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**Report No. P-5707-LA**

**MEMORANDUM AND RECOMMENDATION**  
**OF THE**  
**PRESIDENT OF THE**  
**INTERNATIONAL DEVELOPMENT ASSOCIATION**  
**TO THE**  
**EXECUTIVE DIRECTORS**  
**ON A**  
**PROPOSED CREDIT**  
**OF SDR 6.3 MILLION**  
**TO**  
**THE LAO PEOPLE'S DEMOCRATIC REPUBLIC**  
**FOR A**  
**FOREST MANAGEMENT AND CONSERVATION PROJECT**

**FEBRUARY 23, 1994**

**MICROGRAPHICS**

Report No: P- 5707 LA  
Type: MOP

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CURRENCY EQUIVALENTS

(as of November 1, 1993)

Currency Unit = Kips  
Kip 1.00 = US\$0.0014  
US\$1.00 = Kips 715

WEIGHTS AND MEASURES

1 kilogram (kg) = 2.20 lb  
1 kilometer (km) = 0.62 mile  
1 hectare (ha) = 2.47 acres

ABBREVIATIONS AND ACRONYMS

DOF - Department of Forestry  
FINNIDA - Finnish International Development Agency  
FRCP - Forest Resources Conservation Project  
GEF - Global Environment Facility  
GET - Global Environment Trust Fund  
ICB - International Competitive Bidding  
LCB - Local Competitive Bidding  
MAF - Ministry of Agriculture and Forestry  
SIDA - Swedish International Development Authority  
TFAP - Tropical Forestry Action Plan

FISCAL YEAR

October 1 - September 30

LAO PDRFOREST MANAGEMENT AND CONSERVATION PROJECTCredit and Project Summary

Borrower: Lao PDR

Amount: SDR6.3 million (US\$8.7 million equivalent)

Terms: Standard, with 40 years' maturity

Financing Plan:

	<u>Local</u> -----	<u>Foreign</u> US\$ million	<u>Total</u> -----
Government	1.0	0.0	1.0
GET	1.2	3.8	5.0
FINNIDA	0.9	4.7	5.6
IDA	2.4	6.3	8.7
TOTAL	<u>5.5</u>	<u>14.8</u>	<u>20.3</u>

Economic Rate of Return: Not applicable

Poverty Impact: Program of Targeted Interventions

Staff Appraisal Report: Report No. 10276-LA

Maps: IBRD Nos. 23388, 23534

**MEMORANDUM AND RECOMMENDATION OF THE PRESIDENT  
OF THE IDA TO THE EXECUTIVE DIRECTORS  
ON A PROPOSED CREDIT  
TO THE LAO PEOPLE'S DEMOCRATIC REPUBLIC  
FOR A FOREST MANAGEMENT AND CONSERVATION PROJECT**

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1. I submit for your approval the following memorandum and recommendation on a proposed development credit to the Lao People's Democratic Republic for SDR6.3 million (US\$8.7 million equivalent) to help finance a Forest Management and Conservation Project. The proposed credit would be on standard IDA terms, with a maturity of 40 years. The project would be cofinanced by a SDR3.7 million (US\$5.0 million equivalent) grant from the Global Environment Trust Fund (GET) and a Finnish Marks 28.0 million (US\$5.6 million equivalent) grant from the Finnish International Development Agency (FINNIDA) for parallel financing.

2. Country/Sector Background. The Lao economy is among the least developed in the world, with an average per capita income of about US\$200 (1990). With a population of about 4.2 million people for a total area of 236,000 sq km, the country has a low population density of 17 persons per sq km, but population is growing at 2.9% per year. About 89% of the people live in some 11,000 rural villages. Up to 75% of the land area is hilly to mountainous, predominantly in the north and east, and due to the shortage of lowlands, is under increasing pressure from forest encroachment.

