



# America-Southeast Asia Program

October 10, 2022

## The Hidden Financial Crisis in Laos



People line up at a petrol station in Laos, May 2022, as inflation increases scarcity of essential commodities including fuel. Photo Credit: Reuters

**The America-Eurasia Center**

[www.EurasiaCenter.org](http://www.EurasiaCenter.org)

**Eurasia Brief**

**Southeast Asia Program**

**America-Eurasia Business Coalition**

[www.usebc.org](http://www.usebc.org)

# The Hidden Financial Crisis in Laos

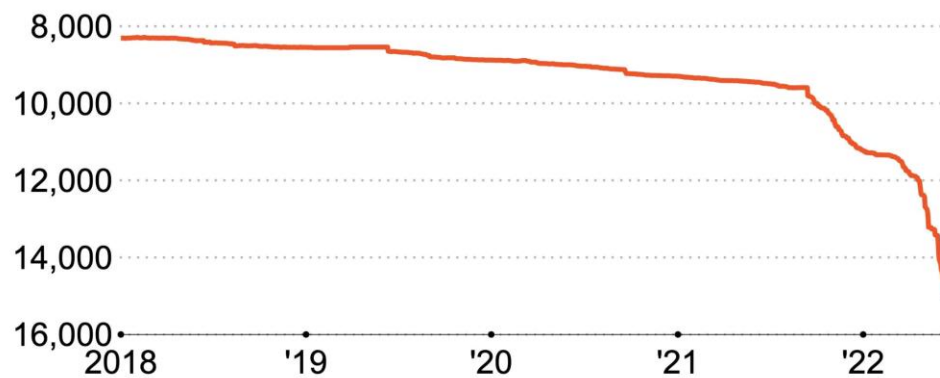


People line up at a petrol station in Laos, May 2022, as inflation increases scarcity of essential commodities including fuel. Photo Credit: Reuters

Laos is a small, landlocked country located in Southeast Asia. It is home to about seven million people and is run by a one-party Communist rule. It is one of the few remaining Communist countries in the world. Like many countries over the last few months Laos has been dealing with record high inflation and rising gas and energy prices. The current inflation rate in the country is 12.8%, the highest in 18 years. The war in Ukraine and the continued economic fallout from the Covid-19 Pandemic has sent prices of everyday items, such as groceries and gasoline, surging. Laos had been facing grave financial issues even before the recent global crises. Their foreign currency reserves have depreciated to only 1.4 billion dollars compared to the average of 110 billion dollars in most other nations. Their debt payments per year until 2025 are supposed to be 1.3 billion dollars, which is almost the entire amount of their current foreign reserves. They also have an extremely high foreign debt, owed mostly to China, and their currency, the Lao Kip, is currently collapsing in value against the U.S dollar. It has lost 36% of its value against the dollar. Laos' foreign debt has amounted to 14 billion dollars and the World Bank estimates that about half of that is owed to the Chinese. Laos is currently one of the most deeply indebted countries in Asia as well as one of the poorest.

---

## Laos currency exchange rate against dollar



*Source: Refinitiv*

---

**This graph depicts the Laos currency exchange rate against the dollar, from 2016 through 2022**

The small nation is nearing a catastrophic debt default that could potentially impact the greater Southeast Asia region. In June, Moody's, an international credit rating site downgraded the country to its "junk" category and warned that it was likely to default on their debt payments. Many economists believe that Laos is stuck in a scenario known as a "debt trap" by China and Chinese investors. The U.S and other nations' have accused China of pursuing "debt trap diplomacy". They say that this tactic is designed to make developing nations more dependent on China for financial support and aid. Chinese debt traps have also been blamed for several other countries' economic issues. One instance of this is in Sri Lanka, where their economy recently collapsed, and the entire government resigned or fled the country. 10-15% of Sri Lanka's foreign debt is owed to the Chinese. This is the same with many African countries as well, such as Guinea and Sudan. These "debt trap" situations often occur since the Chinese government offers to help develop or build a major project for a country. Once the project is completed, the country in question is typically left with larger debt than the projects actually cost to develop. In July, the G7 nations pledged billions of dollars to developing countries to boost their economies hoping to counteract China's recent gains in financial diplomacy.



