several kinds of corruption known to occur in Lao P.D.R, including bribing officials to accelerate FDI applications, or to issue a license for businesses or import goods.

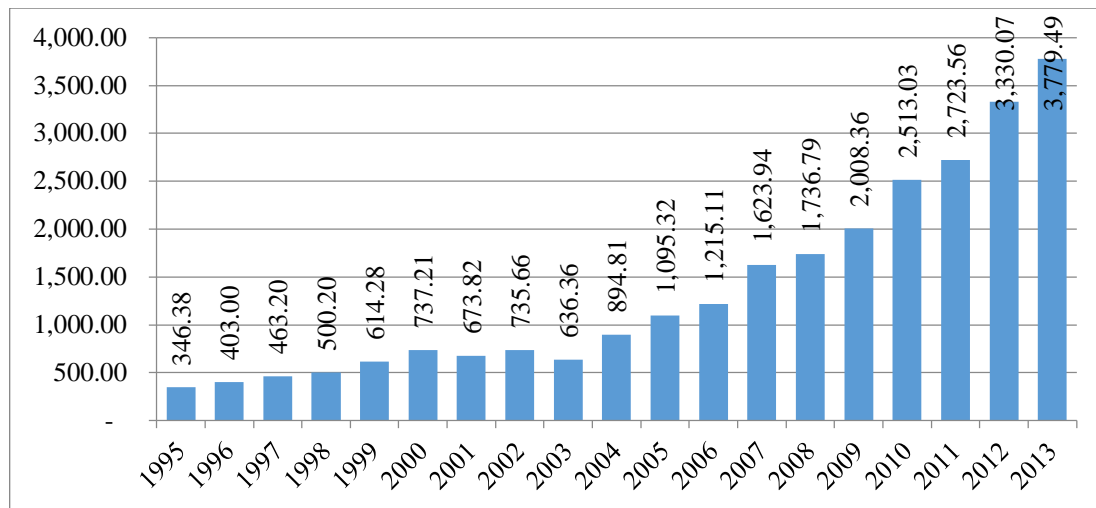
Chapter 4. The foreign direct investment (FDI) flow into Tourism sector

4.1 Lao P.D.R National Tourism Policies

After the Lao government established new policies in 1986, they established guidelines that changed and expanded external cooperation with foreign countries. At this time, the tourism sector did not play a significant role in the national socio-economic development of the nation. The government identified and declared in 1990, as a part of the action plan for national development, that they would promote cultural, natural and historical tourism. The National Development Project (NDP) has linked the north and south by roads. Over the last decade, the government has tried to build and expand international checkpoints into the country to further integration with countries in the region and the world. For instance, the government has expanded the airport to meet the growth of tourism. Now Lao P.D.R has international airports in Vientiane, Luang Prabang, Savannakhet and Pakse. The governments has also exempt ASEAN citizens from requiring visas, in addition to citizens of Japan, Russia, South Korea, and Mongolia (LNTA, 2010). In addition, the NDP has served tourism through the construction of the main national route, mentioned above, linking the Greater Mekong Sub-region, the construction of a bridge over the Mekong River, the improvement and building of airports, construction schemes for electricity, water, phone and the other utilities linked tourist attraction.

As the result of implementation of this policy the development and promotion of tourism sector is growing more quickly. In 1990, tourists visiting the country amounted to 14,400 people, while in 1991 that amount increased to 37,113 people. Year 1999-2000 was designated "Visit Lao P.D.R" and contributed to the surge in tourism, which reached 737,208 people in 2000. The impact on the economy is recorded at \$113,898,285, and was ranked number one in the economic output. In 2004 after hosting the ASEAN Tourism Forum, tourism jumped to 894,806 people, generated revenue at \$118,947,707, and was again ranked number one. In 2005, the number of tourists entering the country reached 1,095,315 people and earned \$146,770,074, 2008 the tourists entering to the country reached 1,736,787 people and earned \$275,515,758. The 2009 world financial crisis effected the Lao tourism industry. Tourism increased to 2,008,363 people and earned \$267,700,224. However, tourism recovered in 2012. The number of tourists that visited Lao P.D.R continued to increase in 2013 and reached 3,779,000 visitors and contributed about \$ 595 million (MICT, 2013)

