STRUCTURED DIALOGUE 2: SCOPING THE FINANCING STRATEGY

Mapping and identifying financing policy areas

Led by the Ministry of Planning and Investment, with support from the United Nations in Lao PDR

November 2021

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Introduction: formulating the 9th NSEDP financing strategy

Background

Lao PDR is entering an **important stage of its national development**, with the 9th NSEDP now finalized, which will take the country to within five years of the 2030 deadline for the achievement of the SDGs and to the edge of graduation from Least Developed Country (LDC) status, planned in 2026. Simultaneously, **access to the necessary development finance to accelerate progress is becoming increasingly challenging**, with high levels of debt, revenue collection falling short of expectations, insufficient private sector contribution to development progress, declining ODA trends, and repeated shocks stretching coping capacity. Against this backdrop, **the Government of Lao PDR, with technical assistance from the United Nations, has been working to develop a practical and realistic financing strategy to ensure that development finance is available and accessible for the achievement of the 9th NSEDP.**

Importantly, the financing strategy does not intend to replace existing frameworks, policies, and projects to address financial constraints and needs for sustainable development. Its main added value lies in (1) the integrated and holistic approach, looking at all sources of finance, beyond the State Budget and ODA, in support of national development priorities, and (2) its underlying ways of working, bringing all relevant stakeholders together on the critical topic of financing for development.

The Ministry of Planning and Investment (MPI) leads this process, with technical and coordination support from the **UN Joint Programme on Financing Efficiency**, and regular involvement from key stakeholders: Ministry of Finance, Bank of Lao PDR, International Financial Institutions, and other development partners.

Overview of the process

The below diagram provides an overview of the entire process and timeline for the formulation of the 9th NSEDP financing strategy, which is tailored to the Lao PDR context, and aligned with the four phases of **the Integrated National Financing Framework (INFF)**.

The inception phase (phase 0) supported the dissemination of key concepts and methodologies and the development of appropriate coordination mechanisms. The diagnostics phase (phase 1) supported the development of robust diagnostics underpinning the financing strategy. The policy formulation phase (phase 2) focuses on the exploration and refinement of practical financing options, reflecting existing policies and projects, and aligned with the findings of the diagnostics undertaken. The finalization of the financing strategy is followed by its implementation, and the monitoring and evaluation of progress.

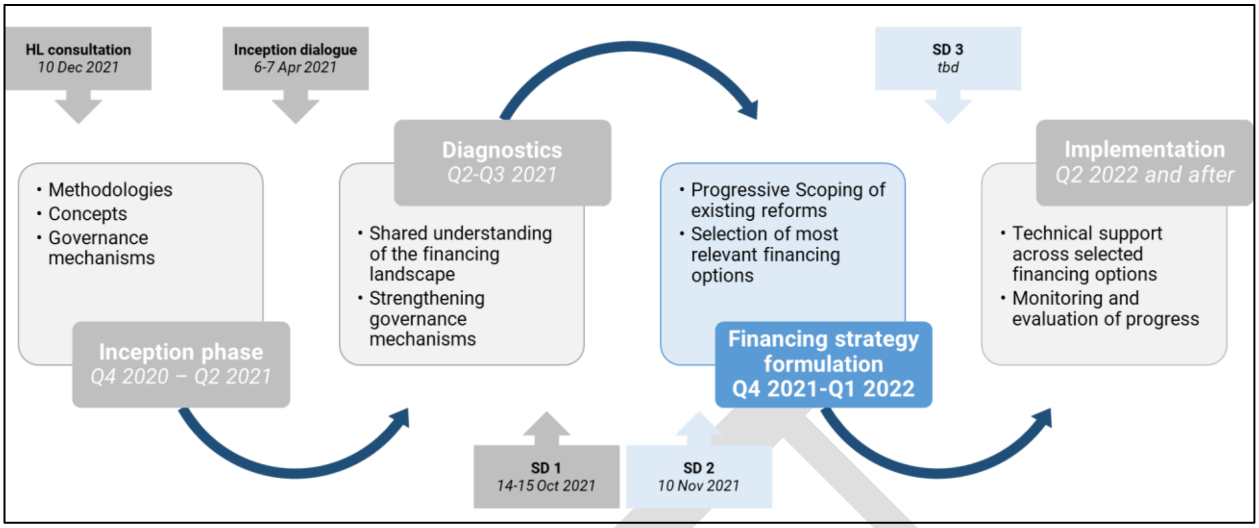

Figure 1 – Formulation of the 9th NSEDP Financing Strategy

This financing strategy formulation is inspired by the Integrated National Financing Framework (INFF) approach. The latter was developed in 2015 in the Third UN Conference on Financing for Development, endorsed by Member States, as a solution to two key problems:

1. **A missing link between planning and financing development**: most national plans lack strategies to finance development priorities, implying that well-consulted financing strategies are necessary to accompany national plans.
2. **A funding gap to achieve the Sustainable Development Goals (SDGs)** and national development priorities aligned to the SDGs, implying that all sources of finance and stakeholders can better contribute to the achievement of the SDGs.

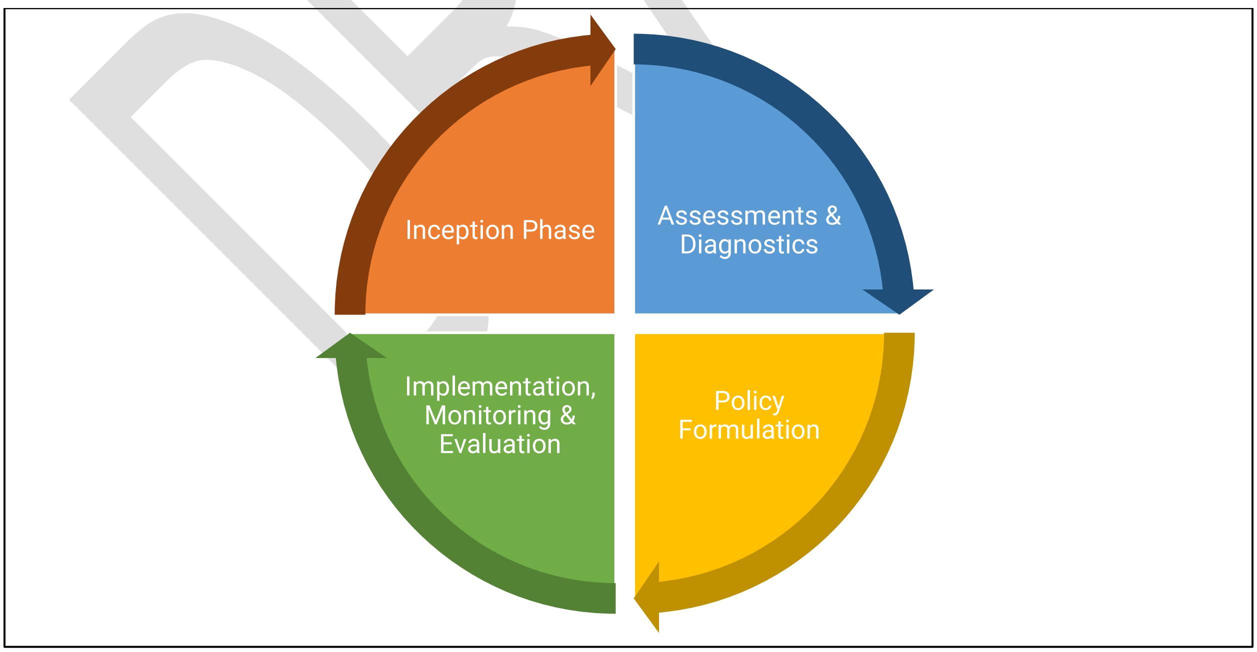

Figure 2 – The INFF process

The INFF progresses through an inception phase, robust diagnostics of financial needs and opportunities, policy formulation, and implementation (see above). It also specifies ways of working, which are summarised in the infographic below:

- **Robustness of diagnostic work**, which is primarily led by ministries and UN agencies, and appropriately consulted with relevant stakeholders.
- **Integrated and holistic approach to financing for development**: all sources of finance are indeed considered: domestic public finance, international public finance (ODA and other official flows), domestic private finance, and international private finance (FDI and remittances).
- **Inclusivity of the process**, engaging all relevant stakeholders across the entire financing landscape. The process follows a threefold progression with two feedback loops. Technical leads (e.g. DoP and UNDP) undertake preparatory technical work, which is then discussed in bilateral and group meetings with most relevant stakeholders (e.g. IFIs, MoF, BoL). These meetings support the first feedback loop, as most relevant stakeholders provide technical inputs, which are then integrated to the documentation. Once most relevant stakeholders agree with the key outcomes of the phase, a structured dialogue brings a larger set of actors together for brainstorming, discussion, and validation of the outcomes of the phase. The structured dialogues therefore support the second feedback loop where stakeholder inputs and validation helps to finalize the key outcomes of a given phase (see table 1).