3. The Forest Resource. Lao PDR is heavily dependent on its natural resource base to provide a livelihood for the bulk of its population and to earn foreign exchange. In 1991, wood products accounted for up to 54% of official exports, while the share of forestry in the Gross Domestic Product was estimated at about 15%. Moreover, some 80% of domestic energy consumption is wood-based, while the forests also provide a host of minor products, foodstuffs and medicine which are also exported. However, the forest cover of Lao PDR is declining steadily. From 1940 to 1981, the national forest area fell from 16 million ha (70% of the country) to 11 million ha (48%), corresponding to an average annual loss of 120,000 ha, or about 1% of total forest area per annum. The Tropical Forestry Action Plan (TFAP) for Lao PDR, which was completed in 1990 with multi-donor support, reported that of the 300,000 ha annually under shifting cultivation, about 100,000 ha involved clearing of forest land while another 100,000 ha were degraded by forest fires. Illicit logging was estimated at about 50% of authorized logging, and unsustainable commercial exploitation using destructive logging practices also significantly contributed to forest degradation. Other factors included the marginalization of forest communities, distortions in pricing and taxation policy which encouraged malfeasance and transfer pricing, and inefficient domestic processing.

4. Forestry Sector Reforms. In the past two years, Government has been developing a forestry reform program. The main features are the improvement of forest inventory and management planning, change of emphasis from forest extraction to sustainable management, provision of incentives to resource users, re-establishment of central jurisdiction over forest management, and elimination of distortions in resource pricing and taxation. To support this reform program, Government issued in November 1993 a Prime Minister's Decree No. 169 on the Management and Use of Forests and Forest Land (the Forestry Decree), and the

entry into effect of the Decree is a condition of Credit effectiveness. This project, which supports the reform program, is consistent with the Bank's forestry policy.

5. Project Objectives. The project aims at assisting Government to implement a new resource management system in Lao PDR to better achieve the sustainable management and conservation of the country's forest resources. The integrated project focuses on implementing forestry sector reforms, developing the Department of Forestry's operational capacity, and implementing improved programs in forest inventory and planning, and sustainable forest management and protection. Project activities in production and village forest areas would be supported by IDA, while the establishment of protected areas for biodiversity conservation would be funded by GET for a Wildlife and Protected Areas Management Project which is an integral part of the project. FINNIDA would fund technical assistance and human resource development for production and village forest areas, and GET for the protected areas.

6. Project Description. The project would cover an estimated total forest area (Maps 23388 and 23534) of about 500,000 ha in provinces throughout the country with forest resources, to be zoned and delineated into village, protection, conservation and production forests, and placed under sustainable forest management and protection. The project areas are located mostly in the central and southern regions, which still have a large proportion of relatively intact natural forest and include several proposed protected areas for biodiversity conservation. Specifically, the five-year project would support:

- (a) implementation of an appropriate institutional framework and formulation of the necessary regulatory framework for the forestry sector;
- (b) field implementation of three programs: (i) forest resource inventory and planning; (ii) sustainable forest management and protection; and (iii) establishment and management of protected forest areas;
- (c) human resource development; and
- (d) technical assistance.

7. Project Implementation. The project would be implemented by the Department of Forestry. The total project cost is estimated at US\$20.3 million equivalent, with a foreign exchange component of US\$14.8 million equivalent (73%). The total financing required is US\$19.3 million, of which IDA would finance US\$8.7 million equivalent (41% of total foreign exchange costs and 46% of local costs), GET US\$5.0 million (25% of foreign exchange costs and 24% of local costs), and FINNIDA an amount of US\$5.6 million on a parallel basis. A breakdown of project costs and the financing plan are shown in Schedule A. Amounts and methods of procurement and of disbursements, and the disbursement schedule are shown in Schedule B. A timetable of key project processing events and the status of Bank Group operations in Lao PDR are presented in Schedules C and D, respectively. Maps are also attached. The Staff Appraisal Report, No. 10276-LA, dated February 23, 1994, is being distributed separately.

8. Project Sustainability. The sustainability of the project is dependent on continued Government commitment to the new resource management

system, based on the provision of adequate incentives to forest users and effective field capability for regulation and control of forest resource use. In addition to supporting the formulation of the necessary regulatory framework, the project design includes the protection of traditional access of users to the forest resources and limited buffer zone development to reduce unsustainable forest exploitation in exchange for forest conservation measures for community and private forest users. Public agencies would be compensated for reduced dependence on forest products from the Forest Management Fund to be established under the Forestry Decree from resource tax revenues and other sources. This Fund would be managed by DOF and used to fund its activities, including the operation of the protected areas system. The establishment of a Conservation Trust Fund under the project is aimed at securing additional longer term financing for the operation of the protected areas.