Figure 4. 1. The Number of Tourist Visited Lao (Th.Persons)



Source: Ministry of Information, Culture and Tourism, 2014

Lao P.D.R government started to develop tourism industry and invest in tourism projects to develop the tourist facilities and infrastructure in order to encourage the private sector participation in providing tourism products and services. The high quality services should be improved. Tourism has to be integrated and upgraded to create more landscapes that are more flexible to the international market. The government has to cooperate with international organisations and on a regional level with GMS countries.

Recently Lao government has been promoting foreign entrepreneurs to invest in Lao P.D.R. According to the Law on investment promotion in Lao P.D.R, there are two types of investment, namely, the general activities and concession. Investment in general businesses activities includes a list of business activities that are allowed and

concessions that are not allowed in these kinds of business. In this kind of business investors should submit the application form in the *One Stop Service* unit at the Ministry or Department of Industry and Commerce² to become registered enterprises in accordance with enterprises law. The registered capital of these enterprises should not be less than one billion kip (\$120,000). On the other hand the term concession business refers to the activities related to the investment right that must be approved by the government such as use government property and other rights in order to develop business operations. The government granted rights include the right to concession of electricity, energy, airlines, telecommunications, insurance and financial institutions. Investors who invested in a concession business must submit the application form to the *One Stop Service* unit at Ministry or Department of Planning and Investment. After that the investors will be considered and selected case by case through a selection process by using methods such as comparative evaluation or auction. The Ministry or Department of Planning and Investment and local authorities cooperate and follow the government to promote activities in the sector depending on the priority given by government to activities related to reducing poverty, improving the quality of life of the people, building infrastructure, developing human resources, creating jobs, etc.

Moreover, the government has been promoting the *One Stop Service* unit for investors. *One Stop Service* unit serves the companies' extensive facilities especially

² For the Department level is belong to the local government in provinces

by providing information, considering the application of investment certificates of registered enterprises or certificate concessions and other promotions. Lao government also protects foreign investors as well as Lao investors. The law also gives equal rights to invest for both Lao investors and foreign investors. These incentives show that Lao government has given response to foreign investment by promoting, facilitating and motivating the economic system in Lao P.D.R.

According to the Five Year National Socio-Economic Development Plan (2016-2020) Tourism sector has been growing actively. In 2013, there are 1,916 tourist attraction sites, of which 849 are natural tourist attraction sites, 435 are cultural sites and 209 are historical tourist sites. The sector completed survey registration of 1,807 tourist attraction sites throughout the country, of which 1,042 are natural tourist attraction sites, 501 are cultural sites, and 264 are historical sites. 141 tourist attractions sites have been surveyed, 230 sites are being surveyed and 496 sites are not yet surveyed while 626 sites have been operating. There are 2 tourist attraction sites that have been accepted as world heritage and 20 sites have been endorsed by the Prime Minister's Office as national tourist attraction sites. At present, there are 290 tour companies and 75 affiliate companies throughout the country. Accommodation services have been expanded and improved to meet the standards including hotels and resorts. Up to date, there are 450 hotels across the country (the target is 300 by 2015) which consists of totally 14,593 bedrooms, the total number of

guesthouse is 1,491 which consist of 18,367 bedrooms, the total number of restaurants is 1,380, while there are 283 entertainment centers (MPI, 2015).