Laos' currency, the Lao Kip. Image Credit: DepositPhotos

Some, like Tokyo University Professor Toshiro Nishizawa, take a different view and believe that China will not let Laos default because it will reflect badly on their reputation as a trusted economic partner as well as harm their expansive Belt and Road trade route initiative in the region. China is also Laos' largest creditor and ally, and they feel a political kinship with the Lao government since both countries govern under a strict communist system. Professor Nishizawa also states that China has recently been working on trade projects with the Association of Southeast Asian Nations (ASEAN) and they would not want to jeopardize their budding economic relationship with a critical organization in the Asia-Pacific region. The bulk of the debt to China comes from the building of new hydro-power plants and a connected Lao-China railroad system. The railroad is the most expensive project ever built inside Laos. 70% of the railroad is owned by three different Chinese companies and only 30% of the project is owned by the Lao government and it cost 5.6 billion dollars to complete. China is also now a major global superpower and one of the richest nations in the world. Many developing countries have begun to seek out the Chinese government for financial loans or joint manufacturing projects that will give a revenue boost to both countries.

There is an ongoing debate about whether the country's current situation is completely blamed on China or if the Lao government simply made poor fiscal policy decisions when they are already a poor and indebted country. The firing of the Bank of Laos Governor, Sonexay Sitphaxay, in June is an indicator of how seriously the government is taking the economic crisis. He was



replaced with former deputy finance minister Bonleua Sinxayvoravong. The autocratic government has now begun to realize how dire the situation is and they are trying to mitigate the public reaction ever since a major public outcry online in June. Since the country is run by a one-party state with very limited freedom of press, speech, and dissent, the Government has not been entirely transparent with the public about the extremity of the nation's economic situation. Nishizawa says that the government is only releasing selective information so as not to alarm the public and potentially spark protests.



**Bonleua Sinxayvoravong, Laos' newly appointed Bank of Laos Governor. Image Credit: EuroCham Laos**

Unlike the situation in Sri Lanka, Laos still may be able to come out of their current economic crisis. Tourism is now beginning to flow back into the nation after borders with Thailand and Vietnam have opened. The China-Laos railroad, despite its expensive cost, is bringing in more trade and the nation still has not lost their ability to trade in international markets. Laos still has an extremely long way to go in repaying their foreign debt and stabilizing their economy, but as they come out of the pandemic, they might yet still have a chance at financial stability.

## Works Referenced

<https://www.economist.com/asia/2022/06/30/will-laos-default-on-its-debt>

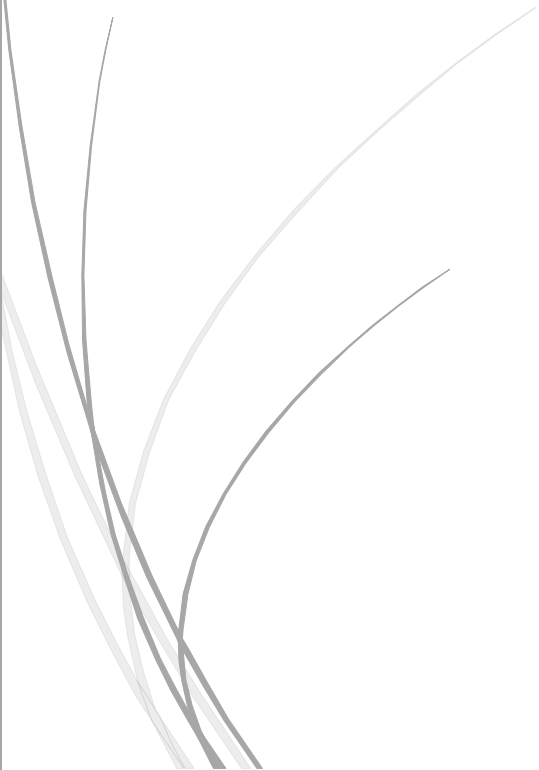
<https://www.cfr.org/blog/laos-economic-crisis-spiraling-out-control-it-struggles-massive-debts-china>

<https://www.voanews.com/a/laos-faces-debt-crisis-after-borrowing-billions-from-china-6641633.html>

<https://www.nytimes.com/2022/08/15/opinion/international-world/sri-lanka-economic-collapse.html>

<https://asia.nikkei.com/Economy/Laos-faces-public-backlash-as-economy-teeters-toward-default>

<https://www.eastasiaforum.org/2022/08/25/claims-of-default-in-laos-are-bankrupt/>



**America-Eurasia Center**