9. Lessons Learned from Previous IDA Operations. The first four agricultural projects supported by IDA were implemented under a centrally-planned economy. They were constrained by a weak institutional framework, unclear or inappropriate sectoral policies, and lack of production incentives. The PCRs and PPAR of these projects highlight the importance of good technical preparation and the critical role of IDA supervision as Lao project skills are limited. Grant funding was thus obtained from the Japan Policy and Human Resources Development Fund to support detailed project preparation, and intensive IDA supervision would be undertaken during project implementation. For sustainable resource management, a system based on adequate resource planning and management and on adequate incentives to all resource users needs to be established and sustained. The project is designed to achieve these objectives.

10. Rationale for IDA Involvement. Since 1986 Lao PDR has been moving from a centrally-planned to a market-oriented economy and implementing structural reforms. Macroeconomic stabilization measures, such as restoration of monetary and fiscal control and price and exchange rate stabilization, have been very successful. Emphasis is now being placed on longer run institutional development measures, such as legal, public administration, and state enterprise reform, and on the sustainable development of its natural resource base. The Government remains committed to these reforms and to the development of basic physical infrastructure, and social and support services.

11. The objectives of IDA's country assistance strategy, as discussed by the Board on October 6, 1992, are to support: (a) Government efforts to move to a market economy and maintain macroeconomic stability; (b) development of the physical capital needed to expand production; (c) sustainable use of the country's natural resources; and (d) human resource development, both to increase labor productivity and alleviate poverty. This project is a key component of the Bank's overall assistance strategy as it will help to implement key reforms in the forestry sector necessary to attain sustainable forest management, and develop and strengthen sector institutions and the human resource base to implement this strategy. IDA has mobilized substantial cofinancing for the proposed project, and has sought to coordinate its activities with other multilateral and bilateral donor agencies to help ensure a sustained and coordinated development effort in the sector.

12. Agreed Actions. Conditions for Credit effectiveness include: (a) the Forestry Decree shall have become effective; (b) establishment of the Project Coordination Committee; and (c) the FINNIDA Cofinancing and the GET Grant

Agreements shall have become effective. Covenants in the Development Credit Agreement include: (a) award of a minimum of two forest management contracts incorporating sustained yield and conservation practices by competitive bidding by March 31, 1996; (b) presentation of satisfactory land and forestry legislation to the National Assembly by September 30, 1997; (c) issuance of implementing regulations to the Forestry Decree is a condition of disbursement for incremental operating costs (on declining basis) of salaries and other allowances; (d) establishment of a uniform pricing and taxation system to ensure parity pricing for the sale of logs for both the domestic and export markets by June 30, 1995; (e) forming of an advisory Consultative Forum by the Project Coordination Committee not later than December 31, 1994; (g) carrying out of a mid-term review of the project by MAF and IDA not later than October 31, 1997; and (h) cross-default conditionality in respect of the FINNIDA Cofinancing and the GET Grant Agreements.

13. Environmental Aspects. The environmental impact of the project would be positive due to improvements in sustainable resource management and biodiversity conservation. The strengthening of the resource data base and management planning, the implementation of sustainable forest management and conservation practices, the enforcement of a regulatory system, and the establishment of protected areas would reduce deforestation and the destruction of wildlife habitats, biodiversity, and watershed values. Environmentally sound village development activities would assist in reducing unsustainable exploitation of forest resources.

14. Program Objective Categories. The project would support the development of forest communities, which are among the poorest segments of the Lao population. It also addresses the Bank's other program objectives, including sustainable resource management and conservation, and human resources and private sector development.

15. Project Benefits. Only the benefits from improved efficiency in forest management and rent capture can be readily quantified. The Net Present Value of the potential rents that could be captured under a ten-year phased program of improved forest regulation and taxation would amount to US\$30.5 million at a 12% discount rate, including US\$16.6 million from export parity pricing and taxation, US\$8.1 million from reduction in the mis-specification of export logs, and US\$5.8 million from reduced log wastage and degradation. Benefits which are difficult to quantify include those from maintaining the integrity of watersheds, biodiversity, non-wood forest products, and from the impact of maintaining forest cover on the potential for hydro-electric development. If the project is not implemented, continued unsustainable forest exploitation will accelerate forest degradation and loss of wildlife habitats, plant and animal species.