4.2 Overview of Luang Prabang Province

The Luang Prabang province is located in the northern part of Lao P.D.R. It is located 400 kilometres from Vientiane, the capital city of Lao P.D.R. The province consists of 12 districts. It is surrounded by Phongsaly province to the north, Xayabuly Province and Udomxay Province to the west, Xiengkhuang Province and Vientiane province to the south, and Huaphanh province and Vietnam to the east. Luang Prabang city is the municipality of the Luang Prabang province. Luang Prabang city was the old capital city of Lane Xang Kingdom meaning Million Elephants. It was established in 1353. The name of the city came from Luang meaning Large or Big and Prabang is the name of the Buddha image called Prabang. It was a gift from the Khmer kingdom to King FaNgum who was the Khmer king's son in law. According to statistics of the Luang Prabang province (2013), in 2013, the total population was 430,000 and the population of the Luang Prabang town was 80,000, with a high density of 96 persons per square kilometre (DPI, 2013). The majority of citizens in Luang Prabang are Buddhists. Almost every Lao P.D.R's people is religious. Buddhism plays a significant role in society and influences people's manner of life. Spiritual wellbeing is important to every individual in achieving common harmony.

Lao art is linked to religious expression in developing Buddhist temples throughout the centuries. In one of their reports the United Nations Educational, Scientific and Cultural Organization (UNESCO) designated 34 temples and 111 buildings of the people to protect and 450 houses, to keep up the city's tradition. UNESCO included this in the list of World Heritage in 1995 under the criteria 2, 4 and 5. One of the reasons for preserving these buildings is the unique combination of nature and architecture in their structure. Another reason for the preservation is the combination of key elements of two traditional cultures, Lao and European, in the buildings that are remarkably well-preserved (DOWH, 2013).

Luang Prabang World heritage Office is one of the representatives for the major local government to maintain, preserve heritage architecture and restore areas (heritage preserved areas) under agreements between Lao's government representative, Luang Prabang province, and UNESCO. The maintenance plan is divided into three zone conservation areas i.e old town areas, outer area across Mekong River, and the area alongside Khan River.

Transportation to Luang Prabang is available by air, road and water. The Northern Road No. 13 is the main route by which people can travel from Vientiane capital city to Luang Prabang in one day trip. This road also links Luang Prabang through the Northern provinces up to the Chinese border. The 'Mekong', 'Khan' and 'Ou' rivers are the major sources of water transportation to other provinces and

neighbouring countries. According to Luang Prabang Provincial Socio-Economic Development five year Plan (2011-2015), tourism sector is considered as one of the major priority contributors to socioeconomic development of the province. The 5 years-plan aims to build Luang Prabang as a tourism centre for cultural, natural and historical sites. It promotes Luang Prabang as a wonderful holiday town (DPI, 2010).

4.3 Main Economic Activities of the Province

According to Social Economic Development 5 year plan (2010-2015) the operating year 2006-2010, the province achieved economic development. Economic growth rate is averagely about 9%. GDP per capita, being \$1,200. The main occupation is related to agricultural activities such as cultivation of crops and livestock. Minor occupation in the province consists of employment in the private and public sector. The structure of the provincial economy consist of agricultural sector covering 39% of provincial GDP, the industrial sector accounting for 21% and service sector 40%. The economic development of the province is primarily stimulated by the private sector and foreign aid and foreign direct investment (FDI). For the last 5 years, private investment has grown significantly and now covers up to 248 projects in total accounting for a capital of \$242,7 million, of which \$127,2 million was formed by local investment. The main investment sectors are services such as hotels, restaurants, guesthouses, resorts including golf courses. They cover 40% of the total investment. Other investment sectors is the agricultural sectors such as teak and rubber plantations and wood industries. Industrial processing power and

mining was 21% of the total investment. Total exports grew rapidly, especially in agricultural products (DPI, 2010).

