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Laos: a state coordinated frontier economy

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Abstract

This paper assesses the current variety of capitalism in Laos using Hall and Soskice's (2001) comparative approach and the emerging body of knowledge on Varieties of Asian Capitalism. In addition to a systematic discussion of the traditional capitalist elements proposed by Hall and Soskice (the financial system, industrial relations, internal structure of the firm, education and skills formation and inter-company relations), this paper also takes into account foreign direct investments, social and environmental sustainability. The available evidence suggests that Laos can be categorised as a State Coordinated Frontier Economy in which elites and foreign investors accumulate wealth at the expense of small firms, villagers and the natural environment. The government is particularly present in the spheres of finance and inter-company relations. A continuation of this variety of capitalism is likely to result in excessive inequality and severe environmental degradation. The task for Laos is now to foster more inclusive forms of state coordination and balance economic growth with ameliorative policy initiatives catering to the natural environment, displaced villagers, ordinary employees and small business owners. This will be a difficult endeavour as there is still a profound mismatch between prevailing economic institutional complementarities and historically informed cultural institutions.

Keywords

Capitalism, institutional complementarities, foreign direct investment, government–business relations, SMEs, inclusive/exclusive development, inequality, Laos

Laos¹

A state coordinated frontier economy

1 Introduction

This paper focuses on the smallest economy in Southeast Asia after Timor Leste: Lao People's Democratic Republic, hereafter simply referred to as Laos. Laos as a territorial entity is a product of the colonial era, in which the French sought to disconnect the area east of the Mekong River from the economy and culture of Siam, contemporary Thailand (Ivarsson 2008). In addition, the Vietnam War caused enormous havoc in Laos with communists and pro-North Vietnamese forces fighting against non-communists, for a considerable part made up of ethnic minorities such as the Hmong people. In 1975 the Communist Party (officially Lao People's Revolutionary Party) claimed victory and has ruled the country ever since.

However, Laos remained a purely communist country for only 11 years. The Communist Party, looking at an economy in shambles and following economic reforms in the USSR and China, announced the New Economic Mechanism (NEM) in 1986 (Stuart Fox 1997: 195-201). The NEM has been responsible for the entry of capitalist institutions, a remarkable opening of markets and influx of foreign direct investment (FDI). Nevertheless, the political system has remained strictly communist. The *Polit Bureau* of the Communist Party is in firm control of all political activities and the Secretary General of the Party is also President of the Republic; currently Lt. General Choummaly Sayasone.

This paper assesses the current variety of capitalism in Laos using Hall and Soskice's (2001) comparative approach and the emerging body of knowledge on Varieties of Asian Capitalism. The last decade has seen a considerable interest in theoretical and empirical approaches that compare the various institutional arrangements in developed capitalist societies. Most spectacularly, the publication of Hall and Soskice's (2001), *Varieties of Capitalism: The institutional foundations of comparative advantage*, has triggered many responses. Some authors have conducted empirical studies following the main theoretical arguments of Hall and Soskice, others disagree on certain domains of thought and have proposed more or less alternative perspectives. According to Hall and Thelen (2009) the approach

...focuses on firms, as actors central to the process of economic adjustment with core competencies that depend on the quality of the relations that they develop with other actors, including producer groups, employees and other firms. Those relationships depend, in turn, on the institutional support provided for them in the political economy. Although the perspective acknowledges that these relationships can take on a wide range of forms, it emphasizes the distinction between liberal market economies [LMEs], where firms rely heavily on competitive markets to coordinate their endeavours, and coordinated markets economies [CMEs], where more endeavours are coordinated strategically.

¹ The author wishes to express his gratitude to Bert Helmsing for valuable comments on this paper.

Most studies have employed a framework in which five institutional spheres are compared: corporate governance (here rephrased as financial system), industrial relations, internal structure of the firm, education and skills formation and inter-company relations. The most important countries with liberal arrangements are the USA and UK; with coordinative arrangements Germany and Japan. Based on this distinction, Hall and Soskice further assert that the first group of countries offers more scope for radical innovation. Competition entails flexibility and short term goals suitable for economic activities directed at designing and marketing new products. Coordination, instead, generally means less flexible relationships, for instance regarding industrial relations, and longer term goals, making it more attractive for incremental innovation; in other words, the enhancement of processes and existing products rather than totally new products. In sum, a particular set of complementary institutions is seen as conducive for particular types of economic activity. Among others, Schmidt (2003) has stressed that the dichotomy between competition and coordination is too rigid. Instead she has proposed the inclusion of a capitalist system based on state dominance. This particularly fits the traditional French capitalist model in the three decades or so after the Second World War.