16. Risks. The main risks would arise from delays and inadequate implementation of the new system of resource management, including only partial acceptance of the national program approach by provincial governments, slow adoption of community mobilization for resource management, poor application of regulation and control activities, failure to establish and apply the Forest Management Fund appropriately, and administrative weaknesses. The provision of adequate incentives to managers and users of the forest resources for sustainable forest management and conservation is designed to minimize these risks. For the protected areas, shortage of budgetary funds for longer term recurrent cost

financing may affect the sustainability of the system. The establishment of the Forest Management Fund under the Forestry Decree is aimed at addressing the issue of financing of DOF operations.

17. Recommendation. I am satisfied that the proposed development credit would comply with the Articles of Agreement of the Association and recommend that the Executive Directors approve it.

Lewis T. Preston  
President

Attachments

Washington, D.C.  
February 23, 1994

LAO PDR

FOREST MANAGEMENT AND CONSERVATION PROJECT

Estimated Costs and Financing Plan  
(US\$ million)

	Local	Foreign	Total
<u>Estimated Project Cost</u> <sup>a/</sup>			
Inventory and Planning	0.3	1.0	1.3
Management and Protection	2.1	4.5	6.6
Protected Areas	0.6	1.9	2.5
Human Resource Development	0.3	0.4	0.7
Technical Assistance	1.3	5.0	6.3
<u>Base Cost</u>	<u>4.7</u>	<u>12.8</u>	<u>17.5</u>
Physical contingencies	0.1	0.2	0.3
Price contingencies	<u>0.7</u>	<u>1.8</u>	<u>2.5</u>
<u>Total Project Cost</u>	<u>5.5</u>	<u>14.8</u>	<u>20.3</u>
<u>Financing Plan</u>			
Government	1.0	0.0	1.0
GET	1.2	3.8	5.0
FINNIDA	0.9	4.7	5.6
IDA	<u>2.4</u>	<u>6.3</u>	<u>8.7</u>
<u>Total</u>	<u>5.5</u>	<u>14.8</u>	<u>20.3</u>

<sup>a/</sup> Excluding taxes and duties.

LAO PDR

FOREST MANAGEMENT AND CONSERVATION PROJECT

Summary of Proposed Procurement Arrangements  
(US\$ million)

Project Element	Procurement Method				Total Costs
	ICB	LCB	Other	NIF	
1. Civil Works	-	1.2	4.1	-	5.3
IDA	-	(0.8)	(3.0)	-	(3.8)
GET	-	(0.4)	(1.0)	-	(1.4)
2. Vehicles and Equipment	3.9	0.6	-	0.4	4.9
IDA	(3.1)	(0.3)	-	-	(3.4)
GET	(0.8)	(0.3)	-	-	(1.1)
3. Fuel and Materials	0.6	0.4	-	0.5	1.5
IDA	(0.6)	(0.2)	-	-	(0.8)
GET	-	(0.2)	-	-	(0.2)
4. Salaries and Allowances	-	-	1.2	-	1.2
IDA	-	-	(0.7)	-	(0.7)
GET	-	-	(0.1)	-	(0.1)
5. Human Resource Development	-	-	0.6	-	0.6
GET	-	-	(0.6)	-	(0.6)
6. Technical Assistance	1.6	-	-	5.2	6.8
GET	(1.6)	-	-	-	(1.6)
TOTAL	6.1	2.2	5.9	6.1	20.3
IDA	(3.7)	(1.3)	(3.7)	-	(8.7)
GET	(2.4)	(0.9)	(1.7)	-	(5.0)

Other = Not subject to procurement, or by direct negotiation

NIF = Non IDA-financed

Figures in parentheses are the amounts financed by IDA

LAO PDR

FOREST MANAGEMENT AND CONSERVATION PROJECT

Disbursements

Category of Expenditure	<u>Amount</u> (US\$ million)	<u>% of Expenditures to</u> be Financed
1. Civil Works	3.0	100%
2. Vehicles and Equipment	3.0	100% of foreign expenditures for directly imported items, 100% of local expenditures (ex-factory cost) and 80% of local expenditures for other items procured locally.
3. Fuel and Materials	0.8	100% up to September 30, 1997, and 50% thereafter
4. Salaries and Allowances	0.7	100% up to September 30, 1997, and 50% thereafter
5. Human Resource Development	-	-
6. Technical Assistance	-	-
7. Unallocated	1.2	-
<u>TOTAL</u>	<u>8.7</u>	

