

LAO PEOPLE'S DEMOCRATIC REPUBLIC

No. 70/2020

15 May 2020

SOVEREIGNS

Sovereign Rating:	BBB
Issue Ratings:	
Senior unsecured	BBB
Outlook:	Negative

Last Review Date: 28/06/19

Sovereign Rating History:

Date	Rating	Outlook/Alert
28/06/19	BBB	Stable
12/06/17	BBB+	Negative
10/06/15	BBB+	Stable

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RATIONALE

TRIS Rating affirms the sovereign rating on the Lao People's Democratic Republic (Lao PDR) and the ratings on the Lao PDR's outstanding senior unsecured bonds at "BBB", and revises the outlook to "negative" from "stable".

The "negative" outlook reflects our view regarding the increasing strain of the Lao PDR's debt servicing burden over the next 12-24 months, caused by the country's weakening economy as a result of the coronavirus (COVID-19) fallout, deteriorating external position, persistently low foreign currency reserves, and the continued depreciation of its currency.

The rating on the Lao PDR continues to reflect its sovereign profile as a small economy with high economic growth potential, albeit with vulnerability to external shocks due to its dependence on external capital to fund economic development, particularly in infrastructure investment. The country's political stability continues to be a positive factor in our rating consideration.

KEY RATING CONSIDERATIONS

GDP growth could shrink to 1% in 2020

The COVID-19 pandemic has pushed the global economy into recession. As a small economy that depends on exports of natural resources and tourism, Lao PDR cannot escape the fallout of the pandemic. We forecast the gross domestic product (GDP) growth of Lao PDR will shrink to around 1% in 2020, from an estimated 5.4% in 2019. We also expect the country's trade and services deficits to widen in 2020. We project service receipts from tourism to drop sharply, while private investment and domestic consumption to slow down significantly, and exports of hydropower to fall short of targets due to the drought that has hindered hydropower generation.

Rise in fiscal deficit and government debt

Fiscal deficit in 2018 was 4.4% of GDP. We estimate the Lao government's revenues will increase by 7% in 2019, whereas fiscal expenditure will increase by 6% in US dollar terms. The rise in expenditure is driven mainly by rising public investment for ongoing projects. Based on that, we expect a wider fiscal deficit in 2019, funded by government debt. The government debt will inevitably sustain at a high level, around 57% of GDP in 2019, and is likely to reach 60% of GDP in 2020. The broadening of the tax base and the completion of hydropower and other productive government investment projects will help on the revenue side and reduce the government's dependency on external sources of funds in the long term. But these benefits will take many years to materialize.

Continual rise in external debt

With limited domestic liquidity and the need to fund ongoing public investment projects, we expect the country's external debt will continue rising. The external public debt of the Lao PDR is expected to rise to over US\$9.9 billion by the end of 2019, up by 4% from US\$9.5 billion in 2018. The ratio of external public debt to GDP is projected to reach 55% in 2020, up from about 52% in 2018 and 2019. We estimated the country's total external debt, both public and private, to rise to nearly US\$16 billion in 2019, accounting for about 82% of GDP.

External public debt made up mostly of bilateral and multilateral loans

Bilateral loans, most of which are long-term amortized project loans related to government infrastructure investments, accounted for 61% of total external debt (US\$9.94 billion) at the end of 2019. More than 50% of total external public debt, including multilateral and bilateral loans, is owed to Chinese creditors. At the same time, the Lao PDR's outstanding bonds issued in Thailand's bond market amounted to US\$1.44 billion, accounting for 14.5% of total external public debt in 2019. A total of approximately US\$248 million in Thai bonds obligations will mature in June (approximately US\$160 million) and October 2020.

Heavy debt servicing burden over the next five years

We estimate the Lao government will be facing scheduled debt servicing obligations of around US\$1 billion per annum during 2020-2025. That will likely put a lot of strain on the government's fiscal position given the slow pace of improvement on the revenue side. We expect the Lao government to source external bilateral loans and bond issuance in international debt capital markets to refinance its debt obligations in the medium term.

Persistently low foreign exchange reserves

According to the Bank of the Lao PDR (BOL), the Lao PDR's official foreign exchange reserves at the end of 2019 were US\$997 million, up by 14% from US\$873 million in 2018, and equivalent to just 1.8 months of imports, the lowest among the countries in the Association of Southeast Asian Nations (ASEAN). The average official foreign exchange reserves were US\$938 million during 2015-2019. The weakness in foreign currency reserves is likely to persist for many years to come, given the country's deteriorating current account position and the need for external debt services. The country's ratio of external public debt services to foreign exchange reserves surged to 73.8% in 2018 and to an estimated level of 75% in 2019, from 43.7% in 2017. Looking forward, we project the ratio could rise over 75% in 2020.

Pressure on the LAK

The Lao Kip (LAK) has been on a depreciating trend since 2017. The LAK stood at Kip8,861 to the US dollar in 2019, depreciating by 3.9% from Kip8,530 at the end of 2018. We expect the LAK to continue its fall in 2020 due to the weakening external position. Given the size of the country's external debt, a weakening LAK will put further strain on its debt servicing burden.

RATING OUTLOOK

The "negative" outlook reflects TRIS Rating's view regarding the increasing strain of the Lao PDR's debt servicing burden over the next 12 to 24 months, caused by the country's weakening economy as a result of the COVID-19 fallout, deteriorating external position, persistently low foreign currency reserves, and the continued depreciation of the LAK.