Increasingly, the Varieties of Capitalism approach is also being employed for developing countries. In 2009 the journal *Economy and Society* (volume 38, issue 1) published a special issue focusing on Latin America, entitled Latin American Capitalism: Economic and Social Policy in Transition. And in the same year *Asia Pacific Journal of Management* (volume 26, issue 3) published a special issue on Varieties of Asian Capitalism (volume 26, issue 3). This issue has not much focused on the way countries innovate, but relatively on the co-evolution of institutional arrangements and firm behaviour, essential in transition economies such as China, Vietnam and Laos, the role of the state and the relationship between institutions and inclusive and sustainable development (Andriessse and Van Westen 2009; Carney et al. 2009; Ritchie 2009; Tipton 2009). This paper builds on these analytical issues. In addition to a systematic discussion of the traditional capitalist elements proposed by Hall and Soskice (2001), it also pays much attention to the role of the state and the relation between capitalism and social and environmental sustainability, in particular in sections 7, 8 and 9. For the creation of sustainable and inclusive societies, particularly in a complex multiethnic society such as Laos, economic growth and innovation certainly do not suffice (see also Andriessse et al. forthcoming; UNDP 2010; Rigg and Wittayapak 2009; Ochieng 2008; Cornford 2006). Another feature of this paper is the inclusion of foreign direct investment in the assessment as the entry of capitalist institutions in Laos has been accompanied with an influx of many foreign investors.

Considering socio-economic poverty in the country and transitory nature of capitalist institutions it is probably not a surprise that Laos does not fit into the category of either a traditional LME or a CME. Instead, it will be concluded that at this stage, the capitalist structure can be characterized as a State Coordinated *Frontier* Economy. Ritchie (2009) has earmarked Singapore's variety of capitalism as a State Coordinated, *Liberal Market* Economy. The Singaporean state has been highly instrumental in fostering certain industries, upgrading technological capabilities and the level of education and advanced

skills while maintaining a liberal market environment. The narrative for Laos is obviously markedly different. In the following sections the interactions between the public and the (foreign) private sector will be elaborated upon and the choice for “Frontier Economy” will be justified. It should also be noted that relatively few academic publications can be found dealing with capitalist institutions in Laos, but fortunately this is compensated for by a number of excellent reports prepared by the development community (notably Ngongvongsithi and Keola 2009; UNDP 2006). There is especially sufficient information about the garments industry. It is thus instructive to use this industry occasionally as illustration of the current variety of capitalism in Laos, all the more as it is the leading factory based industry in the country.

2 Frontier capitalism and foreign direct investment

As Laos is generally a less well known country this section starts with a brief overview of its socio-economic situation. Laos’ population of just over 6 million people is small in the Southeast Asian context. Similarly, the size of the Lao economy is very limited and moreover, 79% of the labour force is still working in agriculture (ADB 2010). Important agricultural produce include rice and sugar from the low lands and timber, rubber and coffee from the hills. In the latest UNDP’s Human Development Report Laos is ranked as 122nd in the human development index (HDI), with a value of 0.497. Timor Leste is ranked above Laos (120st), whereas Cambodia (124th) and Burma/Myanmar (132nd) are positioned somewhat lower on the list (UNDP 2010: 145). The relatively low level of human development is also reflected in the high reliance on development aid. Official development assistance accounts for a staggering 10% of the gross national income (UNDP 2010: 204).

