

## 2. Leveraging Electricity Sector to Ease External Public Debt in Lao PDR<sup>96</sup>

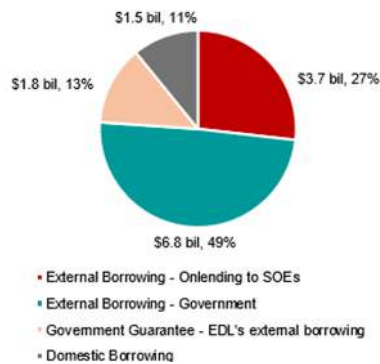
At the end of 2023, Lao PDR's external public debt, including government-guaranteed debt, stood at USD12.3 billion, or 96% of GDP, with annual debt servicing of more than USD1 billion expected in the coming years. Meanwhile, the country's access to capital markets for FCY funding has deteriorated, as highlighted by the downgrade of its sovereign credit rating to non-investment grade by the Thai credit rating agency in September 2023.

This selected issue provides an overview of the external public debt situation of Lao PDR and analyzes how the country's electricity sector could contribute to managing this debt. While some electricity SOEs are facing financial challenges as illustrated in Box B, the sector as a whole has potential to drive the country's economic growth<sup>97</sup> and contribute to resolving external public debt issues. Against this backdrop, the current selected issue mainly outlines how the government of Lao PDR could leverage the electricity sector in the short, medium and long term.

### Overview of Lao PDR's External Public Debt

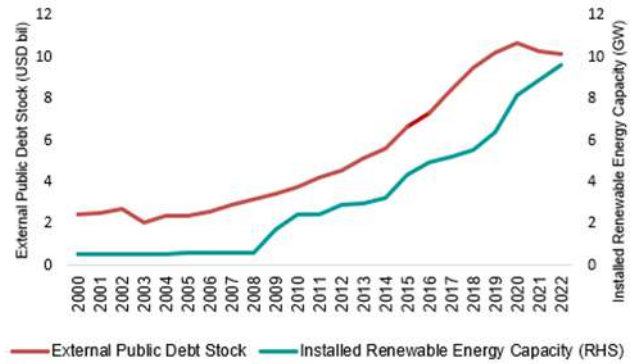
**1. The dominant component of Lao PDR's public debt is external public debt, which is government debt denominated in FCY.<sup>98</sup>** As of end-2023, the country's total public debt, including government-guaranteed debt, amounted to USD13.8 billion, equivalent to 108 percent of GDP, of which external public debt accounted for USD12.3 billion, or 96 percent of GDP. Further breaking down the external public debt, government borrowing makes up USD10.5 billion, and government-guaranteed debt, USD1.8 billion. More than a third of the government borrowing, comprising USD3.7 billion, were allocated to on-lending to SOEs in the electricity sector, including EDL. In addition, all the government guarantees were tied to EDL's own external borrowing (Figure A2.1).<sup>99</sup> Lao PDR's external public debt started to increase in the early 2000s and particularly after 2009, when the country began to develop renewable energy, especially hydropower, to fuel economic growth through export of electricity (Figure A2.2).

**Figure A2.1. Composition of Public Debt as of end-2023**



Source: LMOF; AMRO staff compilation

**Figure A2.2. Increase in External Public Debt Stock and Renewable Energy Development**



Source: CEIC; AMRO staff compilation

<sup>96</sup> Prepared by Akifumi Fujii, Economist.

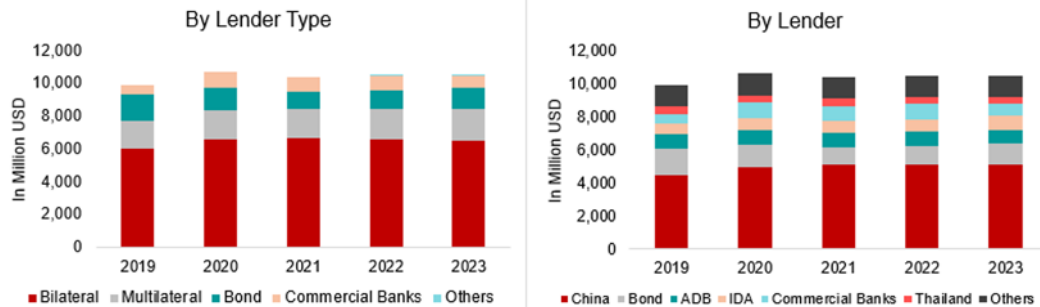
<sup>97</sup> For details, see Selected Issue 1: Assessing Sustainability of Electricity Sector Growth in Lao PDR by Naoaki Inayoshi and Sota Nejime in AMRO Annual Consultation Report on Lao PDR 2023.