4.4 Tourism Development in Luang Prabang Province

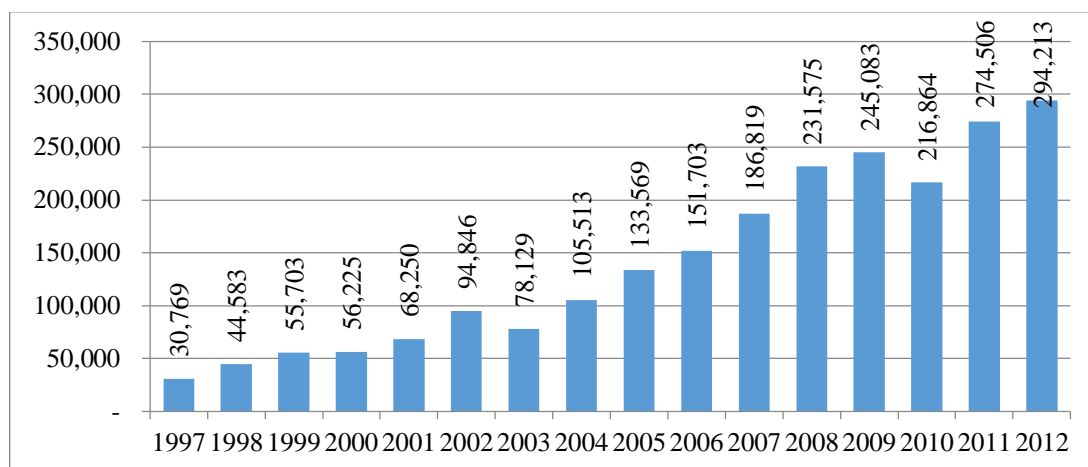
Luang Prabang City is a main tourist attraction especially due to its famous temples such as Wat Xiengthong, Wat Visoun and Luang Prabang. The splendid Royal Palace Museum is another major attraction in the city. The city has outstanding old traditional houses built before the 19th Century. European style houses can still be found on the preservation list. Town of Luang Prabang is a popular tourist destination because the city is unique, beautiful, peaceful, safe, and its residents are welcome visitors with a kind smile.

Lao PDR shares a similar culture with neighbouring countries, but also has its own unique Lao way. The city Luang Prabang exhibits key elements of this unique Lao culture and was therefore selected to the lists of World Heritage from UNESCO. The Lang Prabang City was chosen because of cultural, natural and historical reasons. Luang Prabang was the old capital city of the Lanxang kingdom. The place still preserves the characteristics of unique traditional life styles and architecture and therefore received the award of Top City from Wanderlust Magazine of England. It is the location and potential of the province that makes Luang Prabang city to be charming and interesting for local and foreign visitors. The province is appealing to local and foreign investors because of the business opportunities in the tourism sector.

The most famous festival is PI MAI Lao meaning Lao P.D.R New Year taking place during 13–15 April. Other festivals are Hmong New Year, Khmer New Year and boat racing festival. All of these festivals make Luang Prabang a great tourist destination of the country.

The number of international tourists to Luang Prabang has steadily increased from 1995 to 2012. In 1997 around 30.769 tourists visited. In 2002, that number has grown up to 94.846 tourists. In 2003, the figure fell back to 78.129 tourists. The tourist continued to increase from 133.569 in 2005 to 245.083 in 2009. In 2010 as a result from global financial crisis and political conflict of the neighbouring country, Thailand, the tourism sector saw a decrease to 216.864 visitors. After that, the number of tourists continued to grow. In 2012 about 294.213 tourists arrived.

Figure 4. 2. The Number of Tourists Visited Luang Prabang, (Persons)



Source: Luang Prabang Provincial Department of Information, Culture and Tourism, 2013

According to the location and the potential of tourism in Luang Prabang, provincial authorities have considered tourism as high priority for socio-economic development of the province. The tourism sector is the main sector that encourages and supports producing goods, telecommunications, transportation, education, agriculture, public health and national security. Moreover, the income per capita in the province has increased from \$547 in 2007 to \$1,125 in 2011 (DICT, 2013). Investment in the tourism sector has been promoted by domestic and foreign campaigns to persuade businessmen to invest in the region. Infrastructure has been built to facilitate the growth of tourism. The city has attracted foreign investment in the sector of hotels and restaurants.

