About the Joint Programme “High-Frequency Data”

The global COVID-19 pandemic, coupled with the food, energy, and financial crisis has exacerbated the vulnerability of households and increased poverty. According to the UN Global Crisis Response Group, the world has not been in this state in recent history: 60 per cent of workers have lower real incomes than before the pandemic; 60 per cent of the poorest countries are in or at high risk of debt distress; developing countries lack USD1.2 trillion per year to fill the social protection gap, and USD4.3 trillion will be needed annually - more money than ever before - to meet the Sustainable Development Goals (SDGs).[10]

Lao PDR is no exception. The inflation rate in Lao PDR hit 34.1 per cent in September 2022, the highest since May 2000, amid a surge in energy and consumer goods prices.[11] According to the latest numbers of the Lao Statistics Bureau of September 2022, the price of food rose by 35.54 per cent, while transport costs recorded an increase by 53.8 per cent and healthcare products including medicine increased by 44.5 per cent. Driven by the global energy market, in combination with the shortage of foreign currency reserves, the price of fuel has also increased substantially, and the risk of further fuel shortages such as that faced earlier this year is not over. Owing to macroeconomic structural imbalances, the value of the country’s national currency – the Lao Kip – has depreciated. Existing regular data monitoring systems provide information only with a time-lag, and often in an aggregate form. In a context where substantial shifts occur within days and weeks, there is a need for higher-frequency data. To better understand the impact of the fast-evolving food, energy and financial crisis on the nation’s fiscal capacity and on individual households, in collaboration with the Lao Academy for Social and Economic Sciences / MRI, the UN in Lao PDR prepared a Joint Programme on “High-Frequency Data” with the aim to provide targeted, disaggregated, and timely data to inform efficient policy responses and potential course correction.

The Joint Programme aims at issuing three bulletins to policymakers at all levels. The first issue focuses on understanding and identifying vulnerable groups[12] impacted by the crisis in the country; the second focuses on ‘Food Security and Livelihoods’, and the third, this final bulletin, is on ‘Macroeconomic Analysis of the Country’s Economy’. Lastly, a final summative policy dialogue workshop will bring together all concerned government sector ministers, United Nations agencies, and other development partners to deliberate on the key findings and chart the way forward.

The Joint Programme is supported by the Joint SDG Fund – Development Emergency Modality Response to the Global Crisis on Food, Energy, and Finance.[13]
EMERGING ISSUES

Emerging Issue 1: Consumer confidence has declined, but still shows cautious optimism

Consumer sentiment is a key indicator of the macroeconomic outlook. When consumer confidence is weak, it signals caution among the population at large and insecurity about the near future. This can lead to decreased spending on goods and services, which reduces economic growth and can have a ripple effect throughout the economy.

As part of this High-Frequency Data Joint Programme, MRI has increased the rate of survey rounds for the Consumer Sentiment Index (CSI) in late 2022 and early 2023 to provide faster evidence of the direction of consumer sentiment. Noting the CSI threshold value of over 100, indicating consumer optimism, whilst a value below 100 indicates a more pessimistic outlook, as of Q1/2023, the overall Lao PDR CSI[13] stood at 111.9, a decline from 116.4 in Q4/2022, but still above the threshold for an optimistic outlook[16].

However, looking at the individual components measured within the index, for example, the financial situation alone was below the benchmark of 100, indicating that households feel pessimistic about the economy more generally and as it may be perceived to affect their personal finances[16]. Households reported cutting spending on several items, including food, healthcare, education, and durable/common goods. Most households also cut their spending on entertainment and recreation[17].

Households continue to exhibit considerable uncertainty over inflation expectations. Hence, their confidence level is disposed to decrease by 6.2 per cent to 105.0 in Q2/2023[16]. This implies that with less confidence, the households may not increase their consumption in the near future.

Figure 1: Consumer Sentiment Index

![Consumer Sentiment Index Graph]

Source: MRI, LASES

Emerging Issue 2: Cautiously rebounding business confidence

In contrast to consumers, businesses have been more pessimistic over recent months, but confidence has shown signs of improvement over successive survey rounds.

The Business Tendency Index (BTI) has increased from 81.4 in Q4/2022, to 97.0 in Q1 2023, and expected to reach 101.5 in next quarter (Q2/2023)[19]. Whilst the index is below the benchmark of 100 in some components, such as employment and cost of operation, the figure’s improvement suggests that this pessimistic sentiment is slowly beginning to give way to a more optimistic outlook.

The costs of production/operation fell in Q1/2023 compared to Q4/2022. This can be seen in an improving index for production/operation costs (64.1 in Q4/2022, increasing to 67.4 in Q1/2023). Declining prices of global commodities (especially fuel prices) and stable local currency since the end of 2022 are seen as a key factors underpinning declining costs of production and operation[20].
Emerging Issue3: Controlling the inflation rate will be a significant challenge for policymakers

Lao PDR has seen a rapid acceleration in inflation since early 2022, with important consequences for the affordability of basic necessities. About 70 per cent of the Lao population reported spending less on healthcare and education in December 2022, which could further undermine the government’s human development and poverty reduction efforts.