According to the International Monetary Fund the top 3 exports in 2008 were copper, garments and timber (IMF 2009). Garments are particularly interesting to analyse from a capitalist point of view as it is virtually the only factory based export industry in Laos (see particularly sections 5,6 and 7) (Ngongvongsithi and Keola 2009). The top 3 export destinations are Thailand, Vietnam and China. Another important export industry is labour as wages in Thailand and other countries are much higher. The scope and nature of the migration flows cannot be rigorously studied as there are so many illegal undocumented migrants. The UNDP (2006) considers garments, wood products and processed foods as high potential exports for the future from a human development point of view (employment generation and limited environmental pollution if managed well), but in the contemporary Lao political economy, the booming industries are copper and gold mining and hydropower; industries that generate little employment and destroy the natural environment. Ten years ago there were no copper exports; in 2008 the export value totalled 620.3 million US\$ dollars (IMF 2009). Another example is the joint venture of giants Rio Tinto and Mitsui to explore bauxite mining opportunities (China Mining 2010). Laos even aims to be the *battery* of neighbouring countries. At the end of 2010 the huge Nam Theun 2 dam (NT2) opened and started selling electricity to Thailand (Bangkok Post 2010a).

The remarkable current trends in Lao mining and hydropower are part of a wider economic geographical phenomenon which can be labelled as resource frontier: “a process of change which advances, a constant shifting and restructuring movement involving three interlocking elements – population, land and spatio-productive structure. The frontier is thus not simply a line or even zone but a dynamic process of spatial interaction in which unoccupied resource-rich regions are incorporated into national economic space” (Armstrong 1991). In fact, in the Lao case it is more appropriate to think of international economic spaces as foreign companies have had a dramatic impact on unoccupied resource-rich regions (see also Hayter et al. 2003) for a more theoretical exposition of resource peripheries. Thai companies have invested in sugarcane plantations in Southern Laos, the copper and gold mine in Savannakhet province is owned by the Chinese state owned copper importer Minmetals; Chinese and Vietnamese are involved in rubber plantations in northern and southern provinces respectively and NT2 is a complex project involving direct investments from Thailand and France (Bangkok Post 2010a; Shrestha 2010; International Rivers 2010; Baird 2010; Cohen 2009). According to Barney (2009) the resource frontier “captures empirical reality concerning the political economy of rapid and uneven development in the country”. It should be noted, however, that foreign investors have not only made inroads in resource frontiers, but also in the manufacturing industries such as garments and motorcycles assembly activities (Ngongvongsithi and Keola 2009). Between 2000 and 2005 net average FDI inflows as percentage of GDP was 1.3% of GDP, between 2006 and 2008 not less than 5.8% (ADB 2010)! Since 2006 FDI inflows seem to have really taken off.

Entrepreneurial activity in general has experienced a boost in the last two decades. The share of agriculture in the GDP has declined from 61% in 1990 to 33% in 2009 (ADB 2010) and many new firms have opened doors. At present several types of firms operate in Laos: small and medium sized firms, about 23 joint ventures between the Lao government and foreign firms, joint ventures between private Lao and foreign firms, about 200 traditional state owned enterprises and an unknown number of unregistered firms operating in

TABLE 1
The manufacturing sector in Laos, 2006

Industry	Number of establishments	Number of employees
Construction materials	10300	100720
Food and agro-processing	18855	35000
Garments	82	25000
Wood products	2200	25000
(Hydro)power generation	10	7000
Mining	30	6000
Others	119	10500
Total	31596	209220

Source: Ngongvongsithi and Keola 2009

the informal economy (Vientiane Times 2011). In their research on industrial upgrading Ngongvongsithi and Keola (2009) estimate that there were 24331 manufacturing establishments (excluding construction, power generation and mining) in 2006 and 81780 wholesale, retail trade and repairing establishments. That leaves 20820 establishments in an array of other sectors, generating a total of 126913 establishments.

For the purpose of this paper it is instructive to zoom in on the manufacturing sector (including power generation and mining) as this sector displays most clearly the emergence of certain capitalist institutions in Lao's development trajectory. Table 1 shows that relatively many people work in construction materials businesses, food and agro-processing firms generally employ few workers, whereas hydropower facilities and mining are big in terms of number of workers, but do not contribute much to employment generation in general for the entire Lao labour force.