The government has expanded the international airport to accommodate larger aircrafts such as Airbus and the opening of new routes to connect the region. Furthermore, the cooperation with China for connecting Luang Namtha City and Chiang Hung is going to open road transport by bus from Luang Prabang to Chiang Hung. This will open routes for commercial and tourism activities. Luang Prabang - Chiang Hung cooperation on boat tourism wants to connect the 4 countries connected by Mekong known as the gold square (Lao P.D.R - Thailand - Burma - Chinese) and connect relationships in particular among the Greater Mekong Sub-region (GMS 6) consisting of Cambodia, Lao P.D.R, Myanmar, Thailand, Vietnam, and Yunnan Province, China.

The government promotes and enhances the private sector to invest in the fields of communication, telecommunications, and electricity system and water supply in order to develop and provide satisfaction for the needs of the society. Also, the private sector improves and upgrades the service sector such as hotels, guesthouses and restaurants. Also, it develops tourist sites, facilities, and comfort for all tourism activities. In addition the private sector should be responsible for the maintenance of schools, temples, museums and historical places in Luang Prabang province. The provincial authorities support investment in business hotels, resorts, guest houses, restaurants, services or concessions activities of tourism, which makes them tend to grow faster. This will create jobs and income generation for the community. Tourism in Luang Prabang is focusing on promoting the culture of a minority to preserve and pass on to new generations to study and learn.

Luang Prabang province is one of the provinces located in the northern part of Lao PDR. It is the way to open doors to other province and south China. As the centre of the Northern Province there is potential to enhance and attract foreign investment, especially in the tourism sector. Because of its location and potential of the province, luang Prabang city is becoming charming and interesting for visitors, tourists, local and foreign investors

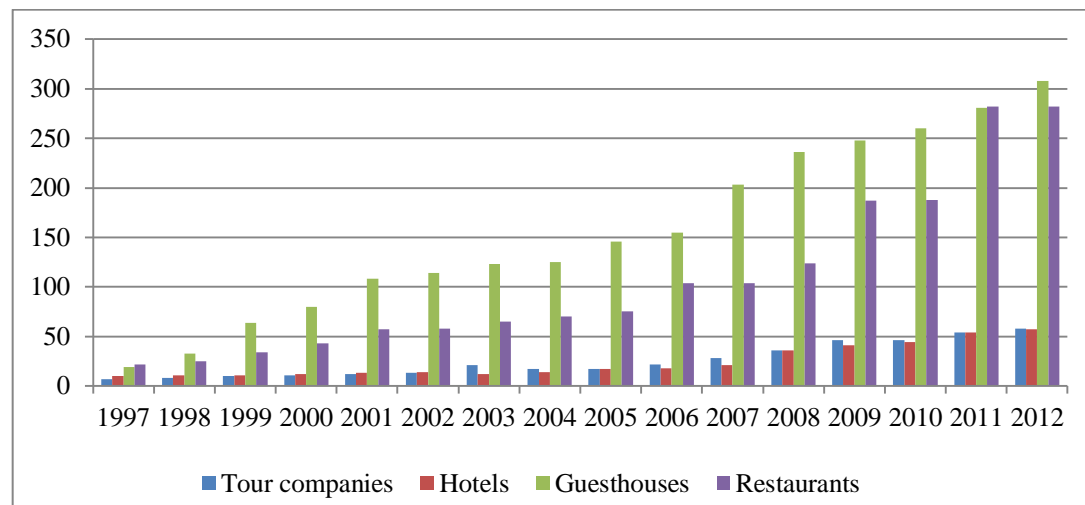
4.5 Private Sector Involvement

After UNESCO declared the city as world heritage on December 1995, the tourism sector of Luang Prabang province has begun growing continuously. In the year 2010, there were 160 attractions in total, consisting of 79 attractions in natural tourism, 67 in cultural tourism and 14 in historical tourism. Out of the 160 attractions 111 are open to visitors. Investment in tourism industry and services can attract investors both domestic and foreign, to invest in services significantly, which in the past made gross value in business services, tourism, hotels, guesthouses, restaurants and tour grow up to 850 billion kip (\$106 million) figures from 2006-2011 (DICT, 2013)