<sup>98</sup> In Lao PDR, public debt is classified based on the currency. Irrespective of creditors' residence, public debt denominated in FCY is considered external public debt, while public debt denominated in the kip is domestic public debt. According to AMRO staff estimates, domestic creditors were holding about 10 percent of external public debt, excluding government guarantees, at the end of 2023.

<sup>99</sup> In Lao PDR, the non-government guaranteed debt of SOEs, which totaled USD3.3 billion as of end-2023, is not included in the public debt. Out of the USD3.3 billion, USD2.3 billion is incurred by the Laos-China Railway and USD0.9 billion by EDL-Gen.

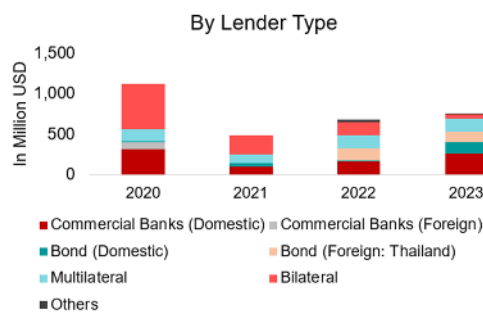
**2. While loans from China constitute almost half of Lao PDR’s external public debt, domestic bank loans and domestic bond issuances have increased recently.** Multilateral lenders such as the Asian Development Bank (ADB) and the International Development Association (IDA) of the World Bank Group follow the lead of bilateral lenders including China (Figure A2.3). Because of greater constraints on borrowing through bilateral and multilateral channels, the Laotian government has increased commercial borrowing through domestic bank loans and domestic bond issuances in the past few years (Figure A2.4). Further, since bond issuances in Thailand have become very costly due to TRIS Rating’s downgrade of the Lao sovereign credit rating in September 2023, the government has increased fundraising from the domestic market. As a result, short-term funding at high-interest has been on the rise (Table A2.1). However, 60 percent of the government’s external borrowing is still made on concessional terms, with 85 percent of the external borrowing at fixed interest rates, indicating low exposure to interest rate fluctuation risks. By currency, borrowing in U.S. dollars accounts for 59 percent of the total external borrowing.

Figure A2.3. External Public Debt Stock by Lender



Source: LMOF; AMRO staff compilation  
 Note: “Bond” and “Commercial Banks” include both foreign and domestic investors and banks, although the breakdown is unknown.

Figure A2.4. External Public Debt Disbursement 2020-2023



Source: LMOF; AMRO staff compilation

Table A2.1. Cost and Maturity of Public Debt

	2020	2021	2022	2023
Interest Payment to GDP	1.59%	1.00%	1.89%	1.93%
Short-term Debt to Total Public Debt	11.06%	12.42%	15.15%	13.85%

Source: LMOF; AMRO staff compilation

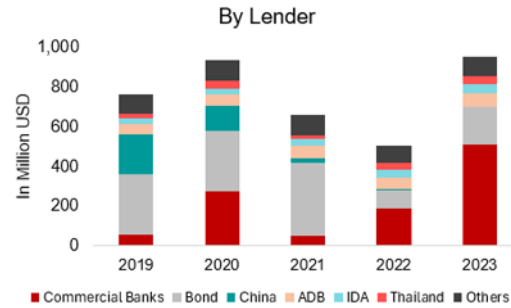
**3. Although Lao PDR was scheduled to repay more than USD1 billion annually from 2020 to 2023, it managed to secure major creditors’ agreement to suspend repayments.** While fiscal revenues in FCY have exceeded pre-pandemic levels,<sup>100</sup> these have been insufficient to fulfill the repayment obligations. Furthermore, international reserves in the Bank of the Lao PDR (BOL) are too low to be tapped.<sup>101</sup> As a result, the government has found it

<sup>100</sup> Fiscal revenues in FCY consist of tax and non-tax revenues, including corporate income tax, lump-sum tax, royalty fees, concession fees, and interest payments from SOEs. Hydropower, mining, transport in the form of overflight fees, and cryptocurrency industries are the main sources. In 2023, these revenues surpassed USD400 million, higher than the pre-pandemic level of USD360 million in 2019.

