Chapter 10

Challenges, Prospects and Strategies for CLMV: The Case of Cambodia

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Chapter 10

CHALLENGES, POROSPECTS AND STRATEGIES FOR CLMV DEVELOPMENT: THE CASE OF CAMBODIA

Chap Sotharith

ABSTRACT

After achieving peace and national reconciliation through the 1991 Paris Accord and the 1993 General Election, Cambodia has enjoyed macroeconomic and political stability for the past 10 years. Though starting from a very low base, Cambodia is considered one of the fastest-growing economies in the region with a double-digit growth for the past five years. Many reforms have been well underway for its successful transformation, from a country in intense conflict to a country in postwar reconstruction committed to peace-building and democratic reforms. However, the development challenges persist, including high poverty rate, wide income gap, low production base, and poor human resources. The country remains poor and governance weaknesses limit both critical spending and the environment for broad-based development. Growth has been narrowly based on garment exports and tourism. This paper explores the challenges, prospects, and strategies for Cambodia to narrow the development gap in the age of regional integration and globalization.

1. INTRODUCTION

Throughout her long history, Cambodia has experienced many regime changes, including coup, political strife, civil war, and genocide, which resulted in the destruction of social and economic infrastructures. With the 1991 Paris Peace Accord and the 1993 General Election, Cambodia has regained full political legitimacy, undertaking various reforms to change from a planned to a market economy and has become a member of the Association of South East Nations (ASEAN) in 1999 and the World Trade Organization (WTO) in 2004.

Cambodia has enjoyed macroeconomic stability in recent years, underpinned by prudent fiscal and monetary policies. Though starting from a very low base, Cambodian economy is considered one of the fastest-growing economies in the region, with a double-digit growth for the past five years and remarkable macroeconomic stability. Though unemployment and underemployment still exist, the economy has successfully created new jobs to absorb the rising working-age population, which has been growing faster than the population at three percent annually.

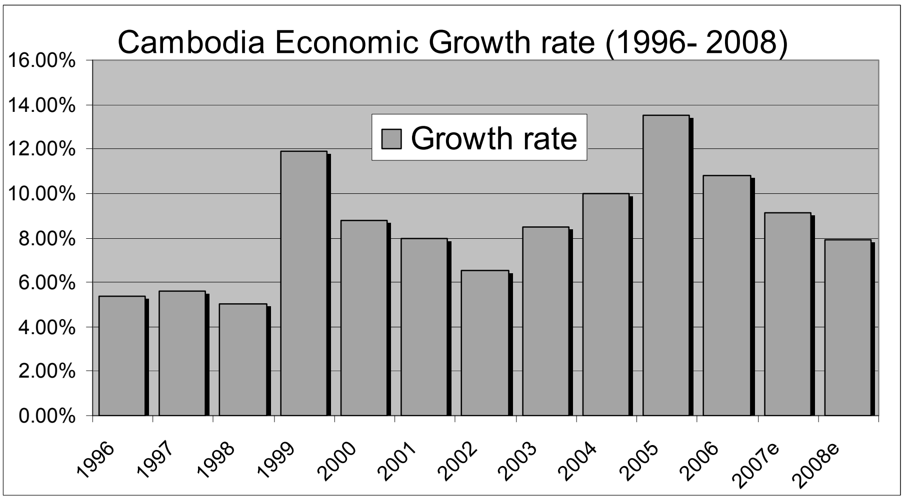
Many reforms have been well underway for its successful transformation, from a country in intense conflict to a country in postwar reconstruction committed to peace-building and democratic reforms, including economic rehabilitation especially in the new age of globalization. Nevertheless, Cambodia is still facing a huge challenge in fighting poverty, narrowing gaps in wealth among its people as well as development gaps within regions of the country, both in the rural and urban areas.