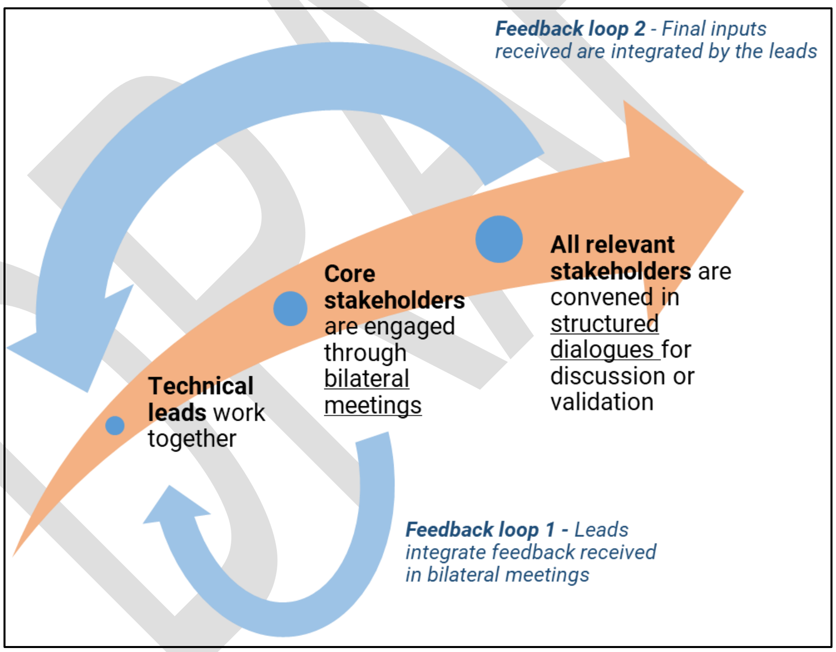

Figure 2 – Ways of working

Table 1 – Structured dialogues

	Dates	Topics addressed	Status and remarks
Inception dialogue	April 6 and 7, 2021	• Methodologies and concepts (e.g. INFF) • Coordination mechanisms	• Completed • Bilateral meetings took place between MPI and the UN to

			clarify methodologies and concepts
Structured dialogue 1: diagnostics	October 14 and 15, 2021	• Investment needs across the NSEDP • Resource envelope	• Completed • Bi and multilateral meetings took place with UN, MPI, MOF, BOL in advance of the dialogue
Structured dialogue 2: scoping policy options	November 10, 2021 (tentatively)	• Financing policy areas	• Ongoing • Consultation workshop with government on October 28th morning • Consultation meetings with World Bank, EU, IMF, ADB, UN on October 28th afternoon
Structured dialogue 3: finalizing policy options	1st Quarter 2022 (tentatively)	• Advanced set of financing policy options	•

The inception phase: agreeing processes, ways of working, and research designs

The objective of the inception phase is to **practically create the conditions for the successful delivery of a financing strategy: create coordination mechanisms, agree processes and timelines, and review methodologies and key concepts.**

An inception dialogue was held in Vang Vieng in April 2021 to discuss key methodologies and concepts. In particular, the core concept of the INFF, its holistic approach and fourfold process, as well as costing methodologies and challenges, were discussed. Prior to that event, a Technical Working Group to mobilise this large group of stakeholders was created by the Deputy Prime Minister upon request of the Deputy Minister of MPI early in the year. The UN Joint Programme's Steering Committee, with an extended board including MOFA and LSB, in addition to MPI, MOF and MOH, also met in July 2021 to coordinate UN's technical support and agree on a workplan for the completion of the financing strategy.

The diagnostics phase: understanding financing constraints and investment needs

This phase aimed to **provide all stakeholders with a set of key findings that would serve as the analytical backbone of the financing strategy.** In addition to providing robust analytics that all can agree with, this phase serves as another way to **consolidate collaborative ways of working.**

The diagnostics can be divided into two types of assessments which complement one another in painting a clear picture of the financing landscape for the achievement of the 9th NSEDP:

- **Investment needs, often referred to as "costing"**, have been estimated through 6 reviews of the literature corresponding to the 6 outcomes of the 9th NSEDP and a modelling of health costs. Due to difficulties encountered when attempting to conduct modelling of the costs of each outcome of the 9th NSEDP, a brief was developed to highlight gaps and challenges and potential solutions to ensure costing of policy priorities can take place in the future.

- **The resource envelope, often referred to as "financing",** is estimated through the Development Finance Assessment (DFA), which analyses four sources of finance according to the Addis Ababa Action Agenda, namely: State budget, domestic private finance, international private finance, and Official Development Assistance (ODA). Two additional briefs complement the picture painted by the DFA- on climate finance and on State borrowing.

Taken together, the resource envelope and investment needs provide the financing gap, or in other words, the resources missing to achieve national development priorities.

The main findings from these various assessments were presented and agreed with some necessary data updates at a first structured dialogue on October 14 and 15, in Vientiane Capital. Representatives from MPI, MoF, MoH, BoL, various line ministries, World Bank, IMF, EU, embassies, and the UN participated.

The financing strategy formulation phase

The formulation of the financing strategy is the most critical phase of the process. The two main objectives are to identify (1) the **most relevant financing policy options** and ensure that policies, instruments, and regulatory frameworks are coherent, sustainable and risk-informed, and (2) **needs and opportunities of technical assistance and capacity building** required to support its smooth implementation.

The financing strategy formulation (Phase 2) will span across Q4 2021 and Q1 2022 and includes three distinct steps (see figure 3):

- **A scoping step**, to map, identify, and discuss a draft list of financing policy areas, against the findings of the diagnostics carried out during. This step will be executed between October and November 2021. It included series of pre-consultations to discuss a preliminary scoping of financing policy areas and existing reforms and policies, and a second structured dialogue, organised ahead of the High-Level Round Table Meeting, to agree the outline of the financing strategy. A secondary objective is to reinforce coordination and ways of working between key stakeholders at the beginning of the policy formulation phase.
- **A policy formulation step**, to refine relevant policy options. This step includes more policy discussions in smaller clusters under each financing policy area, to define practical options. A more comprehensive structured dialogue ("structured dialogue 3", see above) should take place agree, at a technical level, to agree the financing strategy.
- **A validation step**, to integrate final technical-level feedback and progress towards the endorsement of the financing strategy at a high-level.

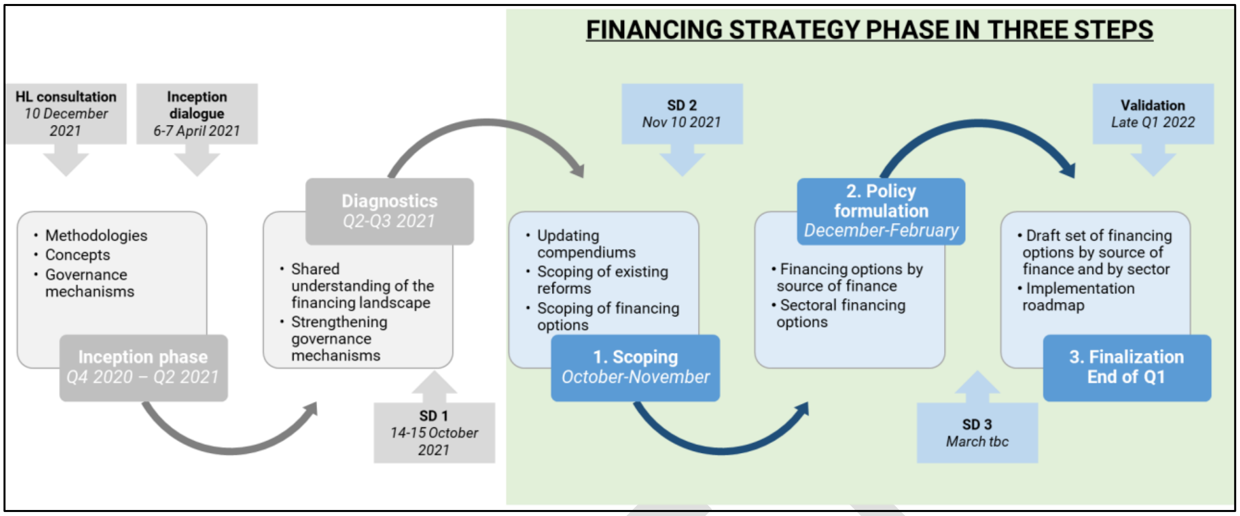

Figure 3 – Zoom on the policy formulation phase (in green)

Updated diagnostics following the first structured dialogue

As of early November 2021, all relevant stakeholders had reached a shared understanding on the financing constraints and investment needs. This section summarises the main findings of the diagnostics phase, has been updated with the feedback provided by participants, and specifies ways forward for later improvements of the quality of these diagnostics.

Financing national development priorities

Documents produced

- Development Finance Assessment (DFA)
1. *Mapping of public sector resources*
2. *Mapping of FDI resources*
3. *Mapping of ODA resources*
4. *Mapping of Domestic Private Investment and Other Resources*
- Lao Sovereign and SOE Bonds analysis
- Climate Finance Analysis Brief

A. The Development Finance Assessment (DFA)

- **Objectives**

The DFA guidance developed by UNDP provides extensive details on the role of this diagnostic tool and the Integrated National Financing Framework (INFF, see below). This approach, which is being undertaken in almost 50 countries, is essentially supporting the diagnostics phase. It is, in fact, the analytical backbone of the financing strategy. Investigating the trends of financing flows from the four different sources and their value in the economy – State budget, domestic private sector, international private sector, and Official Development Assistance (ODA) – the DFA provides policymakers with a set of key findings and directions for the financing strategy formulation.