3 The financial system

The financial system is still in its infancy. Probably most telling is the fact that one can easily pay with Thai Baht and US Dollars in Vientiane and many other provinces. For tourists prices are also shown in US Dollars. Moreover, in provinces neighbouring Vietnam and China the Vietnamese Dong and Chinese Yuan are also widely used. The government is trying to institutionalize the Kip by putting up signs to persuade citizens and tourists to use the national currency, but so far this has not been an overwhelming success. With respect to *haute finance* Laos just celebrated a mile. The New Straits Times (2010) reported December 28: "Eager novice investors in communist Laos signed up for shares as the country's first-ever initial public offerings (IPOs) came to a close, an investment banker said yesterday". The IPOs involved two companies: Electricite du Laos (EDL), a spin off from a state-owned company and the state-owned commercial Banque Pour Le Commerce Extérieur (BCEL). Eventually, the aim of the Lao stock exchange authorities for the near future is to offer share trading in around 20 (state owned) companies (Vientiane Times 2011; People's Daily Online 2009). Obviously, it remains to be seen to what extent the Lao Stock Exchange will be genuine success.

Banks are important for Laos, but mainly for state owned and foreign firms. The banking structure can roughly be divided into three groups: state owned banks such as BCEL, new privately owned banks and Thai banks. At least five major Thai banks have opened branches in Vientiane, partly catering to the many Thai investors in the country. For small and medium sized companies it has been extremely difficult to obtain access to finance from banks and the interest rate is high (Ngongvongsithi and Keola (2009). The UNDP (2006: 10) summarized the deplorable situation as follows:

The state banking system is still weak and burdened by non-performing loans to state-owned enterprises (SOEs)...Many Lao private firms without any FDI have limited or no access to credit. As a result some of these firms are unable to invest enough and remain too small, unable to take advantage of economies of scale, less able to compete with imports, and less able to make investments to protect the environment.

These comments also hold for the smaller firms in the garment industry. There seems to be a lack of working capital and borrowing money is cumbersome. The UNDP (2006: 47) complained that for certain companies the financial system is “simply not at all accessible”. On the other hand, companies that have teamed up with foreign investors have had much easier access to finance, notably in the fields of the power generation, rubber and sugarcane plantation, mining and industry and handicrafts. Companies from neighbouring countries have been particularly instrumental (Table 2).

TABLE 2
Approved FDI data in percentages 2003 - 2008

by country		by sector	
Thailand	23.7	Power generation	53.9
China	16.9	Agriculture	11.4
Vietnam	9.3	Mining	9.8
Japan	5.8	Industry and Handicraft	7.5
France	5.7	Services	4.3
India	4.8	Trading	3.8
South Korea	4.7	Construction	2.9
Australia	4.6	Hotel and Restaurant	2.6
Malaysia	1.8	Other activities	3.7
Singapore	1.4		
Others	21.3		

Source: IMF 2009

Microfinance is a growing industry that could have benefits for small enterprises in the future; particularly for the many small food and agro-processing firms located in the periphery of the country. In sum, the financial system is state mediated. Access to finance still depends on the relationships companies have with the government. For instance, EDL Generation and BCEL are clearly very well connected to the public sector. Also, many of the firms, that currently operating in joint ventures with foreign companies, are in effect direct or indirect state-owned enterprises.

4 Industrial relations and internal structure of the firm

The liberty has been taken here to merge the internal structure of the firm and industrial relations as there are few publications on these matters, especially on internal structures. It is possible to comment on the perception towards employees, but virtually no publications deal exclusively with the management culture and leadership styles in general. In addition, global surveys such as the World Competitiveness Report do not include Lao PDR. Fry (2008) has identified four phases in Lao’s industrial relations: 1. The colonial era; 2. The Royal Lao Government era between 1947 and 1975, of course very much disturbed by the Cold War; 3. The communist era between 1975 and 1986 and 4. The post 1986 era in which capitalist formal and informal institutions have

made serious inroads into Lao's development trajectory. For the purpose of this paper it is most instructive to focus on this last era.