Estimated IDA Disbursements

	<u>FY</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
		----- (US\$ million) -----				
IDA	Annual	0.4	1.3	2.9	1.7	2.4
	Cumulative	0.4	1.7	4.6	6.3	8.7

LAO PDR

FOREST MANAGEMENT AND CONSERVATION PROJECT

Timetable of Key Project Processing Events

- 
- (a) Time taken to prepare the project: 30 months
- (b) Prepared by: Government with IDA Assistance
- (c) First IDA mission: June 1990
- (d) Appraisal mission departure: 11/91
- (e) Negotiations: 02/93; 01/94
- (f) Planned date of effectiveness: 07/94
- (g) List of relevant PCRs and PPARs:

<u>Credit/Loan No.</u>	<u>Project</u>	<u>PCR/PPAR No. (Date)</u>
760-LA	Agricultural Rehabilitation and Development Project	PCR No. 7250 (May 16, 1988)
924-LA	Second Agricultural Rehabilitation and Development Project	PPAR NO. 90-1007 (July 27, 1990)
1021-LA	Third Agricultural Rehabilitation and Development Project	PCR No. 9858 (August 26, 1991)
1395-LA	Agricultural Production Support Project	PCR No. 9857 (August 22, 1991)

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This report is based on the findings of an IDA appraisal mission which visited Lao PDR in November 1991, and updated by IDA/FINNIDA post-appraisal missions in April and December 1992, respectively. The appraisal mission comprised Messrs. Y. Wong (Mission Leader), J. Blakeney (Forestry Specialist), and D. Hulse (Forest Conservation Specialist, Consultant). Messrs. E. Hurtig (Program Officer), H. Rissanen (Forestry Adviser), and T. Oksanen (Forestry Adviser) of FINNIDA, and Mr. R. Salter (Forest Conservation Specialist, Consultant) participated in the post-appraisal missions. Peer reviewers were Messrs. H. Wagner (AGRNR) and C. Rees (ENVLW). The document was cleared by Mrs. Pamela Cox (Chief, EA1AN) and Mr. C.E. Madavo (Director, EA1)

STATUS OF BANK GROUP OPERATIONS IN LAO PDR

A. STATEMENT OF DEVELOPMENT CREDIT /a  
(As of December 31, 1993)

Loan or Credit Number	Fiscal Year	Borrower	Purpose	Amount (US\$ million)/b (less cancellations)	
				IDA	Undisbursed
Eight IDA Credit credits fully disbursed				136.75	
Of which SALs, SECALs and Program Loans					
2037	1989	Lao PDR	Structural Adj. Credit	40.00	
2304	1992	Lao PDR	Structural Adj. Credit II	<u>40.00</u>	
				80.00	
1826	1987	Lao PDR	So. Prov. Electrification	25.80	1.33
1846	1988	Lao PDR	Southern Transport	14.10	1.66
1947	1989	Lao PDR	Industrial Credit I	10.00	3.52
2001	1989	Lao PDR	Polytechnic	3.50	3.17
2079	1990	Lao PDR	Upland Agric. Development	20.20	18.60
2101	1990	Lao PDR	Telecom II	24.50	15.63
2218	1991	Lao PDR	Highway Improvement	45.00	32.99
2425	1993	Lao PDR	Prov. Grid Integration	36.00	34.72
2488	1993	Lao PDR	Education Development	<u>19.00</u>	<u>18.92</u>
Total				334.85	130.55
Of which has been repaid				<u>1.83</u>	
Total Now Held by IDA				333.06	
Amount sold				0.0	
Total undisbursed				<u>130.55</u>	<u>130.55</u>