- **Approach, scope, and limitations**

The INFF approach categorises development finance into the following: domestic public finance, international public finance, domestic private finance, and international private finance (see table below).

The **rationale for using the INFF approach** is threefold. First, adopting the INFF approach allows key policymakers to think holistically about development finance (four sources of finance, covering the entire economy), by simple criteria (domestic/international and public/private), to **identify the most comprehensive set of relevant policy solutions**. For example, policies to support FDI in green growth (e.g., fiscal incentives) are different from policies to support public investment (e.g., budget reallocations), ODA (e.g., strengthened coordination and strategic planning with development partners), or domestic private investment (e.g., loans for SMEs) in green growth. Second, and more practically, this international classification has been agreed at the 2015 UN Conference on Financing for Development, at the same time as the AAAA. Adopting **this approach to development finance will enable cross-country comparisons** with the many countries that undertook or are undertaking DFAs. Third, adopting this approach yields the above-mentioned benefits while **aligning closely with the current Government classification**, mentioned in the 9th NSEDP. The below comparison table shows the comparison of the financing flows defined in the INFF versus the 9th NESDP.

INFF	9th NSEDP
1. Domestic Public Finance	**1. State Budget**
• Tax revenue (direct, indirect) • Non-tax revenue • Government borrowing (loans, bonds) • Public enterprise revenues	• Ministerial and Provincial recurrent expenditure • Ministerial and Provincial capital expenditure • Government borrowings
2. Domestic Private Finance	**2. Domestic and foreign private investment**
• Private sector equity – *Gross Fixed Capital Formation* • Domestic borrowing • National NGOs, foundations, and faith-based organisations	• Private sector equity – *Gross Fixed Capital Formation* • International borrowing by private sector • Foreign Direct Investment (FDI) ○ *financial flows* ○ *associated commodity imports* • Foreign Portfolio investment (FPI) - *immaterial*
3. International Public Finance	**3. Official Development Assistance**
• ODA grants • ODA loans • Other official flows South-south cooperation	• ODA grants • ODA loans • Other official flows South-south cooperation
4. International Private Finance	**4. Other investments**
• Foreign Direct Investment (FDI) • Foreign Portfolio investment (FPI) - *immaterial* • International borrowing • Remittances • International NGOs, foundations, and faith-based organisations	• Remittances • Microfinance and Building Society (Financial Sector, not Banking Sector) net credits • Community contributions

Most limitations in the DFA involve data availability: certain key datasets were not accessible, such as detailed breakdown of allocations in the State budget and ODA flows.

The main findings, detailed below are considered robust to any foreseeable errors or omissions in the data updates. They have been shared and discussed bilaterally with key government and development partner agencies and validated with all stakeholders during the first structured dialogue.

- **Main findings**

Domestic public finance	1. Revenues need to significantly increase to support the achievement of 9th NSEDP policy priorities. 2. On the spending side, there are inconsistencies between current public allocations and the 9th NSEDP policy priorities that will need to be resolved.
International Public Finance	1. ODA heavily contributes to social sectors and should continue to be a driver of development progress throughout the 9th NSEDP. 2. The ODA Management Information System (ODA-MIS) Dashboard of MPI-DIC needs to be regularly and completely updated to inform Government on the scope, timing and focus of ODA investments.

	3. The Government of Lao PDR's absorptive capacities may be a constraint to ODA's contribution to development progress and delivery strategies need to consider this. 4. It will be important to take into consideration upcoming LDC graduation, which may impact country's ability access to ODA, and link the LDC Graduation Smooth Transition Strategy and the Financing Strategy.
International Private Finance	1. Significant policy reforms will be needed to direct future FDI in support of social sectors in the 9th NSEDP. 2. FDI inflows are likely to continue in line with regional economic growth prospects, underpinned by investments from China. 3. Reliance on a single source country without clear coordination and transparency mechanisms exposes Lao PDR to economic risks if that economy was disrupted, or the relationship was to change. 4. Foreign Portfolio Investment (FPI) fluctuated significantly over the 8th NSEDP 2016-2020. FPI is highly mobile and requires stable capital markets to be an effective source of development financing. FPI can include sale of equities in State-Owned Enterprises (SOEs), which would support Lao PDR policies for reform and subsequent divestment/ recapitalising of SOEs; and/ or State debt amortization. The sales of SOE assets also support debt servicing. 5. Remittances are primarily used for household consumption and can support the poverty alleviation and household well-being objectives of the 9th NSEDP. It was recognized that remittances are also supporting household consumption and that incentivising responsible and sustainable consumption in line with the 9th NESDP could be envisaged. 6. Further researching ways to eliminate illicit finance will be important as this would help to improve the quality of the business environment and increase the attractiveness of Lao PDR's economy.
Domestic Private Finance	1. Domestic private investment has significant potential as a source of development finance but is largely untapped. 2. Lao PDR investment promotion policies focus on the attraction, retention, and growth of foreign investors. 3. Efforts need to be made to stimulate domestic private investment through SME development strategies, business start-ups in Lao PDR and through more robust access to credit that stimulates investments. Credit policies to support domestic private investments will need to consider macroeconomic stabilization priorities. 4. A better proxy than Gross Fixed Capital Formation will be identified to measure the potential contributions of domestic private finance.

1. Domestic Public Finance	**15.7%**	1. **State Budget**	**15.7%**
1. Domestic Private Finance	**21.0%**	2. **Domestic and foreign private investment**	**27.1%**
3. International Public Finance	**3.1%**	3. **Official Development Assistance**	**3.1%**
4. International Private Finance	**7.5%**	4. **Other investments**	**1.4%**
TOTAL OF ALL INFF FINANCING TYPES	**47.30%**	**TOTAL OF ALL 9th NSEDP FINANCING TYPES**	**47.30%**

B. Sovereign and SOE bonds analysis (UNCDF)

- **Objectives**

The Lao PDR Bonds Review analyses the Lao PDR government issued sovereign and State-Owned Enterprise bonds as of 2020. The report provides a succinct background to the accumulated public debt stocks and examines the appetites of investors for Lao sovereign debt. It complements the analysis undertaken in the DFA on domestic public finance (State budget).

- **Approach, scope, and limitations**

The report was generated using sources from the Government and external datasets, including MOF, BOL, Thailand Bond Market Association, LSX, SGX, and rating agencies. However, data unavailability and inconsistencies between various sources are important limitations. A series of assumptions underpin the analysis, notably that Lao PDR will be able to meet its debt service repayments, that the 9th NSEDP will require extensive level of investments, and that further downgrading of the Lao PDR's rating is averted.

- **Main findings**

Finding 1: the impacts of bond servicing cannot be under-estimated when considering the issued bonds that are due to mature during the cycle of the 9th NSEDP. Over USD 1,700 million is due to be serviced by the government during the lifecycle of the 9th NSEDP (figure does not include unlisted bonds issued by the government and other SOEs besides EDL-Gen). With increased pressure on revenues, there is mounting pressure from debt servicing.

Finding 2: With Moody's August 2020 downgrade of Lao PDR credit rating to Caa2 from B3, the country now has the lowest credit rating in Asia without being in default. Analysis indicates that there is no market demand for a Caa2-rated Asian sovereign bonds in Thailand, Singapore, and Hong Kong, limiting the scope of borrowing as a potential source of development finance.

Finding 3: sentiment for new Lao PDR debt is weak, due to the current credit rating, and potential for default. Although debt is available, its high cost must be considered in the context of debt sustainability.

The data analysis presented in the report and the key findings are to be further validated by UNCDF and Ministry of Finance in the near future.

C. Climate finance (UNDESA)

- **Objectives**

The climate finance flows analysis examines the available climate finance in Lao PDR, the sources of funding and aims to identify the challenges and opportunities for capacity building interventions to scale climate finance mobilisation and implementation in Lao PDR. It complements the analysis undertaken in the DFA across all sources of finance through a sectoral lens.

- **Approach, scope, and limitations**

The Lao climate finance analysis relies on primary data through key stakeholder interviews and secondary data through a review of the literature. Without a unified climate finance database in the country, quantitative data came mostly from various international climate finance funding sources.

- **Main findings**

Finding 1: Climate finance in Lao PDR is mostly adaptation finance (71%) and majority of the climate finance mobilised are grants. This is consistent with general trends in Least Developed Countries while Middle Income Countries attract proportionately higher mitigation investments. With a high debt to GDP ratio, grants will continue to be a priority for climate finance mobilization for Lao PDR. Under such circumstances, it is necessary to explore innovative mechanisms to maximize grant utilization. One possible option is to consider leveraging grants to support private sector investment in Nationally Determined Contribution (NDC) priority sectors.