RATING SENSITIVITIES

The rating downgrade will be considered in a scenario of a materially worsening trend in foreign exchange reserves and/or a weakening ability of the Lao PDR to service external debt over the next 12 to 24 months.

On the contrary, a revision of the rating outlook to "stable" will depend on how well the Lao government manages its debt obligations over the next three years, a positive trend on foreign exchange reserves, and improvement in fiscal deficits on a sustainable basis.

COUNTRY OVERVIEW

The Lao PDR is the smallest economy in ASEAN. In 2018, the Lao PDR's GDP was approximately US\$18.14 billion, according to the BOL. The GDP in 2019 is estimated to grow by 5.4%. The Lao PDR's economy trailed in size the economies of Myanmar, Cambodia, and Brunei Darussalam. However, the Lao PDR is among the fast growing GDP per capita economies, due to an average GDP growth rate above 6% per annum during 2017-2018, before slower to 5.4% in 2019. The Lao PDR's GDP per capita was projected to be US\$2,732 in 2019, growing by 5% from US\$2,599 in 2018.

The Lao PDR has abundant natural resources, such as copper, gold, and lignite. The Lao PDR has positioned itself as the "Battery of Asia" as it has plenty of water resources suitable for generating power. Electricity exports to neighboring countries have been an important part of the revenues of the Lao government.

KEY ECONOMIC INDICATORS OF LAO PDR

	2015	2016	2017	2018	2019P
GDP (US\$ million)	14,363	15,916	16,964	18,142	19,357
GDP per capita (US\$)	2,226	2,408	2,467	2,599	2,732
Real GDP growth rate (%)	7.3	7.0	6.9	6.4	5.4
GDP per capita growth rate (%)	14.2	8.2	2.5	5.4	5.1
Government revenue (US\$ million)	2,669	2,603	2,768	2,810	3,009
Government revenue (% growth)	4.8	(2.5)	6.4	1.5	7.1
Government revenue (% of GDP)	20.2	16.4	16.3	15.5	15.5
Government revenue from tax (% of total revenues)	66.3	77.3	74.8	71.1	70.7
Government revenue from non-tax (% of total revenues)	11.4	13.7	15.5	19.9	21.2
Grant (% of total revenues)	22.3	9.0	9.7	10.0	8.1
Government expenditures (US\$ million)	3,755	3,426	3,706	3,615	3,836
Government expenditures (% growth)	13.58	(8.8)	8.2	(2.5)	6.1
- Current expenditures (% of total expenditures)	58.8	71.8	57.5	62.6	65.6
- Capital expenditures (% of total expenditures)	41.2	28.2	42.5	37.4	34.4
Government budget balance (deficit)(% of GDP)	(5.9)	(5.2)	(5.6)	(4.4)	(4.8)
Government external debts (US\$ million)	6,656	7,381	8,729	9,548	9,936
Government external debts (% of GDP)	46.3	46.4	51.5	52.6	51.3
Government external debts (% growth)	16.3	10.9	18.3	9.4	4.1
Government external debt services (US\$ million)	254	371	444	644	750
Government external debt services (% of foreign exchange reserves)	25.7	45.6	43.7	73.8	75.2
External Debts (US\$ million)	10,839	12,813	14,189	15,501	15,936
External Debts (% of GDP)	75.5	80.5	83.6	85.4	82.3
Net external debts (% of Current account receipts)	203.5	220.8	216.6	215.2	206.8
Balance of payments (US\$ million)	171	(172)	201	(143)	124
Official foreign exchange reserves (US\$ million)	987	815	1,016	873	997
Official foreign exchange reserves as months of imports (Months)	2.1	1.8	2.2	1.7	1.8

Sources: 1) Bank of Lao (BOL)
2) Ministry of Finance of Lao (MOFL)
3) Estimation of TRIS Rating

P = Projection

RELATED CRITERIA

- Sovereign Credit Rating, 8 October 2013

Lao People's Democratic Republic (Lao PDR)

Sovereign Rating:	BBB
Issue Ratings:	
MOFL206A: Bt5,000 million senior unsecured bonds due 2020	BBB
MOFL200A: Bt2,791.30 million senior unsecured bonds due 2020	BBB
MOFL21NA: Bt1,870.50 million senior unsecured bonds due 2021	BBB
MOFL21NB: Bt1,767.80 million senior unsecured bonds due 2021	BBB
MOFL22OA: Bt1,019.80 million senior unsecured bonds due 2022	BBB
MOFL23NA: Bt1,063.80 million senior unsecured bonds due 2023	BBB
MOFL23NB: Bt2,546.50 million senior unsecured bonds due 2023	BBB
MOFL24OA: Bt340.90 million senior unsecured bonds due 2024	BBB
MOFL256A: Bt6,000 million senior unsecured bonds due 2025	BBB
MOFL26NA: Bt1,371.50 million senior unsecured bonds due 2026	BBB
MOFL27OA: Bt2,967.00 million senior unsecured bonds due 2027	BBB
MOFL28NA: Bt1,891.30 million senior unsecured bonds due 2028	BBB
MOFL28NB: Bt532.50 million senior unsecured bonds due 2028	BBB
MOFL29OA: Bt1,505.50 million senior unsecured bonds due 2029	BBB
MOFL30NA: Bt2,153.20 million senior unsecured bonds due 2030	BBB
MOFL32OA: Bt5,375.50 million senior unsecured bonds due 2032	BBB
MOFL25DA: US\$162 million senior unsecured bonds due 2025	BBB
MOFL27DA: US\$20 million senior unsecured bonds due 2027	BBB
Rating Outlook:	Negative

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