MRI analysis of the determinants of this inflation suggests that underlying factors reflecting the structure of the economy and the behavior of firms and individuals play an important role. For example, in part reflecting the reliance of the Lao economy on imports, the exchange rate for the Lao Kip (LAK) also showed a clear and significant relationship with inflation. The price of fuel alone, all of which is imported, has a statistically significant effect on the headline inflation rate.

The analysis also points towards the inflation building up momentum, which may make it more challenging for policy responses to bring the rate of price increases under control.

Lagged Consumer Price Index (CPI) shows a strong correlation with current CPI. Conversely, the policy levers available to counter accelerating inflation show substantially weaker transmission. For example, the volume of currency in circulation does show a statistically significant relationship with CPI, but the correlation is only around half as strong as that with the exchange rate. Official reserve requirements for commercial banks and the policy interest rate did not show a statistically significant relationship with CPI.

Notes:
- Smavong & Vialvong. Laos must address rising inflation in 2023. EAST ASIA FORUM, 1 Feb 2023
- Correlation of 0.733, statistically significant at 1 per cent confidence interval; MRI, LASES, Determination of Consumer Price Index (draft), Feb 2023
- Correlation of 0.275, statistically significant at 1 per cent confidence interval; Ibid
- Correlation of 0.918, statistically significant at 1 per cent confidence interval; Ibid
- Correlation of 0.339, statistically significant at 1 per cent confidence interval; Ibid
- MRI, LASES, Price Structure of Key Commodities (draft report), Feb 2023
Emerging Issue 4: Exogenous factors play a key role in determining the price of key commodities

The prices of fertilizer and animal feed play an important role in the evolution of overall inflation in Lao PDR. As these items are inputs in many other industries when the prices of these items increase, it can lead to an increase in the overall cost of production. Moreover, as these prices increase, it can reduce farmers’ profits and put a strain on their livelihoods. The demand for animal feed in Lao PDR in 2022 was estimated at about 592,670 tons, of which about 60 per cent was produced domestically\(^1\). However, over 60 per cent of the raw materials included in domestic feed production were imported. The cost structure of animal feed consists of raw materials and other costs; the raw materials cover roughly 77 per cent of the total cost\(^2\). This implies that exogenous factors play a significant part in setting the price of animal feed in the country.

Figure 4: Domestic price for essential foods and Domestic price of animal feed (Unit: Lao LAK)

Prices for agricultural fertilizer in the global market have climbed significantly over the past year. Fertilizer prices have risen nearly 30 per cent since the start of 2022, with a peak in 2022 that saw an 80 per cent surge\(^3\). This has directly impacted almost all vulnerable economies around the world, including Lao PDR. On average, fertilizer price in the country has increased by nearly 112 per cent compared with the previous year\(^4\). Whilst both the international and domestic prices of fertilizers have shown significant increases, since September 2022 the international price has shown a decline whilst the domestic price continues to appreciate.
The increase in fertilizer price in Lao PDR is mainly derived from the depreciation of LAK, transportation costs, and labor costs\textsuperscript{31}. This, in turn, has led to a decline in fertilizers import in recent months, as they became less affordable. The sharp increases in the prices of fertilizers and animal feed, are, therefore, also likely leading to discouraged agricultural activity and associated food processing and manufacturing.\textsuperscript{32}

**Figure 5: Trends of fertilizer prices (domestic vs. international markets)**

Source: MRI Price Structure of Key Commodities (draft report), estimated based on data from the Ministry of Industry and Commerce and World Bank.

**POLICY RESPONSES**

Whilst showing some areas of optimism, both Consumer Sentiments and Business Tendency surveys show that the economic situation remains fragile for many. This points towards the urgent need to continue progress in stabilizing the macroeconomic situation and protecting the most vulnerable from negative consequences.

The research has shown that both domestic and exogenous factors contribute to the rising prices in the country, calling for a unique blend of policy measures that includes – monetary and fiscal policies that address the LAK depreciation, money supply, and the increase in fuel price, as well as strengthening international partnerships.

It is also imperative for the Government of Lao PDR to prioritize and address issues related to rising prices of fertilizer and animal feed prices in order to stabilize the cost of living and protect vulnerable members of a largely rural and agrarian society highly and directly dependent on these commodities.

\textsuperscript{[17]} Ibid
\textsuperscript{[18]} Ibid
\textsuperscript{[19]} World bank, 2022
\textsuperscript{[20]} MRI, LASES, Price Structure of Key Commodities (draft report), Feb 2023
\textsuperscript{[21]} MRI, LASES, Price Structure of Key Commodities (draft report), Feb 2023
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