2. DEVELOPMENT TREND AND ISSUES

2.1 Macroeconomic situation

After achieving full peace in 1999, the Cambodian economy has become more resilient and dynamic despite major challenges faced by the regional and global economy and the unfavorable natural disasters in the country. For the period 2000-2006, it has achieved an average growth of approximately 9.4 per annum. In particular, during the last three years, economic growth reached unprecedented double-digit rates of 11.4 percent per year on the average, with 2005 as its peak year for reaching 13.5 percent. In 2006, economic growth was 10.8 percent and is projected to be 9.5 percent in 2007. The average per capita income almost doubled from US$288 in 2000 to US$513 in 2006. Inflation has been kept low at an average of below three percent between 2000 and 2006 (Source: Prime Minister Hun Sen's Speech at the 1st Cambodia Development Cooperation Forum, Phnom Penh, 19 June 2007). The exchange rate has been broadly stable at around 4,050 riels per US dollar. During the same period, the country's international reserves doubled from about US$500 million in 2000 to more than US$1 billion in 2006 or about three months of imports. Inflation will continue to be maintained under a five percent rate and the exchange rate will be stable.

Figure 1: Cambodia Economic Growth Rate (1996-2008)



Source: Hang (2007)

With the future oil and gas revenue expected to start in 2009 and the expansion of regional economic cooperation, Cambodia has a potential to achieve growth and poverty reduction, which will help narrow the development gap among the ASEAN member countries.

Nevertheless, at present, the economy has withstood pressures from high world oil prices, albeit with a small deterioration in the balance of payments. The external debt burden has eased to 51 percent of GDP in 2005, from a peak of 60 percent in 2003. The country remains poor and governance weaknesses limit both critical spending and the environment for broad-based development. Growth has been narrowly based on garment exports and tourism and thus while the overall poverty rate has declined—from 47 percent in 1993 to 35 percent in 2004—rural poverty remains persistently high, and many Millennium Development Goals appear beyond reach. Low revenue has led to development spending shortfalls while corruption has contributed to poor government operations and high costs of doing business (Source: IMF http://www.imf.org/external/np/ sec/pn/2006/pn0678.htm).

Largely because of exceptionally favorable weather conditions, following a drought in 2004, agriculture output grew by around 17 percent. Contrary to earlier concerns of a large negative impact of the termination of the Multi-Fibre Agreement quotas, with the introduction of safeguard restrictions put in place for China by the United States and the European Union, garment exports continued to expand in 2005, albeit at a slower pace. After increasing by 50 percent in 2004, tourist arrivals rose by 35 percent in 2005 to nearly 1.5 million with a related increase in construction activity.

Fiscal policy was cautious, as expenditure restraint and slower donor project execution led to a decline in the overall deficit to 3.5 percent of GDP in 2005, from 4.75 percent in 2004. The deficit was again more than financed by external aid. Despite greater than budgeted tax revenues and one-off receipts from the privatization of a state bank, the revenue-to-GDP ratio in 2005 was only 10.5 percent. Expenditure declined as a share of GDP as capital spending continued its downward trend—in line with external financing—and current spending grew only moderately.

Financial intermediation continued to expand, in the context of extremely high dollarization. Broad money and bank deposits grew by about 16 percent (year-on-year) in 2005 and have picked up pace in early 2006. The banking system, however, remains relatively undeveloped and concentrated, financial intermediation remains low, and private sector credit averaged less than 10 percent of GDP in 2005, allocated mainly to the services and retail sectors.