According to Fry the lack of democratization has led to a vulnerable situation for employees. Employees are not allowed to strike and extremely limited possibilities for associations, trade unions and collective bargaining exist. Trade unions can 'present claims' and 'negotiate, but have no right to conduct collective bargaining.' (Fry 2008) Moreover, wages in Laos are very low, putting the majority workers in a difficult position. The labour law of 1990, the new Constitution adopted in 1991 and the revised labour law of 1994 have not been helpful for employees. Fry ironically reports on a conclusion of a study conducted by UNIDO in 2003 "in which the only item [out of 19 items] Laos scored a perfect 10 out of 10 for being 'market based' was 'wages'". In fact, one can conclude that labour is perceived as an input factor which can be exploited rather than as human capital which should be embraced. There is more room for manoeuvre for employers. Employer associations such as Lao National Chamber of Commerce and Industry (LNCCI) and the Association of the Lao Garment Industry (ALGI) are relatively free in promoting their industries. In section 6 more on these organisations.

No study has been found explicitly dealing with the general internal structure of firms. Doing objective research within SOEs or companies that are somehow connected to the state is probably difficult if not impossible, so it is not a surprise that Southiseng and Walsh (2010a) have focused on SMEs. They interviewed 52 entrepreneurs in Vientiane, Luang Prabang and Savannakhet. Their study focused somewhat more on the relationships between SMEs and the external competitive environment, but provides also some insights into internal affairs. Most SMEs are family run businesses focusing much on day-to-day operations rather than longer term strategic planning. Business owners manage their firms with little input from employees and learn more from their parents when they were the owners than from their time in high school or college. In sum, Southiseng and Walsh conclude that there is in general limited entrepreneurial experience and a lack of professional business administration and managerial skills. On the one hand these results are logical as the private sector itself is phenomenon which is only approximately 25 years young. On the other hand, it seems that the government pays insufficient attention to the development of SMEs; particularly with respect to professionalizing internal structures (see section 8 as well). Overall, industrial relations and the internal structure resemble more institutions in a LME than in a CME. Many employees are forced to fend for themselves and participate little in decision making processes.

5 Education and skills formation

Education and Skills formation poses a great, if not the greatest socioeconomic challenge in contemporary Laos. To start with a dramatic statistic: Only 37% of males aged over 25 years have completed secondary education and this is only 23% for females, a sign of enormous gender inequality (UNDP 2010: 158). Many commentators on Laos have said that there is not a shortage of labour, but of skilled labour (see for instance Rasiah 2009 and UNDP 2006: 47;

Cornford 2006). The educational system is still in transition and clearly needs to be massively improved, but three interrelated complex problems arise. First, due to extremely low wages for teachers and university lecturers it is not easy to attract motivated and skilled educators (Rehbein 2007: 106). Most teachers and lecturers need to have second jobs to make a reasonable living. Second, not less than 50% of the Lao population, mainly living in peripheral upland areas, have grown up using languages other than Lao such as Mon-Khmer, Tibeto-Burman, Miao-Yao or Viet-Muong (Rehbein 2007: 96). This makes it hard to integrate those people in the mainstream society. Simply encouraging unemployed men and women to migrate to places where work is available, is therefore not advisable (Cohen 2009; Cornford 2006). Third, there is a large gender inequality in terms of skill levels. Cornford (2006) for instance, argued that road improvements in Savannakhet do not automatically lead to easier access to urban fresh markets for rural women, because they cannot sell vegetables and fruits due to language problems. Worst off obviously are women who neither have completed secondary education nor have a sufficient command of the Lao language. In case they migrate to the cities of Vientiane, Savannakhet or Luang Prabang or perhaps even abroad, they are vulnerable to various degrees of economic and/or sexual exploitation. In sum, benefiting from capitalist opportunities requires much more than setting the economic institutions right.

Primary education in general has a good national coverage, but secondary education should be expanded (UNESCO 2000). In some parts of the country children need to travel very far to find a high school. Another critical issue is the quality of education. A shift in national budget priorities seems to be welcome in this respect. According to the UNDP (2010: 204) Laos had spent 2.3% of its GDP on education between 2000 and 2007. This percentage is quite low considering that Thailand had spent 4.9% and Vietnam, also a country in transition, 5.3%. Higher education has experienced remarkable expansion since the start of the NEM in 1986. The only comprehensive university in the country is the National University of Laos in Vientiane, but several other small universities and many private institutes have been set up in the previous decade (Ogawa 2008).