<sup>101</sup> To increase the FCY supply in the market and the international reserves, the BOL implemented a new regulation mandating the repatriation and a minimum conversion requirement of export proceeds. For more details, see Box A.

necessary to borrow more in FCY to cover the shortfalls. However, as mentioned above, the borrowing options have gradually become limited. Against this backdrop, the government agreed with major creditors to suspend repayments totaling USD1,892 million<sup>102</sup> from 2020 to 2023 (Figure A2.5), and to commit to annual debt servicing of more than USD1 billion from 2024 to 2028. Given the commitment, fulfilling FCY liquidity shortfalls is a big challenge for the government of Lao PDR.

Figure A2.5. External Public Debt Service 2015-2023 (Actual)

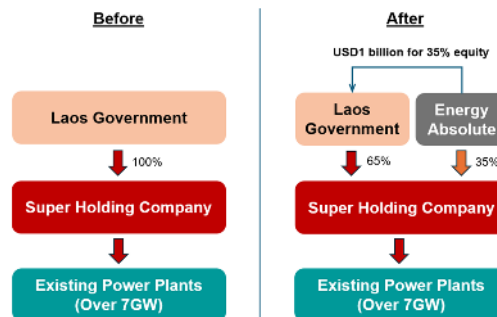


Source: LMOF; AMRO staff compilation

### Strategies to Address Future External Debt Services – Leveraging Electricity Sector

**4. The Lao government is carrying out a short-term funding strategy that involves partially selling and privatizing power plants by establishing a super holding company.** The government will transfer more than 7GW of existing power plants to a new super holding company and sell 35 percent of its shares in the company to Energy Absolute, a Thai-based alternative energy firm (Figure A2.6).<sup>103</sup> The Lao government expects to earn USD1 billion from this equity sale and intends to use the proceeds for external debt repayment. Asset selection for transfer to the super holding company is now underway alongside negotiations with Energy Absolute. The Lao government aims to complete the transaction by the end of 2024.

Figure A2.6. Planned Scheme for Super Holding Company Transaction



Source: AMRO staff compilation

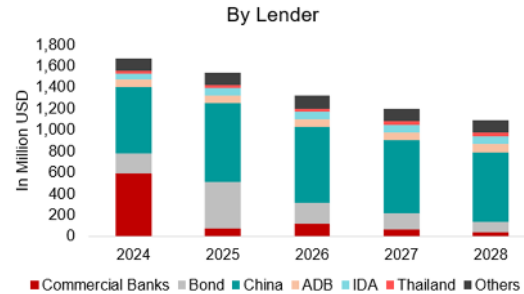
**5. Considering possible delays in closing the super holding company deal, the government is concurrently negotiating debt restructuring with major creditors.** The temporary suspension of debt repayments from 2020 to 2023 has helped the country manage its foreign exchange liquidity. However, more comprehensive debt restructuring is desirable as debt servicing in excess of USD1 billion will continue for each of the next five years (Figure

<sup>102</sup> The USD1,892 million comprised suspended principal repayments of USD1,422 million and suspended interest payments of USD470 million.

<sup>103</sup> In May 2024, the Lao government concluded a joint development agreement with Energy Absolute regarding the super holding company.

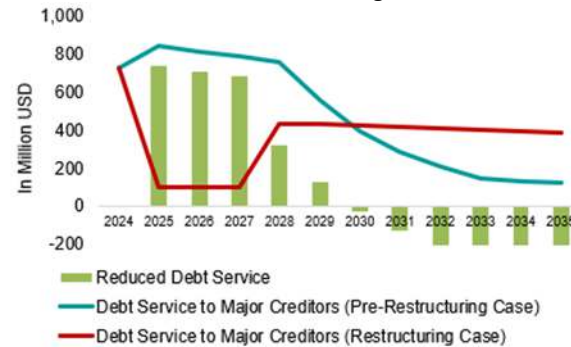
A2.7). According to AMRO staff estimates, sustainability of external public debt could be restored if the country were to conduct the following debt restructuring with major creditors: (1) suspending principal repayments from 2025 to 2027, (2) resuming principal repayments from 2028 in 15-year equal installments, and (3) reducing interest rates to 2 percent (Figure A2.8).