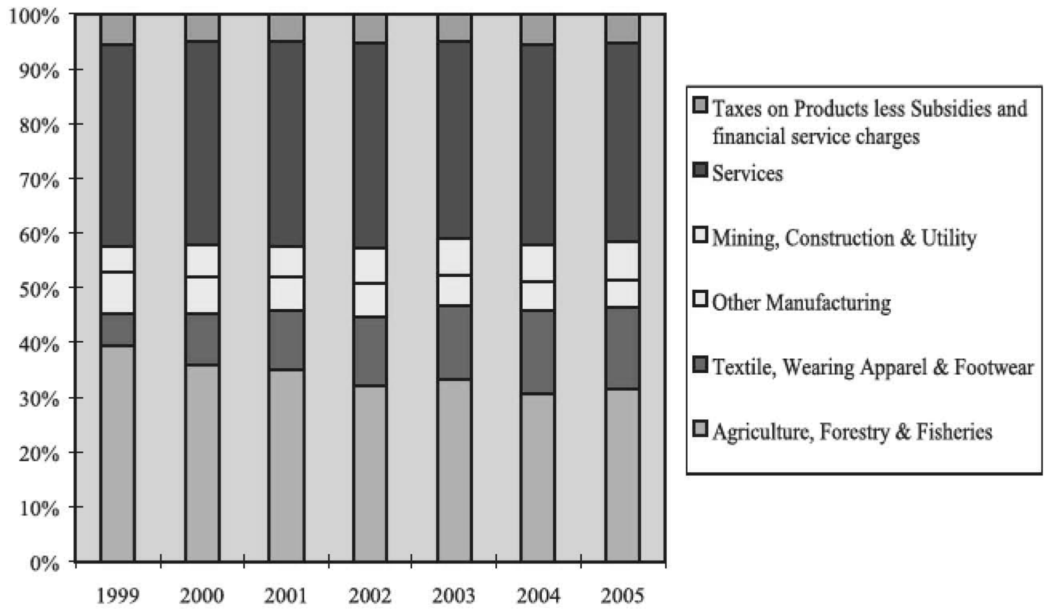
External developments were mixed. Robust tourism earnings and tourism only partly offset higher petroleum prices and strong nongarment imports. The current account deficit (excluding transfers) widened to 9.5 percent of GDP in 2005, but this was financed by an upswing in foreign direct investment (FDI), which was concentrated on the garment, tourism, and construction sectors. The riel was fairly stable both in terms of dollars and partner country currencies.

Progress has been made on the wide-ranging structural reform agenda. The authorities are implementing their flagship Public Financial Management (PFM) reform program, which addresses the weaknesses of Cambodia's public expenditure management system. In the area of land policy, the issuances of subdecrees on economic land concessions and on state land management were significant developments.

2.2 Economic Structure

Cambodia's economy is based mainly on garment export, services (in which tourism is the biggest part), and agriculture. The composition of real GDP is shown in Figure 2. Comparing real GDP composition in 1999 and 2005, the most distinctive change found is the drop in the share of agriculture, from 39.4 percent to 31.4 percent, while that of manufacturing has seen a rapid growth, from 18.0 percent to 27.0 percent (Council for the Development of Cambodia 2006).

Figure 2: Composition of GDP by Industry



Source: CDC (2006).

Growth of agriculture gross value added (GVA) increased by 28 percent, the highest agriculture sector production on record. This stellar performance was attributable to excellent weather conditions, improved irrigation, and increased acreage under cultivation. Fisheries GVA increased by 5.6 percent, and livestock and poultry GVA grew by 5.8 percent. Forestry GVA increased by 5.4 percent, with logging for domestic use being partly offset by the decrease in illegal logging for export.

As for industry, garment (and apparel) has drastically increased in share from 5.9 percent to 14.9 percent, becoming the single dominant manufacturing subsector of Cambodia. The industry sector grew by 12.1 percent in 2005, accounting for 27 percent of total GDP in constant 2000 prices. It should be noted that the share held by industry declined in 2005 owing to the exceptional growth in agriculture and services, which grew at the same rate as industry. The main contributors to the growth of the industrial sector were garment manufacturing and construction. Textiles, wearing apparel, and footwear manufacturing GVA increased by 10.3 percent in 2005 (24.9% in 2004 and 16.8% in 2003). However, export products under the Generalized System of Preferences, mainly manufactured garments, declined from 83 percent of Cambodia's total goods exports in 2004 to 82.4 percent in 2005 in constant 2000 prices. Construction GVA also made a large contribution to 2005 growth, increasing by 20.1 percent (13.2% in 2004 and 11.l% in 2003). Significant increases in construction of residential dwellings, hotels, and factories have been among the main contributors to the high GDP growth rates during the last four years.