The available sources on skills formation and training in the private sector generate a bleak picture. Southiseng and Walsh (2010a) have found out that SMEs value honesty, well mannered and ability to speak Vietnamese, Chinese and English and experience more than educational levels. And in another study Southiseng and Walsh (2010b) compared human resource development practices in Thai's and Lao's telecommunications industry. Based on interviews they conclude that Thai telecommunications companies are doing much more to improve their employees' capabilities. In Laos it is actually inappropriate to use the term human resource department. The traditional personnel department is more suitable. Insights from the relatively well studied garments industry confirm the lack of proactive human resources development. The UNDP (2006: 47) summed up a lack of skilled labour, high turnover and the absence of efficiency wages – “paying above market wages to retain the best workers, increase productivity and reduce training costs” – as major obstacles for further growth. Those obstacles might even become a serious threat to the survival of the garment industry in the event of removal of preferential trading

regimes by developed importing trading blocs/countries such as the European Union and the USA (Rasiah 2009). In that case garment factory owners, particularly the foreign ones, could opt for relocation to cheaper areas nearby sea ports such as Cambodia or Vietnam. Note that high transportation costs remain a burden for any industry in Laos (Ngongvongsithi and Keola 2009; National Statistics Centre unknown).

Although the educational and skills formation system will be probably be in transition for the coming two decades or so, it is possible to conclude that Laos is as of now, leaning towards a LME model in which labour is valued more as an input factor than as human capital. There are virtually no signs of coordinative, effective institutional arrangements resembling the Japanese or German model.

6 Inter-company relations

No publications deal explicitly with inter - company relations in the mining, hydro power generation and plantation industries, three activities operating in Lao's resource frontiers. Nevertheless, it is possible to distil inter-company relations from authors who have studied socioeconomic changes in the frontiers. Frontier industries need approval and licenses from the Lao government before resource extraction or the built up of plantations can be embarked upon. And as in all frontiers there is a tendency of *first come, first serve*. Henceforth, companies interested in beginning operations obviously tend to cultivate good relations with the government and consider other companies as competitors who should be kept at bay rather than as possible partners for cooperation. Barney (2009) has documented how the Japanese company Oji Paper purchased BGA Forestry in 2005, a company who held the original concession, to start commercial eucalyptus plantations in Khammouane province totaling 150 000 hectares. In 2008 17 large mostly foreign companies already obtained concessions to start large scale rubber plantations (Baird 2010) and even the military granted a rubber plantation concession to a Chinese company (Cohen 2009). Also, many people in Vientiane think that the rich have become rich because they have somehow close connections to the government. Furthermore, the new Lao Holding State Enterprise is increasingly engaged in joint ventures with foreign companies, an indication that inter-company relations are becoming more mediated such as in France between the 1950s and 1980s or in Malaysia (Andriessse and Van Westen 2009; Schmidt 2003). This State Enterprise is part of the Ministry of Finance and is mainly engaged in hydropower generation, but it can be expected that it will venture in other industries as well in the future. Currently, this Enterprise has a 25% stake in the NT2 dam; Electricité de France International 40% and the Electricity Generating Company of Thailand 35% (International Rivers 2010). As the tax base in Laos is very narrow, the government is very eager to find ways to boost revenues. Frontier industries provide an excellent opportunity for generating royalties, export duties and other revenues. For instance, the export duty for electricity is 20 percent of the invoice value (IMF 2009), which means that NT2 will become a huge contributor to the Lao state coffers.

Another observation can be made regarding customers. The majority of the customers are foreign. The Electricity Generating Company of Thailand buys 90% of the total output of NT2, Thai companies buy the sugarcane from plantations in central and southern Laos and Chinese companies buy natural rubber from northern Laos and copper and gold from the mines, but it is not known whether contracts are used or more informal arrangements. In fact, this would be an interesting topic for further research.