Finding 2: The review found that most climate change projects are financed by multilateral funds, UNFCCC, and non-UNFCCC, which were designed to support LDCs to shift towards low emissions and carbon resilient development. Funds which Lao PDR has not be able to access are often those that do not target LDCs and/or do not have an accessing channel outside host government countries.

Finding 3: Lao PDR so far relies on development partners that are multilateral funds' Accredited Entities (for GCF) or Implementing Entities (for AF) or Partner Agencies (GEF/LDCF). Some of the funds require the government to work with the funds' partners due to limited capacity of government entities to meet criteria set by the funds to access funds directly. Significant time and resources are required for proposal development and in making timely submissions to these global climate funds.

Finding 4: Monitoring and reporting on climate finance should be a priority area. A clear overview of climate finance flows and their use will allow a targeted resourcing and planning of activities towards the NDC.

Finding 5: There is a need to strengthen the government's capacity in mobilizing climate finance through long-term, systematic, strategic, and continuous interventions.

Costing national development priorities

Documents produced

- Costing the national plan: methodologies, challenges, and opportunities
- Six literature reviews covering 9th NSEDP outcomes investment needs

1. *Continuous quality, stable and sustainable economic growth achieved*
2. *Improved quality of human resources to meet development, research, capacity, science and technology needs, and create value-added production and services*
3. *Enhanced wellbeing of the people*
4. *Environmental protection enhanced, and disaster risks reduced*
5. *Engagement in regional and international cooperation and integration is enhanced with robust infrastructure and effective utilization of national potentials and geographic advantages*
6. *Public governance and administration are improved, and society is equal, fair, and protected by rule of law*

- Model Investment Case for the Health Sector (part 1 on investment needs)

A. How to cost national development priorities (UNDP-DOP)

- **Objectives**

At the outset, the objective was to estimate the financial cost of the achieving the outcomes and associated outputs of the 9th NSEDP (how much financial resources does it require to achieve national development priorities?). This would have allowed stakeholders to match a figure against the total value of available development finance (which is estimated in the DFA and other diagnostics undertaken), thereby identifying a financing gap, and then to use this to inform the formulation of the financing strategy.

However, due to data limitations and the timing of the finalization of the Monitoring and Evaluation Framework of the 9th NSEDP, MPI and supporting technical agencies acknowledged the difficulties of deriving sufficiently robust estimates and projections.

Therefore, to take forward the overall objective of informing the financing strategy, a decision was made to complement modelling efforts with literature reviews of global, regional and best practice estimates of costs across various sectors linked to the outcomes and associated outputs of the 9th NSEDP (see below).

To address the challenges encountered with the modelling efforts, and to develop national capacity on costing of national development priorities for the next planning cycle, this report now identifies (1) best practices and methodologies in costing national plans and sectoral plans (2) challenges and limitations in data and current capacity, and (3) practical solutions to improve capacity.

- **Approach, scope, and limitations**

The report is organised into three chapters. The first covers best practices and methodologies, drawing from the various methodologies agreed at the global level and implemented in other developing countries. The second identifies challenges and limitations, reflecting on the collaborative technical work done between UNDP and the Department of Planning (DoP) in the first half of 2021. The third chapter stems from matching of the gaps between the best practices and current available capacity and challenges, to identify practical ways forward.

- **Main findings**

Finding 1: most relevant techniques to cost national development plans were not applicable in Lao PDR, due to data availability issues. Calculations could only be derived from an incomplete set of development interventions, which did not comprehensively cover output and outcome priorities.

Finding 2: it is important to position the costing exercise carefully in the planning cycle, before and throughout the policy formulation, and build consensus on the importance of the costing exercise to ensure it informs prioritisation in resource allocation.

Finding 3: it is important to define, prior to the costing exercise, its scope (which priorities to cost, at the national and subnational levels, or both) and clarify key parameters (such as the definition of the costs).

Finding 4: reviewing programmes and historical costs can support improved accuracy and reliability of the costing exercise.

Finding 5: it is important to engage experts and stakeholders early in the costing exercise to collect relevant information, discuss findings, and identify synergies and trade-offs.

B. Investment needs across the 9th NSEDP (UNDP-DOP)

- ***Objectives***

Acknowledging the difficulties of modelling the financial costs of the 9th NSEDP, UNDP and the UNRCO, under guidance from MPI, decided in the summer 2021 to include specific reviews of the global, regional and national literature to estimate, quantitatively and qualitatively, investments needs across the six outcomes and associated outputs of the 9th NSEDP. This is intended to provide stakeholders with appropriate background information on the relative financial costs and the types of costs identified across the 9th NSEDP, to inform the formulation of the financing strategy and stimulate a conversation with relevant stakeholders on where funding is most needed, and why.

- **Approach, scope, and limitations**

<u>What we mean by "cost"</u>: the costing briefs review two elements. The first one is financial costs, also referred to as investment needs. Simply put, these are the monetary values of the costs of achieving a specific policy priority (e.g., achieving the country's mitigation targets will cost 2% of GDP). Implications are that these briefs <u>do not</u> review economic costs (e.g., climate change costs

X% of GDP of Lao PDR every year), opportunity costs, costs of inaction (e.g., not investing in climate change mitigation will cost X% of GDP in ten years), or socioeconomic costs (e.g., climate change leads to X number of additional deaths through extreme weather events).

What we mean by the nature of the "costs": this literature review allowed for comparison of costs across the 9th NSEDP. These papers identified outputs and sectors in which specific policy priorities were less financially costly because they involved, for instance, regulatory or legal changes, rather than, say, infrastructure construction. In addition, certain costs lend themselves, by nature, to be mostly born by a specific stakeholder. The public administration is for instance more engaged in governance reforms.

How we express "costs": where possible, briefs have expressed financial costs in % of GDP per year over the duration of the 9th NSEDP, for ease of comparison.

Sources: Lao-specific literature is richer in certain outcomes than others. A few studies have indeed been able to measure the investment needs of several sub-sectors, such as education or health, or the cost of climate change mitigation. However, for sectors with limited information on Lao PDR, global or regional estimates are used to provide an indicative estimate.

The methodology chosen – literature reviews – to estimate costs limits the scope and objectives of this exercise. In particular:

Global estimates: international or cross-country estimates of costs can be useful for providing a rough gauge of costs at the country level; however, they cannot be taken too precisely. The costs of achieving climate change priorities at the global scale differ from one country to another, due to climate risk vulnerability and exposure, pollution levels, etc, as well as the efficiency of implementation of spending.

Adding costs: it is both technically challenging given data availability and varying methodologies and would provide only unreliable information to add the costs of various sectors to derive a single figure for the cost of each outcome. First, for each outcome, there are both national and global estimates. Second, while it was attempted to express each figure in percentage of GDP, the exact denominator may not be the same.

Financing/investment gap vs. total investment/financing needs: the financing gap is the required additional amount of resources to achieve a given target, beyond the current trend levels of investment, while the total investment need integrates both current trend investments and additional investments required.

- **Main findings**

Outcome 1	• The direct financial costs to the state of achieving most outputs under outcome 1 relate to the costs of administrative reforms and systems enhancements and investments, as well as the role of State-Owned Enterprises. **Compared to the overall financial costs of the 9th NSEDP, the financial costs of many policy reforms are likely to be relatively modest, although implementation of SOE reforms can be costly, e.g., regarding the energy sector, and technically challenging.**

	• **Realising the objectives set out in Outcome 1 will require many investments beyond the State budget**, given the predominant role of private sector investment in driving growth. Possible measures to influence these investments could have additional financial implications for the state. • **More recent and accurate estimates of aggregate investment are required to model the historical relationship between investment and growth, and thereby approximate investment needs.** Specific challenges were identified in the use of Gross Fixed Capital Formation estimates (which have been discontinued).
Outcome 2	• For Lao PDR, sector plans for health and education, aligned to the 9th NSEDP, provide estimates of anticipated costs to implement initiatives designed to achieve priority outcomes. **Together, health and education investment needs make approximately 4.4% of GDP per year. This is well below global estimates of resources required to achieve the corresponding SDGs.** For countries in Asia-Pacific, on average 4.7% of GDP is estimated to need to be spend on health. The Education 2030 Framework for Action sets two key education finance benchmarks for Governments- to allocate 4-6% of GDP to education and/or to allocate 15-20% of public expenditure to education. • Expected financial costs of achieving the outputs related to skills and science & technology are significantly lower.
Outcome 3	• The assessment by UNFPA (detailed below) found that the scale-up of Sexual and Reproductive Health and Nutrition, Maternal, New-born, Adolescents, and Child Health interventions could cost an additional USD 109.0 million more than business as usual over 2021-2030. • While financial resources are important, most strategies for achieving gender equality require a mix of financial investments and political commitment coupled with changes in legislation, political and administrative rules, social attitudes, and norms. • **ILO has undertaken a costing of social protection, which found that the planned roll-out would cost around 0.1-0.15% of GDP annually.** • The costs related to UXOs will be USD 525 million over five years, or 105 million a year, which roughly amounts to 0.5% of GDP per year.
Outcome 4	• According to global estimates, green and resilient infrastructure investment could reach an average 4-5% of GDP for low and middle-income countries annually. In Lao PDR, this would represent around USD 1 billion a year. • Biodiversity protection costs amount, globally, to 0.3% of GDP per year, which applied to Lao PDR, would represent USD 60 million a year of investments in 2020. • **Lao PDR's 2021 Nationally Determined Contributions, aligned with the 9th NSEDP objectives, estimated that mitigation investment needs amount to USD 4.8 billion by 2030, which is around USD 500 million a year (around 2.5% GDP per year).** • **Outcome 4 also includes governance reforms, including legislative and regulatory changes and investments to promote a shift in production and consumption patterns to reduce environmental pollution, which may have more limited financial costs.** These call for catalytic public investments as well as measures to (1) internalize the costs of pollution and (2) unlock private sector finance and promoting private sector to support