In addition to that, the hotels, guesthouses, restaurants and tour companies organized a private sector association to enhance bargaining power in its relation with the government. This association wants the governments support in developing and promoting tourism. The government and the association together organize festivals in Luang Prabang province for the public regularly. The association and the government work together to ensure that the businesses in the tourism sector are in accordance with the law. Tourism sector in Luang Prabang has improved steadily as domestic and foreign investment increased in tourism industry and services. This can attract more investment in services of tourism such as hotels, guesthouses, restaurants and tour operators. In the year 2010 the worth of turnover is 263 billion Kip (\$32,875,000) compared to 105 billion Kip (\$13,125,000) in 2008. FDI invests in

agriculture which also supports the tourism sector. For instance; growing organic vegetables to provide for the restaurants and organizing demonstrations on the farm. This is seen as the tourist activities of a farm friendly environment. In 2013 the Luang Prabang province has 57 tours companies, 54 hotels, 285 guesthouses, 282 restaurants and 227 tourist attraction sites (DICT, 2013).

Figure 4. 3. The Number of Tourism Providers in Luang Prabang Province



Source: Luang Prabang Provincial Department of Information, Culture and Tourism, 2013

In order to further develop the tourism sector, the provincial authority cooperates with international organizations in order to strengthen the tourism sector in Luang Prabang province. In the past Luang Prabang has been supported by many international organizations, which include Asia Development Bank (ADB),

sustainable tourism, and organization development from the Netherlands (SNV), the JICA, JBIC, and the KOICA. Cooperation took place with Yunnan Province to upgrade the tourism development plan in the development and management of tourism. Moreover, grants from international organizations UNESCO, European Union to develop tourism have been granted in the area (DICT, 2013)

Lao P.D.R is rich with natural resources and beautiful landscapes. The Lao government has an open policy to prepare and support the growth of investment. FDI in tourism in Lao P.D.R was instrumental in developing tourism industry. Lao government has allowed foreign investors to invest in this sector up to 100% from 2009 onwards. The investment plays an important role in the development and upgrading of infrastructure and tourism products leading to overall tourism growth. It is important for the government and private sector to understand the advantages and disadvantages of tourism industry and to analyse the conditions of the market potential of Lao P.D.R tourism development.

Chapter 5. Conclusion and recommendation

This chapter is the conclusion of the study by using the empirical and existing theory of FDI and tourism that appropriately respond to its objectives and questions. FDI inflow to Lao P.D.R has contributed largely to support social economic development of Lao P.D.R. especially during the transition from planned economy to market economy FDI creates benefits and contributes to social economic development by earning foreign currencies, technologies, increasing the total amount of products within the country, and create jobs. Moreover, FDI supports Lao P.D.R's economic growth which leads to reduction in poverty. Lao P.D.R Government has experience in terms of promoting investment from abroad to support key development during economic reform. In the last decades, FDI influx into Lao P.D.R has been growing and increasing.

Since 1990, we noticed that the increase in FDI in the world is a result of liberalizing the rules of investment. The government in many countries such as in the developing countries try to attract more foreign investment as a mechanism to develop their economy. Another aspect of the proposed investment policy is to solve major challenges related to foreign investment. Countries in South East Asian received investment from abroad since the 1980s and 1990s. These countries consider investment from abroad as the key to economic development. Lao P.D.R also used

FDI as a tool to develop their economy, which in the past has been opened up to economic cooperation with foreign countries. This experience has led to the lack of funds from foreign investment in the country. Lao P.D.R is one of the least develop countries (LDCs) and needs to improve and develop the nation by using FDI as tool for attracting more capital investment from multinational enterprises which are looking for resources, markets and minimal cost of production and services. Investors from China invested in many sectors in the economy of Lao P.D.R.