Once again, turning to the garment industry brings about more in-depth insights into current inter-company relations, particularly among SMEs. Kyophilavong (2009) used the garment industry as a case in a report on SME development in Laos and surveyed 20 companies. External networking seems to be non-existing. Out of 20 SMEs only 1 is in touch with the Small and Medium Sized Enterprise Promotion and Development Office (SMEPDO) and none with ALGI! Kyophilavong and the UNDP (2006: 48) furthermore noticed that owners have insufficient market information, for instance about industry trends and the implications of the ASEAN-China free trade area taking effect in 2015. A study executed by a team comprising among others the National Statistics Centre (date of publication unknown) sums up the shortcomings:

Small and medium companies tend to operate on their own, a risky policy in an increasingly competitive market, and the team points to strengthened networks within the garment industry where larger companies, ALGI and the government should develop mechanisms to assist small and medium companies in the sector.

Indeed, ALGI and the Lao national chamber of commerce seems to be a more a vehicle for large domestic, foreign owned, joint ventures and SOEs rather than SMEs. Another problem for SMEs is the supply side. Most inputs for garment manufacturing come from abroad (IMF 2009; Rasiah 2009) and SMEs find it difficult to foster good relations with foreign suppliers.

Besides garments food and agro-processing is regarded as a suitable export industry that should be nurtured (UNDP 2006). Andersson et al. (2007) analysed the coffee value chain in southern Laos. Coffee production and exports have increased dramatically since the mid 1990s, but more positive is that two larger firms have been able to capture part of the value chain from foreign actors. Value addition such as roasting and packaging used to be carried out abroad, but is increasingly done in Laos. Furthermore, the Lao Coffee Export Association has been instrumental in providing access to foreign buyers and foreign coffee experts. Nowadays, Germany, France and Japan are the top three destinations for Lao coffee. This example shows that networking and fostering inter-company relations in Laos is possible and moreover, has a positive impact on coffee farmers as they have more secured sales.

Overall, however, it is not easy to escape the view that inter-company relations are virtually absent among SMEs and remain stated mediated, despite the NEM instigated in 1986. The Lao government is not only a facilitator of the booming mining, hydropower and plantation industry, but is also a genuine *interventionist*. As such, Laos more resembles its former colonial master France than a LME or CME (Schmidt 2003).

7 Lack of economic cohesiveness and environmental sustainability

Besides the challenges with respect to Hall's and Soskice's (2001) institutional spheres discussed above three features hamper the blossoming of an inclusive and sustainable form of capitalism in Laos.

First, the country is geographically fragmented (Andersson et al. 2009 and 2007). In economic terms Southern Laos is better connected with Vietnam and Thailand than with the rest of Laos, Vientiane has many linkages with Thailand and Northern Laos is better connected with China than with the rest of Laos. Furthermore, ethno-linguistic fragmentation is not conducive for social capital/enabling informal institutions. Ultimately, fragmentation might create *regional* varieties of capitalism, but further research is needed as the country is still in transition (Andriessie forthcoming). For example, it would not be a surprise if pockets of positive development emerge in certain localities through inclusion in international value chains and through informal trust based networking (Andriessie et al. forthcoming).

Second, it remains to be seen whether the current leading industries are viable. Once resources become depleted, foreign investors might pack their bags and look for mining and plantation opportunities elsewhere. Moreover, the two main rationales for a sizable garment industry are extremely low wages and access to preferential trading agreements with the USA and the EU rather than comparative advantages in garment materials, economies of scale and scope and proximity to cheap logistical services (Rasiah 2009; Ngongvongsithi and Keola 2009; UNDP 2006). This does not seem to be a viable model for the long term. In the event the current leading industries become obsolete, it is difficult to think of alternatives. Wood products and food and agro-processing might be suitable (UNDP 2006), but much need to be done in order to make those industries viable. As of now, Laos is squeezed between Vietnam and Thailand.

Third, there is the major issue of environmental sustainability, especially in the emerging hydropower industry. It is now well accepted that dam building has created major environmental pressures (The Nation 2011; Hirsch 2010; International Rivers 2010, Shrestha 2010). According to Barney (2009) "relational frontier processes and actors, both central and local, produce new landscapes of commodity production and extraction, as well as unexpected transformation and displacement effort for a vulnerable upland and rural population". Local populations generally experience the bulk of negative externalities. Unfortunately, the government does not seem to acknowledge this phenomenon to the greatest possible extent. In this respect it might be worthwhile to take up Ochieng's (2008) conclusion that relevant stakeholders should be at the heart of reforming capitalist systems rather than orthodox, purely economic growth and profits.