The services sector has had a relatively stable share, between 36 percent and 38 percent, in recent years. It grew by 12.1 percent in 2005, accounting for 36.2 percent of total GDP in constant 2000 prices. Tourism continues to be the main contributor to growth in the services sector, with revenue from overseas tourists increasing by 33.6 percent in 2005 (50% in 2004). Hotels, restaurants, and other services directly benefit from tourism growth and infrastructure development. The number of tourists visiting Cambodia reached 1.4 million. Tourists, including visitors from overseas to Cambodia's casinos, contributed to the growth of the hotel and restaurant industry (17.3%), transport and communication (13.1%), and other services (17.7%). Tourism has forward and backward linkages with the service sector in general. Thus, the beneficiaries will not be just travel, hotel, restaurant, and tourist establishments but also enterprises engaged in retail trade, transportation, communication, and finance.

However, the comparison of industrial structure with other Southeast Asian nations, as shown in Table1, indicates that Cambodia is still at the initial stage of industrialization, together with Laos and Myanmar. These countries are still dependent on agriculture as the main sector.

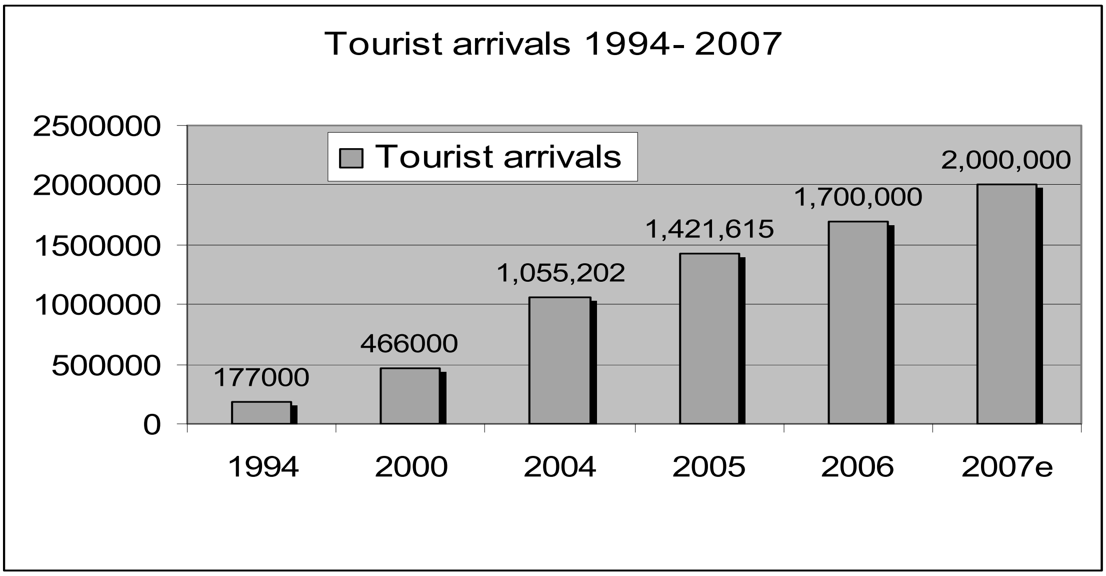
Table 1: Composition of GDP of Selected Southeast Asian Countries In 2004

	Agriculture	Industry	(Manufacturing)	Service
Cambodia	36.0	27.7	20.2	36.2
Indonesia	15.4	43.7	28.3	40.9
Laos	48.6	25.9	19.2	25.5
Malaysia	9.1	48.5	30.2	42.4
Myanmar	54.6	13.0	9.2	32.3
Philippines	15.3	31.8	23.0	52.8
Singapore	0.1	33.7	27.7	66.2
Thailand	9.9	44.1	35.2	46.0
Vietnam	21.8	40.1	20.3	38.2

Source: Asian Development Bank Key Indicators 2005.