This case-study of the Luang Prabang province, where is well known as a World Heritage City. This study tries to explore the full role of FDI in tourism development in Lao P.D.R., especially to find on how FDI contributes to tourism development in Lao P.D.R. Tourism has a significant impact on poverty reduction in developing countries. The results deducted from this study clearly show that the tourism industry can attract FDI which will also function as a tool for developing the tourism sector.

Tourism is linked to many parts of economic activities. Tourism-related activities form the main source of income for the local community in the area of Luang Prabang province. The local community's livelihood depends directly or indirectly on the tourism sector. Moreover, tourism has an impact in the field of agriculture, including raising crops and livestock in their community. The crops and livestock supply the restaurants, hotels, etc. This study analyzes the

relationship between FDI and tourism development as a factor of economic growth and poverty reduction in Lao P.D.R.

By doing the qualitative and quantitative analyses, this research found that tourism plays an important role in term of increasing foreign exchange, employment, income, and integration to local economy. For the details are indicated below:

Tourism contributes to the economy of Lao P.D.R. Tourism also contributes to employment, earnings of foreign exchange and revenue of the government such as visa fee and tax from entrepreneurial businesses involved in the tourism sector. Other tourism is an important factor to reduce poverty in the area of study. Although, the policies and regulation procedures related to tourism are in place, the government should align them more with the current situation.

Tourism could create the job opportunities through the tourism activities. The most important economic tourism activities in the area of study are companies providing services to travelers, detail shops and selling handicraft. However, agricultural activity also gains benefit from tourism. A substantial amount of people is employed directly or indirectly in the tourism sector. Direct employment creates many jobs in hotels, restaurants, tour guides, marketing and handicrafts entrepreneurship. In general, there is an increasing amount of people

generating income from local tourism-related activities directly with their own businesses. Also tourism creates a good opportunity for people in the community to benefit from tourism by indirect employment.

Tourism provides long term and sustainable benefits. Tourism is a sustainable economic sector which is directly benefited to the local economy together with participating in the protection of natural environment besides creating economic value. Sustainable tourism is a great opportunity in the tourism industry. Tourism can build the necessary infrastructure to meet tourism industry, such as new hotels, guesthouses, restaurants, transport and communications, providing water supply and sanitation, safety, education and health services. These can also benefit the poor people in the community. For better improving in this industry, it may take times to develop so the government should take some possible and suitable lessons from other countries with a good model in tourism development. In addition, the government should consider and include into the master plan for long term development especially the province needs some financial support by attracting the investment from foreign investors (FDI).

In Lao P.D.R, the FDI in the manufacturing sector is positive. Regarding the service sectors, getting a clear image is more difficult due to intangible and limited data. The results of studies show that in total the related sectors have grown in terms of capital inflow, human resources development and improved

quality of institutions. FDI in areas such as agriculture, mining and hydro power have a little benefit in upgrading skilled labor and technology transfer of the host country. FDI in manufacturing sectors are growing. Indeed, FDI has benefits and strengthened the upward trend in the manufacturing industry. FDI in the tourism sector is not clear because this sectors are related to many economic sectors. In this study, I focus on hotels, restaurants and travel agencies as a proxy. This research recommends that all forms of FDI have advantage in economics of the host country.

Research has discovered that sustainable economic development in the long term requires the government to fix the forms of investment and to consider carefully before investing and attracting investment. In the past, FDI in some areas had a negative impact on social-economic community and the environment, particularly on natural resources. In the current situation the government should set the target of the country's policies to attract more FDI. The government should encourage and give priority to that sector. In Lao P.D.R's economic development policy obtains the FDI, which is the key to ensure the long run of the economic development.

Therefore, this study can conclude that the FDI is the first contribution to the development of Lao P.D.R' tourism industry; even though, this research has some limitations but it also reached a significant findings which covered the

scope of the study and development of Lao P.D.R. for further extended study in the future, the researchers should focus on: (1) collecting the primary data and information such as field survey of individual sectors. This could help in getting the opinions from investors, businessman and policies makers and, (2) looking for opportunities and lessons from tourism development industry in the Province.

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