8 Complementarities

According to Hall and Soskice (2001) institutional complementarities can be referred to as interlocking sets of arrangements that jointly promote certain types of economic behaviour, while discouraging others. Based on the institutional arrangements discussed above, it is possible to identify two institutional complementarities:

1. The financial system *and* inter-company relations are both state mediated (Tipton 2009; Andriessse and van Westen 2009; Schmidt 2003). This has led to enabling arrangements for large companies, particularly those that are well connected to the public sector. On the other hand, it has resulted in disabling arrangements for SMEs. Ordinary entrepreneurs find it very difficult to obtain access to finance, the LNCCI, SMEPDO and other business organisations do virtually not support SMEs and the public sector in general is favoured towards large (foreign) companies interested in hydropower, mining and large scale plantations. In this respect Laos could take Thailand as an example, where state owned banks such as Krung Thai Bank, SME Bank and Export-Import Bank provide easy access to finance and other services to small entrepreneurs.
2. Internal firm structure *and* industrial relations *and* education and skills formation resemble more or less a LME model. Somewhat ironically, the *Communist* Party has facilitated an economic environment in which hierarchical decision making processes, extremely low wages, weak employee protection and little investments in formal education as well as on the job training have accommodated a process of taking quick advantages of resource frontier opportunities. The main beneficiaries of these arrangements are the political elite and, again, large companies at the expense of labourers and villagers. The danger in the long term is increasing socioeconomic inequality. Indeed, walking in Vientiane provides a good window into this phenomenon. Hummers and beggars both occupy public space.

On the one hand, it seems that without policies taking into account more fully environmental pressures and the plight of SMEs, labourers and villagers, excessive inequality may ultimately undermine the legitimacy and very nature of the current political economic model. Corruption, for example, is a growing problem (Linter 2008), but at the end of 2010 the National Assembly appointed a new Prime Minister. According to the Bangkok Post (2010b) the former one wished to crack down on corruption, but was not backed by the Communist Party. More in general terms Rigg and Wittayapak (2009), writing on market based developments in the Greater Mekong Subregion, contend that negative side effect should be comprehensively “identified, managed and ameliorated”. On the other hand, it should nevertheless be noted that Laos is a country in transition, so it is rather difficult to predict how the institutional complementarities will co-evolve with firm behaviour (Carney et al 2009; Hall and Thelen 2009).

9 Conclusion: a state coordinated, frontier economy

Cohen (2009) has concluded that the economic activities in Northern Laos are a form of *unregulated* frontier capitalism. The available evidence presented in this paper provides a different picture. In fact the Lao government has enabled frontier capitalism through deliberate facilitation and intervention in markets, notably the financial market as well as mediation of inter-company relations (the first complementarity identified above). Moreover, the government forbids employees to strike and trade unions to bargain collectively and has invested relatively little in the educational system and education and skills formation. Therefore, it is argued here that deregulation in economic frontiers is an outcome of overarching state coordination. Laos can thus be categorised as a *State Coordinated Frontier Economy*. Even the garment industry based in and around Vientiane displays frontier characteristics. Garment factory owners seek to take advantage of low wages and preferential trading access to the USA and the EU, but could easily leave for other short term frontiers once those advantages disappear. This is a stark contrast to Ritchie's (2009) conclusion of Singapore as a highly effective State Coordinated *Liberal Market* Economy where entrepreneurs in the manufacturing and services sectors set up businesses for the long term. The task for Laos is now, as suggested by Ritchie as well, to incorporate appropriate pockets of Singaporean effectiveness balanced with ameliorative policy initiatives catering to the natural environment, displaced villagers and ordinary employees. This will be a difficult endeavour as there is still a profound mismatch between the institutional complementarities identified above and cultural institutions. Reihbein (2007: 72-73), an expert on contemporary Laos, has expressed this very eloquently:

While the habitus of most Lao is still firmly rooted in the rural past, it is now being exposed to radical changes and is under pressure to adapt to the market economy...And even if they succeed in adapting to the market economy, Lao often adhere to traditional conceptions of time, work, happiness and behavior that are hardly compatible with the 'spirit of capitalism.

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