	sustainability objectives. Technical assistance and knowledge transfers are crucial in support of dedicated financial resources, which mostly originate from the public sector (both the State budget and ODA).
Outcome 5	• **The costs of realizing the transformative priorities set out under this Outcome are amongst the most expensive in the 9th NSEDP. The likely cost of Outcome 5 alone far exceeds Government capital expenditure and ODA that is likely to be available.** However, the nature of these costs allows scope for greater involvement of private funds, and therefore the full cost is not expected to fall directly on the public budget. **Important to recognize that trade-offs exist between concessions to attract private investment, and the need for macroeconomic stabilization set out in Outcome 1.** • **Various global estimates suggest that total infrastructure investment needs for Lao PDR would be from USD 1 billion or 5% of 2020 GDP (lower World Bank estimate) to USD 2 billion or 10% of GDP (higher IMF estimate) per year over the course of the 9th NSEDP.**
Outcome 6	• **Priorities of outcome 6 are mostly concerned with improving public sector efficiency and effectiveness and therefore imply a heavy reliance on public sector investment** (domestic and international), as it has been the case historically. • Governance priorities, across the entire 9th NSEDP, were estimated, to require 6% of GDP of annual investments, which amount to USD 1.2 billion in 2020 in Lao PDR. • For low-income countries, achieving justice targets would cost USD 20 per person to provide access to basic justice services, while for middle-income countries the cost would increase to USD 64 per person. In Lao PDR, this would amount to USD 146-467 million a year, which represents around 0.7-2.5% of GDP. • Many policy priorities are considered to require relatively low investment needs as they consist in legislative and regulatory improvements but are technically challenging.

C. Model investment case for the health sector (UNFPA-MOH)

- **Objectives**

This workstream has two overarching objectives: identify most relevant interventions in Sexual and Reproductive Health (SRH) and Nutrition, Maternal, New-Born, Adolescents, and Child Health (NMNCAH) in Lao PDR, but also aims to set a model for evidence-based policymaking, when robust diagnostics, the costing estimates of health interventions and development returns, inform prioritization. More specifically, this project aims to estimate the costs, health impacts, and economic impacts of scaling up health interventions (the diagnostics), before developing a prioritization strategy, at both the national and provincial levels. As of September 2021, the diagnostics phase was completed and was set to inform the broader conversation on the financing strategy, specifically on the health financing front.

- **Approach, scope, and limitations**

The Investment Case aims to estimate the financial needs, health gains, economic benefits, and benefit-cost ratios of investing in a range of SRH and NMNCAH interventions. Although outside the scope of the investment case, costs presented in this brief also include Immunization, Non-communicable diseases (NCD) and Communicable diseases (CD) obtained directly from the costing of the Essential Health Services Package Report. The study used a mix of qualitative and quantitative methodologies to identify the costs of selected health interventions. Unit costs were calculated using the ingredients-based approach, while the sizescale of interventions were based on global literature. This assessment considers costs and benefits through to 2030, as the deadline for the SDGs, rather than only the 5 years of the 9th NSEDP.

A series of limitations must be considered:

<u>Data issues</u>: data for some health indicators, coverages, and economics benefits were only available nationally. Additionally, sizescale of interventions were based on global literature, while the actual impact of interventions will depend on the quality of care, which is difficult to measure.

<u>Health financing</u>: noting that external funding finances a significant amount of health program costs, a comprehensive fiscal space analysis for health is outside the scope of the Investment Case and this brief. It should be undertaken considering taking into account the DFA findings particularly in relation to trends in international public finance (ODA) support and recognizing the potential for leveraging international and domestic private sector investments for the health sector.

<u>COVID-19 impact</u>: the impacts are still uncertain on service coverage, and new evidence may ultimately change projections.

- **Main findings**

<u>Finding 1</u>: full scale-up of SRHNMNACH interventions could cost an additional USD 109.0 million more than business as usual (baseline scenario) over 2021-2030.

<u>Finding 2</u>: this would avert 1,044,000 unintended pregnancies, 286 maternal deaths, 6,866 child deaths and 5,070 stillbirths, reduce stunting prevalence children under 5 by 5.6 percentage points, and generate USD 661.5 million in economic benefits by 2030. **The benefit to cost ratio is of 6.0.**

<u>Finding 3</u>: to reach the sectoral targets, Family Planning, followed by Child Health and Maternal Health required most investments. **The greatest return on investment,** across SRHNMNACH interventions, **would result from investing in family planning**. A positive effect may be achieved through improved coverage of NMNMACH interventions alongside increased contraceptive prevalence, as reducing unintended pregnancies can cut demand for, and the cost of, other health services.

<u>Finding 4</u>: **investment in maternal health can have major benefits beyond simply reduced mortality, leading to lower morbidity and health complications associated with childbirth**. This can also decrease downstream costs associated with these health conditions and avert complications such as loss of income, although such costs can be difficult to quantify.

<u>Finding 5</u>: the priority should be ensuring access to family planning services in each province. Beyond family planning, scaling up vaccines, breastfeeding promotion and HIV interventions within each province would have the greatest impact. The highest returns came from investing in provinces that had the highest mortality rates.

The scope of the financing strategy and tentative financing policy areas

The scoping step of the policy formulation phase serves to ensure that there is **a successful transition between phase 1 (diagnostics) and phase 2 (policy formulation)** through:

- The mapping, identification, and discussion, between all relevant stakeholders, of **a draft list of financing policy areas against two key elements**: the established diagnostics of phase 1 and existing reforms and projects. Practically, this means that, by the end of this step, relevant stakeholders have agreed a draft outline for the financing strategy.
- **The strengthening of coordination and ways of working between key stakeholders at the beginning of the policy formulation phase**. It is important, as stakeholders are about to begin a critical policy formulation step, that all coordination mechanisms work, and all relevant stakeholders have the necessary forums to share their expertise and feedback in this integrated and consultative process considering all of development finance.

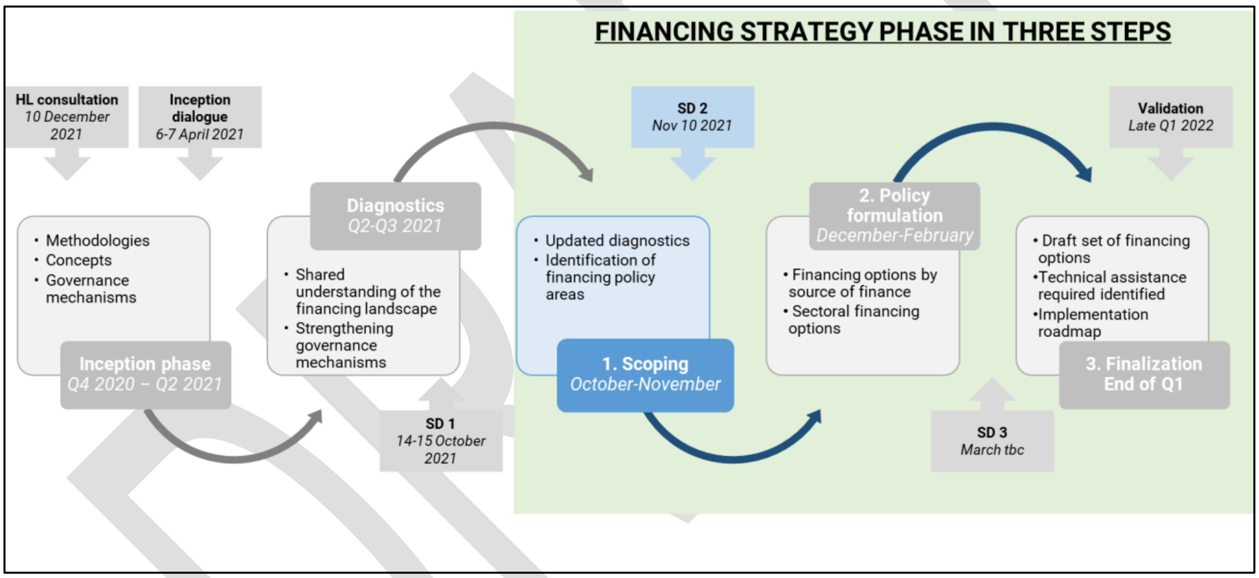

Figure 4 – Scoping step

A. Consultations undertaken to scope the financing strategy

The scoping step development was threefold:

1. **MPI, with technical support from the UN, mapped a preliminary list of financing policy areas** against the identified diagnostics presented earlier, or in other words, an outline for the financing strategy. At the first structured dialogue, a list of key findings were identified for each source of finance.