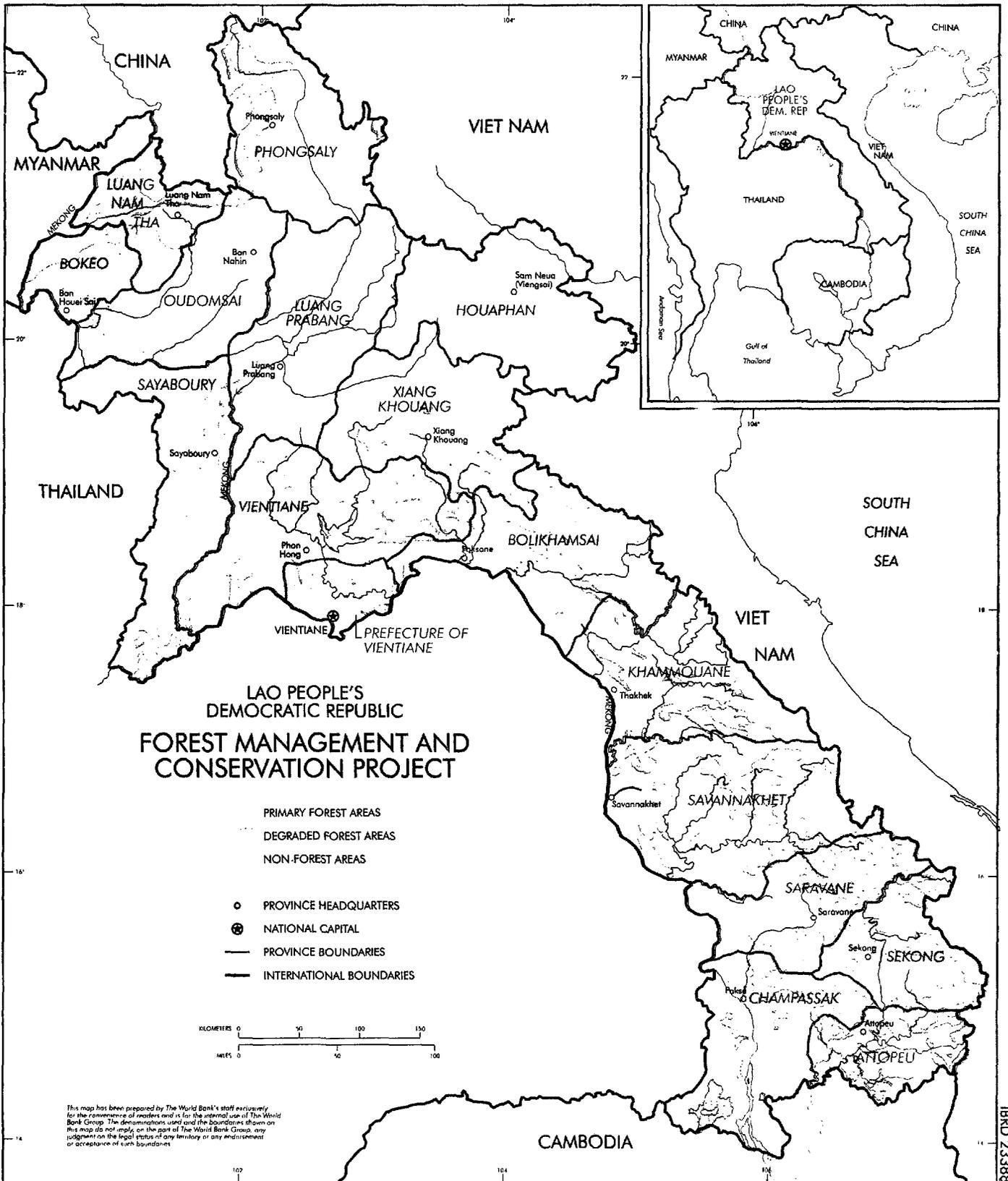
/a The status of the projects listed in Part A is described in a separate report on all IBRD/IDA-finished projects in execution, which is updated twice yearly and circulated to the Executive Directors on April 30 and October 31.

/b Principal amounts in US\$ equivalent at date of negotiations, and undisbursed amounts in equivalent are valued at exchange rate applicable on the date of this statement.

\* Indicates SAL/SECAL Loan and Credits.

B. STATEMENT OF IFC INVESTMENTS

None



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