Figure A2.7. Scheduled External Public Debt Service 2024-2028



Source: LMOF; AMRO staff compilation

Figure A2.8. Level of Annual Debt Servicing under Different Scenarios



Source: LMOF; AMRO staff estimates

Note: Under the pre-restructuring case: (i) the projection on debt servicing is based on the outstanding debt as of end-2023, and (ii) the deferred principal and interest payments between 2020 and 2023 are assumed to be repaid to the major creditors over the weighted average maturity as of end-2023.

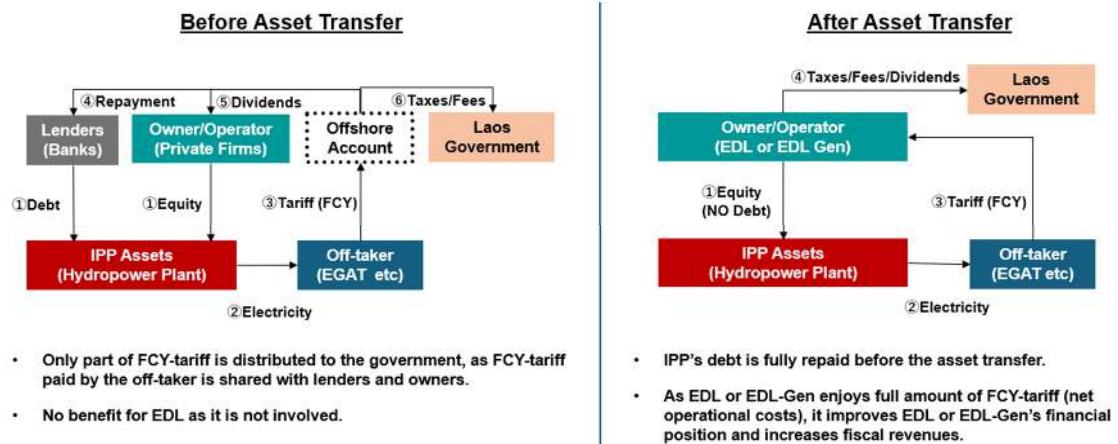
**6. In the medium term, it is also important to restore EDL’s profitability to avoid additional fiscal burdens.** As mentioned in Box B, the Lao government has provided substantial government guarantees to EDL totaling USD1.8 billion. If EDL encounters difficulties in its debt repayment and calls for government guarantees, it will put more pressure on the government’s FCY cash flow. To restore EDL’s profitability, the government needs to consider a road map to increase electricity tariffs at least to cost recovery levels, in addition to EDL’s cost-cutting efforts.<sup>104</sup>

**7. As an initiative over the longer term, the government should also consider how to monetize IPP assets developed under the Build-Operate-Transfer (BOT) scheme.** According to the BOT scheme, power plants will be transferred to the government at the end of the concessionary period. These IPP assets can benefit the government in the following ways. Firstly, most IPPs in Lao PDR export electricity to neighboring countries such as Thailand, earning a steady stream of foreign exchange. Secondly, IPP debts are usually fully repaid by the end of the concessionary period. Therefore, the Lao government could acquire profitable IPP assets without debt, presenting an opportunity to reap the full benefits of FCY incomes (Figure A2.9). However, if the government plans to take over IPP assets and operate them

<sup>104</sup> According to the Ministry of Finance of Lao PDR, EDL has reduced its workforce by roughly 1,000 employees out of about 6,000 in total.

through SOEs such as EDL or EDL-Gen, meticulous preparation would be warranted. This includes prior discussions with current concessionaires to sort out staff training and the handover, and negotiation of power purchase agreements with electricity off-takers. Since the first asset transfer is scheduled to happen in 2029, the government needs to start preparations now.

Figure A2.9. IPP Asset Transfers under BOT Scheme



Source: AMRO staff compilation

### Conclusion

**8. Although the government of Lao PDR is facing challenges in managing external public debt, there is room to restore debt sustainability.** The electricity sector has the potential to help overcome these difficulties. The Lao government could improve the situation by steadily advancing short, medium and long term efforts as described above.

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