2. **MPI and the UN organised on October 28th series of meetings** to present this list and receive feedback. Government counterparts, including MPI, MoF, MoNRE, MoES, MoH, MoIC, and others, met in the morning. In the afternoon, World Bank, IMF, ADB, EU, and UN agencies

(WHO, UNFPA, UNCDF, UNODC) were consulted. The list of financing policy areas was updated to reflect feedback received that day.

3. **The second structured dialogue** will be organised on November 10th. It is expected that at the end of structured dialogue 2, key stakeholders should have agreed a preliminary list of financing policy areas for exploration against the established diagnostics of phase 1 and existing reforms and projects.

B. <u>Objectives and scope of the financing strategy</u>

The financing strategy's core objective is that national development priorities are appropriately financed and achieved within the expected timeframe of the 9th NSEDP. Informed by the shared understanding reached in the previous phase, this means that relevant stakeholders will aim to:

1. Identify most relevant financing policy areas and financing options and ensure that financing policies, instruments, and regulatory frameworks are coherent, sustainable, and risk-informed;
2. Identify opportunities to access technical assistance and capacity building support from development partners.

This set of agreed objectives has several implications:

The financing strategy is not meant to replace existing frameworks, policies, and projects: as mentioned in the introduction to this explanatory note, this means that the financing strategy builds on existing policies, projects, and initiatives led by critical stakeholders in financing for development to identify policy gaps and challenges and ensure coherence between the various financing policies, to achieve national development priorities within the expected timeframe.

The financing strategy aims to support the achievement of the 9th NSEDP: it looks at the financing policy areas and options achievable and realistic for the achievement of the 9th NSEDP policy priorities. 2021 is already year 1 of implementation of the 9th NSEDP, which leaves, with a likely finalization of the strategy mid-2022, around 3 years and a half of implementation.

This implies that the financing strategy should be composed of practical and quickly implementable financing options: considering that the objective of this financing strategy is to ensure that the 9th NSEDP policy priorities are achieved, it is crucial to focus efforts on rapidly implementable solutions which do not derail long-term financial sustainability plans, but allow for an increase in the total amount of resources available and/or a better use of existing resources.

The financing strategy is a collective effort: relevant stakeholders have been initially mobilized through a technical working group, in advance of the inception dialogue held in Vang Vieng in April 2021. These included most relevant ministries (such as MoF and BoL) as well as international financial institutions (such as the World Bank, ADB) and key development partners (EU, UN Agencies). Nonetheless, considering the holistic approach taken by MPI and the UN in formulating this financing strategy, there is a need to make sure that all relevant stakeholders are included. Much progress has been made to include new line ministries (such as MoES, MoH, MoNRE, MoIC) and new departments from core ministries (such as MoF's tax department). This effort must continue and considering the growing importance taken by private finance in the financing strategy, representation from the private sector, through the chambers of commerce for instance, will be necessary to ensure that all inputs are considered and policies recommended appropriate and implementable.

The financing strategy will look at how can all sources of finance contribute to national development priorities: the formulation of financing options will continue to be done under the INFF approach and its key characteristics of holism, integration, and national ownership. Holism suggests that all sources of finance – domestic public, international public, domestic private, and international private – are considered. These four sources of finance will be the first four chapters of the financing strategy.

Three additional elements have been discussed and received positive feedback with key stakeholders:

The financing strategy should try to prioritise, within practical and implementable solutions, those that require the most immediate focus: because this financing strategy attempts to be comprehensive and cover all sources of finance, many policy areas and policy options will be discussed. As mentioned, this financing strategy should only be composed of practical and implementable options with the aim of supporting the 9th NSEDP achievement. Nonetheless, by the end of Q1 2022, it will be critical to have an even more refined list of options, ranked from most urgent and most able to unlock development finance in support of the 9th NSEDP, to least.

Some key sectors require more specific, in-depth look: it has been recognized by relevant stakeholders that specific sectors, namely health, education, and environmental management and climate change, required more specific sectoral insights. This is due to the acknowledgment that they face specific challenges that need to be addressed (e.g. accessing climate funds requires specific capacity building of national staff) and that the achievement of human capital and environmental priorities in the 9th NSEDP are critical for the achievement of all national development priorities. It is suggested that the financing strategy could have one specific chapter covering all key sectors.

Some challenges are cross-cutting, such as data, information management and coordination: even if the financing strategy would be primarily structured against the four sources of finance, key issues require consideration by all stakeholders, such as data (e.g. tracking financing flows into the economy), coordination (e.g. how to maintain, in the implementation phase, a sensible coordination of relevant stakeholders across the entire development finance landscape?) and information management (e.g. how does the data held by ministry X inform policy making in ministry Y?). These should be covered in a final chapter.

C. Tentative financing policy areas

Financing policy areas is the expression given to the topics which have been identified by stakeholders as needing more attention in the policy formulation phase. Under these financing policy areas, with the objective to achieve national development priorities set out for 2025, stakeholders will have to identify financing options that are practical and implementable in the short-run to ensure increased access and availability of development finance or better use of existing resources.

In line with the process that was followed to identify financing policy areas, the below table summarises the potential outline of the financing strategy. It identifies tentative financing policy areas, with, for each, the related diagnostics and a brief explanation of the rationales behind its potential inclusion. The information contained in this table is the result of almost a year of work, integrating diagnostics identified through desk research, bilateral and multilateral meetings and a structured dialogue, and since then conversations held on October 28th with all relevant stakeholders, and prior and after that exercise, between MPI and the UN. The diagnostics are simplified for convenience: a longer version is accessible in the diagnostics section of this note.

Financing policy areas	Related diagnostics	Rationale for inclusion
1. Domestic Public Finance		
Urgently increase domestic revenue mobilization	▪ Revenues need to increase ▪ Scope of further borrowing is constrained	Finding ways to urgently increase the revenue to GDP ratio (in particular, the tax to GDP ratio) will increase fiscal space and public investment possibilities in priority sectors. In addition, the 9th NSEDP highlights budget balance as a key priority to achieve within the cycle. **Mining and energy royalties (non-tax revenues) do not represent sustainable alternatives as they do not align with national priorities and international commitments on environmental management and climate change.** Changing fiscal policy is usually a long-term endeavour, so practical and implementable solutions will need to be identified, on tax management, tax administration reform, and non-tax revenues management.

Improve expenditure management: align public investment management with the 9th NSEDP priorities and strengthening planning and budgeting functions integration	▪ Inconsistencies between current allocations and the NSEDP policy priorities	Investments during the 9th NSEDP need to be prioritized in specific sectors (human capital, environment) and on specific activities that are currently under-resourced in line with the COVID-19 recovery strategy that the government and development partners are working on Strengthening relationships between the planning and financing functions through improved information management, coordination mechanisms, and specific tools (IFMIS, budget tagging) will support more evidence-based and consulted budget allocation. Social sectors have identified challenges with budget allocations, currently below expectations. In addition, the 9th NSEDP highlights budget balance as a key priority to achieve within the cycle.
Debt and borrowing management, including for SOEs	▪ Scope of further borrowing is constrained ▪ Inconsistencies between allocations and policy priorities ▪ FPI can help with SOE management	Debt servicing has become an important share of the budget. Further borrowing is constrained but could be explored through specific bonds. Facilitate private sector participation for some SOEs and full divestment of ownership to private sector for selected SOEs and strengthen governance of SOEs to promote efficiency and effectiveness are identified as 9th NSEDP policy priorities.
	2. International Public Finance	
Improve predictability, efficiency and effectiveness of ODA	▪ ODA contributes heavily to social sectors ▪ Better data on ODA will support more informed ODA management ▪ Absorptive capacity constrains ODA's efficiency and effectiveness	ODA has been identified as a key contributor to sustainable development. Nonetheless, there are possibilities to keep improving its efficiency and effectiveness through better coordination and strategic prioritization of sectors to invest in, based on development partners' comparative advantages. Taking into consideration absorption capacity in this prioritization will ensure that development results are sustainable. Government has also stressed that improving predictability of ODA trends and areas of focus would help with strategic prioritization.
Take advantage of LDC status and managing impacts from LDC Graduation on ODA	▪ LDC Graduation potential impacts on ODA need to be managed	Lao PDR will be a LDC until the end of the 9th NSEDP, which suggests taking advantage of concessional LDC-specific finance, while preparing for the next cycle, and managing potential negative trends in ODA due to graduation.
	3. Domestic Private Finance	
Improve the business environment to unlock private finance for	▪ Domestic private finance can be an important source of development	Realising the potential importance of the domestic private sector in supporting 9th NSEDP policy priorities, updating legislation and regulations, could give a boost to investments in key sectors.

green and social sectors	finance but is largely untapped	Mobilising private finance in support of national development is a long-term process but identifying practical options in the short-term has been identified as not only unlocking financial resources but also supporting 9th NSEDP policy priorities regarding private sector development, growth, and poverty alleviation.
Support a sustainable private financial sector to stimulate the economy	▪ Credit policies need to consider macroeconomic stabilization needs	The role of the financial sector has been identified as critical, but there are concerns with macroeconomic stabilisation and the sustainability of the financial sector. Identifying short-term financial policies that could support key investments in important sectors while ensuring the long-term sustainability and stability of the financial sector will be critical.
4. International Private Finance		
Diversify FDI countries of origin and improve their contributions to key sectors	▪ Need to redirect FDI towards social sectors ▪ Need to diversify countries of origin	Realisation of FDI's limited contribution to NSEDP policy priorities, and in particular limited contribution to social sectors and the green economy, suggests that policy changes are necessary. Improved regulations and legislation could help to stimulate investments in key sectors.
Manage SEZs to balance benefits of attractiveness and fiscal costs	▪ Revenues need to increase ▪ Need to redirect FDI towards social sectors ▪ Need to diversify countries of origin	SEZs generate attractiveness for Lao PDR but need, in order to better support the 9th NSEDP policy priorities, ensure that FDI inflows lead to more inclusive growth creating employment for Lao citizens. In addition, SEZs generate fiscal costs through tax exemptions. Reviewing SEZs management, including tax exemptions, could lead to identifying a more sensible balance, aligned with the 9th NSEDP objective, between revenue growth imperative, public investment in critical sectors, and attractiveness for foreign investors.
Tackling illicit finance to improve Lao PDR's international profile	▪ Tackling illicit finance can improve the business environment and attractiveness	Illicit finance was identified as an area that requires more attention at the first structured dialogue. With Lao PDR's hope to maintain FDI flows on the same upward trend, tackling illicit finance could improve Lao PDR's investor profile, reassuring investors about the credibility of Lao PDR as an investment destination.
Facilitate remittance transfers to support poverty alleviation and sustainable consumption	▪ Remittances play a vital role for communities	Remittances were identified as critical flows for Lao PDR's poverty reduction objectives. With the possible recovery period, suggesting easier travel and a rebound of remittances, the improvement ofregulations and legislation to facilitate transfers and encouraging consumption in health, education, and green growth should be explored.
5. Sectoral finance		
Improve the sustainability of education and health financing	▪ State budget allocations to key sectors are below expactations	Social sectors have repeatedly identified budget allocation as being too low to ensure that national development priorities are achieved. Identifying opportunities to achieve national development

	▪ Importance of ODA in social sectors	priorities within the next cycle, while improving the sustainability of health and education financing, considering the emphasis of the 9th NSEDP on human capital development, will be critical.
Facilitating investments in green and low-carbon development	▪ Green and climate finance largely untapped despite importance in 9th NSEDP priorities	Studies have identified that Lao PDR does not access climate and green finance as much as it could, and that the potential is relatively untapped. Overcoming certain challenges linked to national capacity to access climate funds, or exploring opportunities to finance biodiversity, environmental management and climate adaptation through conventional and innovative finance will be explored.
6. Cross-cutting challenges		
Resolving key data gaps for the implementation and monitoring and evaluation of the financing strategy	▪ Data issues have been identified across all sources of finance and across all financing policy areas	The diagnostics phase highlighted several data gaps that need to be improved to ensure the financing strategy is based on solid analytical grounds and to prepare for a successful implementation (e.g. ODA data, private sector flows, forecasts).
Strengthening coordination and information-sharing between all relevant stakeholders, including the private sector	▪ Coordination and information-sharing issues identified across all sources of finance and across all relevant stakeholders	The diagnostics phase and the pre-consultations revealed that key adjustments in coordination mechanisms and information-sharing tools could help to improve budget allocations and facilitate, in the short-run, more informed, evidence-based decision-making.

Annex 1 – Questions and Answers

The context

A. What is financing for development and why should we care?

Financing for development is about ensuring the financial resources to support collective ambitions for a more resilient, inclusive, equitable and sustainable future.

Financing for Development focuses on the mobilisation and efficient use of resources in support of the Sustainable Development Goals (SDGs), and is itself an important focus area of Goal 17 on Partnerships for Sustainable Development. Investments in many critical areas are needed, to ensure that the world, and individual Member States, achieve the 2030 Agenda for Sustainable Development adopted in 2015.

As of mid- 2021, as noted the 2021 Economic and Social Council Forum on Financing Development, the situation is critical: the pandemic aggravated a chronic underfinancing of the SDGs, so that several multi-generational objectives, such as the protection of our planet, the elimination of poverty and hunger, and necessary improvements in people's wellbeing, may not be achieved.

B. How has the Covid-19 pandemic affected development financing?

COVID-19 has impacted public finances, with additional health and recovery expenditures and a drop in revenues; the private sector, through lockdowns and disruptions to trade; and development partners, with declining ODA trends.

The pandemic has caused immense suffering across the planet, in the region, and in Lao PDR. The range of impacts on people's wellbeing is wide, with deaths, changes to fertility patterns, long-lasting physical and mental and psychosocial health consequences, especially for most vulnerable groups, disrupted access to essential health services, and weakened social protection systems. On the socioeconomic front, preventative lockdowns, and disruptions to trade and travel, albeit necessary to mitigate the pandemic, have caused unprecedented rises in poverty rates and increased vulnerabilities. At a time where reprioritization of and increases in development spending to cushion these shocks and progressively recover from the pandemic, while progressing towards the SDGs is imperative, the global financial envelope in support of these goals has shrunk.

The financing gap is increasing, with a public sector needing to spend more while managing a decrease in tax revenues, severe stresses in the private sector, and declining trends in Official Development Assistance (ODA) and people having less money to spend. COVID-19 has negatively affected our chances to achieve development priorities.

Albeit privately channelled, remittances are also a form of development financing supporting economic activity, stimulating production and trade, and in turn generates both formal and informal employment. Due to COVID-19 many migrant workers and their families in Lao PDR, responsible for an estimated 1-2% of GDP annually in remittances pre-pandemic, have been impacted by the pandemic. Remittances drastically decreased in 2020 (-0.7% of GDP).

C. What is the United Nations' value added in financing for development and the Integrated National Financing Framework (INFF)?

The United Nations provides clarity of purpose with the Sustainable Development Goals (SDGs) as a common framework, while supporting a holistic and integrated approach to finance progress towards its objectives, engaging all sources of finance including both public and private, domestic, and international, and all relevant stakeholders.

As the United Nations Secretary General sets out in the Strategy for Financing the 2030 Agenda for Sustainable Development, the 2030 Agenda for Sustainable Development aims at a fundamental transformation of society, and its patterns of production and consumption. The United Nations has therefore defined an ambitious common horizon for all relevant stakeholders, to which all national and sector-specific strategies align. In addition, by providing a narrative on the role of finance in support of this commonly agreed set of objectives, the UN offers a holistic and integrated approach, called the Integrated National Financing Framework (INFF), which considers:

- All four sources of finance (public/private and domestic/international) and how they can best contribute to sustainable development with a substantive push to engage the private sector.
- A wide variety of tools: tax reforms, including to internalize the true costs of production and consumption, resource mobilization, improvements in the business environment, regulatory and legal changes to incentivise investments in specific sectors and address illicit financial flows and corruption.
- Additional necessary improvements in data quality, transparency, statistics, and capacity building of key relevant stakeholders.

The United Nations, using its mandate as a convenor and facilitator of systemic change, is, moreover, well placed to support the technical and political dialogues required to engage all in a meaningful shift towards financial flows in support of the SDGs.

A Financing Strategy for Lao PDR

A. Why developing a financing strategy in support of the national development plan in Lao PDR?

Without a clear, practical, and realistic plan to urgently address financial constraints, and match resources with ambitions, engaging all relevant partners and sectors, Lao PDR will struggle to achieve the national development priorities contained in the 9th National Socio-economic Development Plan and the SDGs.

Lao PDR is at a crossroad. The 9th National Socio-economic Development Plan (9th NSEDP) provides a set of ambitious and coherent outcomes and outputs aligned with the SDGs. Now finalized, this framework will guide the country within five years of the 2030 deadline of the Global

Agenda for Sustainable Development and to the edge of the anticipated graduation from Least Developed Country (LDC) status in 2026.

With the additional investments required to yield a demographic dividend, address climate change and environmental degradation, and recover from the COVID-19 pandemic, the national agenda is filled with multigenerational and transformational priorities. Simultaneously, access and availability of development finance are constrained, with high levels of debt, revenue collection falling short of expectations, and limited contributions from the private sector to national development priorities.

It is urgent that current financial difficulties threatening the realization of national objectives are addressed through a strategy highlighting necessary policy directions and decisions. Such exercise should ensure that the country optimises available development finance use and mobilises untapped sources whilst addressing sustainably the challenges to a more stable macro-economy. This is a precondition to progress towards sustainability, prosperity, and wellbeing for all.

B. How will Lao PDR formulate a financing strategy? Who participates?

The formulation of a financing strategy is as much a technical as a governance exercise: policy choices to support the sustainable financing of development objectives must rest on evidence-based, technically accurate, and reliable diagnostics, and be participatory, engaging all relevant stakeholders in meaningful policy dialogues.

The formulation of a financing strategy is based on three main steps and is expected to near finalization at the end of 2021, after a year of work:

- The inception phase is to present the INFF approach (see above): this took place at a workshop early April in Vang Vieng.
- The second phase aims to get consensus on the current financing landscape and investment needs to achieve development priorities. This diagnostic phase involves technical work and dialogues, and agreement on main conclusions that will be the backbone of the financing strategy development.
- The third phase involves series of strategic dialogues to interpret and translate initial diagnostics into practical and realistic options.

The formulation is, throughout its two phases, inclusive and participatory, and meant to ensure that all relevant stakeholders can provide inputs and feedback to the policy recommendations that will be made. A dedicated Technical Working Group was created by the Deputy Prime Minister upon recommendation from the Vice-Minister of Planning and Investment earlier in 2021 to facilitate stakeholder mobilisation.

As of late August 2021, the diagnostic phase was nearing finalization and a dedicated structured dialogue to validate the main assessments was to be organised in September. The financing strategy is led by the Ministry of Planning and Investment, namely the Department of Planning, with support from and consultation with the Ministry of Finance, Bank of Lao PDR, and relevant line ministries, as well as from the United Nations (through a dedicated Joint Programme, see below) and International Financial Institutions (IFIs) and other partners. Once the financing strategy is formulated, assessing the success of its implementation is crucial to inform budget decisions: this is the monitoring and evaluation phase.

C. What are the main challenges in formulating a financing strategy?

Challenges are threefold: technical, as the availability of quality data is limited, and limits the reach and robustness of diagnostics, and political and institutional, considering the difficulties associated with convening stakeholders. Fortunately, these difficulties can be overcome through active participation of all relevant stakeholders, clear communications, and a political push from the Government.

The formulation of a holistic financing strategy, considering all sources of financial contributions to sustainable development, is full of challenges. Credibility, technical accuracy, political support, and communications are critical in a process that is both political and technical, and therefore highly demanding. Technically, challenges arise mostly during the diagnostics phase (see above). Data limitations and difficulties in interpreting economic and financial data, as well as the uncertainties of budget and macroeconomic forecasts at a very uncertain time, must lead analysts to adopt careful research methodologies, and clearly highlight assumptions (e.g., there can be several GDP growth assumptions when forecasting) and limitations (e.g., part of the State budget is not publicly available). It is crucial that diagnostics aiming to paint a clear picture of the financial constraints of Lao PDR are undertaken with as much rigour as possible to generate maximum credibility. The formulation of a financing strategy is as much, if not more, about policy decisions as it is a technical exercise. Indeed, as mentioned above, identifying policy choices across four different sources of finance implies the active participation of a wide variety of stakeholders: Government, bilateral partners, traditional development partners, the private sector, including the financial sector and to gain the trust of society, also the need for transparency in the exercise.

In this context, the clarity of the process, including the sequencing of the various dialogues, is important. Political support from the highest level of decision-makers in the country to put financing for development high on the national agenda can improve visibility and create momentum. Moreover, adequate communications, capable to simplify technical content into easily digestible information and to reach various audiences, the timely circulation of information, and the quality of translation and interpretation during dialogues too help mitigate the difficulties of convening and generating meaningful discussions between different stakeholders are all vital to the process.

The UN Joint Programme on Financing Efficiency

A. What is the role of the UN Joint Programme on Financing Efficiency?

The UN Joint Programme provides technical and coordination support to the Lao PDR Government across the three main stages of the Integrated National Financing Framework (INFF) implementation: diagnostics of the country’s financial constraints, formulation of credible and realistic policy options, and monitoring and evaluation of progress towards the implementation of a holistic and ambitious approach to development finance.

The United Nations Joint Programme on Efficiency and Optimization of Lao PDR's Public budget to finance the SDGs through the National Plan works to strengthen the national architecture for managing and allocating development finance to support more efficient and effective use of available resources, and mobilisation of other sources of finance in support of national priorities and the 2030 Agenda.
As the main vehicle to support the formulation of a financing strategy for the 9th NSEDP, it is coordinated by the Ministry of Planning Investment, Department for International Cooperation (DIC), and the United Nations Resident Coordinator's Office (UNRCO), and involves the Ministries of Finance (MoF), Planning and Investment (MPI), and Health (MoH), as well as UNFPA, UNCDF, and UNDP, which is the technical lead entity from the UN country team.
Three main workstreams are progressing in parallel and align with the three main stages of the INFF development, mainstreaming governance and coordination support throughout. Assessments and diagnostics in support of the financing strategy are primarily led by the Department of Planning of MPI, with technical support from UNDP, through the identification of all resources available to fund development, and an assessment of the investment needs to reach shared development objectives (see below). The financing strategy formulation is also mainly supported by UNDP, which provides technical and coordination support to MPI to develop a practical financing strategy for the 9th NSEDP, through series of dialogues with relevant stakeholders. UNFPA, under MoH's strategic guidance, and considering its specific mandate and expertise in the health sector, contributes to assessments, costing health sector priorities, and policy formulation, identifying health interventions with the highest development returns in a resource-constrained environment. As to the monitoring and review of the implementation of the financing strategy, this is supported, under strategic guidance from MoF, by UNCDF, which uses its expertise to develop an innovative methodology to track expenditures against development priorities.

B. What is a Development Finance Assessment (DFA)?

The DFA is the analytical backbone of the financing strategy: it maps Lao PDR's resources envelope and seeks to understand to what extent and how each financial source has contributed and can contribute to sustainable development.

The DFA guidance developed by UNDP provides extensive details on the role of this diagnostic tool and its position in the INFF cycle. This instrument, which has been completed or is ongoing in almost 50 countries, is essentially supporting the diagnostics phase. It is, in fact, the analytical backbone of the financing strategy. Investigating the contributions of the four different sources of finance in the economy – State budget, domestic private sector, international private sector, and Official Development Assistance (ODA) – the DFA will provide policymakers with a set of key findings and directions during the financing strategy formulation.

The DFA is however, not only an analytical piece. In Lao PDR and elsewhere, it is also a tool through which the coordination of the most relevant stakeholders first takes place and can facilitate the emergence of a consensus on the panorama of development finance. Active participation of all relevant parties early in the process, including during the most technical phase of the process, is crucial. The DFA main findings, led by MPI with the support of UNDP, will be presented at a first structured dialogue, which should happen in September 2021.

C. Why focusing on the health sector in a Joint Programme on financing for development?

The model investment case for the health sector not only supports the identification of most relevant interventions in a crucial sector for Lao PDR, but also ambitions to set a standard in evidence-based policymaking, when robust diagnostics, the costing estimates of health interventions and development returns, inform prioritization.

This workstream, led by MoH with UNFPA's support, has two parallel objectives: identify most relevant and efficient interventions in the health sector, and set a precedent in terms of evidence-based policymaking. The selection of the health sector is based on the role of improvements of development outcomes in the health sector in achieving national development priorities (considering the 9th NSEDP prioritization of investments in human capital), the 2030 Agenda for Sustainable Development, and LDC Graduation. with regards to the health dimension, the project has two objectives, at both the national and provincial levels, which are to (1) estimate the costs, health impacts, and economics impacts of scaling up health interventions, and (2) develop a prioritization strategy. Its role in setting standards in terms of evidence-based policymaking is equally important. The project, focusing on a specific sector, is indeed structured along the same phases identified in the INFF, with an initial diagnostics phase, in which health interventions are costed and development returns measured, followed by a policy formulation phase, in which prioritization of interventions is developed. It is hoped that the lessons learnt from this project will support the many ongoing reforms, supported by the development community, of Public Financial Management (PFM), and specifically public investment management, to ensure the more efficient and targeted use of available development finance.

D. What are the objectives of the tagging of the national budget with national priorities and the SDGs?

Setting up systems to monitor and evaluate the progress of the implementation of the financing strategy is essential: ensuring that we know what investments contribute to, in a resource-constrained environment, will help to reorient budget allocation and strengthen the linkages between planning and financing.

Few countries have worked on strengthening the link between budget processes and SDGs and national priorities. In Asia, Lao PDR could be a pioneer. The workstream led by the MOF and supported by UNCDF is located at the tail end of the INFF cycle, as it builds monitoring and evaluation systems. The development of a specific methodology to categorise public investments and of a review of financial flows, against the national development priorities and the SDG framework, will help us understand where and for what resources are used, and strengthen the accountability of Government to its citizens. The encoding of these frameworks directly within the national budget, through the Chart of Accounts and the Integrated Financial Management Information System, ensures that economic policymakers can plan budget allocation being aware of which sectors and priority areas are underfunded. SDG-tagging of the budget will thus facilitate the formulation of an optimized public sector budget. The tool will help inform decision-makers and support coordination of ministries and partners against a unique framework. This new system is also meant to measure the success of the implementation financing strategy, specifically on domestic public resources.