With a great potential for tourism, especially Angkor Wat, which is regarded as one of the World's Wonders, Cambodia can use tourism as an engine of growth. Revenue from tourism amounted to more than US$2 billion in 2006 or about 20 percent of the GDP (Source: Ministry of Tourism). At 1.7 million in 2006, tourist arrivals are expected to reach 2 million in 2007, with the largest number likely to come from South Korea and Japan (See figure 3).

Figure 3: Tourist Arrivals 2004- 2007



Source: Ministry of Tourism

Progress has been made on the wide-ranging structural reform agenda. The authorities are implementing their flagship Public Financial Management (PFM) reform program, which addresses the weaknesses of Cambodia's public expenditure management system. In the area of land policy, the issuances of subdecrees on economic land concessions and on state land management were significant developments.

2.3 Trade Pattern

Cambodia's exports increased by 102 percent from 2002 to 2006 (US$1.7 billion to US$3.6 billion. Exports continued to rise at about 27.5 percent in 2006 from US$2.9 billion in 2005 due to the continued increase of textile and garment exports (Hang 2007, p.22). Garment exports increased by 18.2 percent from US$2.2 billion in 2005 to US$2.6 billion in 2006. Garment exports accounted for 75.7 percent of total export in 2006, followed by paper and pulp (18.6%) (Table 2). Cambodia's trade deficit is about US$1 billion in 2006 (Chap 2007, p.15).

Though Cambodia is an agricultural country, trade in agriculture is conducted mainly within Cambodia. It exports garment and textile products and some primary agro-product such as paddy, rice, rubber, raw fish, maize, and others. In 2006, export in agriculture covered only about one percent of total export, and was dominated by textile and apparel products (see Table 2).

The current underperformance of agricultural exports in Cambodia is the result of several problems such as high cost of production, processing, and transportation, lack of a developed marketing and postharvest system, difficulty in procurement of raw materials, widespread corruption practices, an underdeveloped financial system, and the lack of certification for Cambodian products (Ministry of Commerce 2001). In spite of all these constraints, export potential is still present and could be seized if adequate institutional, policy, and investment measures are set in place. The potential of export

Table 2: Comparison of Cambodia Export 2002 and 2006

Chapter	Section	2002 ($)	2006 ($)	% change	% of 2006

5-Jan	Live Animal	6,080,158	6,273,395	3%	0.2%
14-Jun	Vegetable Products	5,568,898	11,262,225	102%	0.3%
15	Fats and Oils	5,549	1,152,871	20677%	0.0%
16-24	Prepared Foodstuffs	3,985,993	9,485,156	138%	0.3%
25-27	Mineral Products	14,386	2,290	-84%	0.0%
28-38	Chemicals	440,259	1,404,812	219%	0.0%
39-40	Plastics	29,641,234	50,502,456	70%	1.4%
41-43	Hides and Leather	1,571,501	2,384,672	52%	0.1%
44-46	Wood and Wood articles	15,906,674	10,132,098	-36%	0.3%
47-49	Pulp and paper	423,231,534	662,468,337	57%	18.6%
50-63	Textiles and apparel	1,206,864,927	2,700,415,433	124%	75.7%
64-67	Footwear	41,963,995	67,661,560	61%	1.9%
68-70	Stone/Cement/Ceramics	32,238	1,281,611	3,876%	0.0%
71	Gems	16,525,788	15,880,087	-4%	0.4%
72-83	Base metal and Metal articles	1,141,799	4,161,898	265%	0.1%
84-85	Machinery and Electrical Appliances	7,778,520	18,242,805	135%	0.5%
86-89	Vehicles	5,466,119	582,316	-89%	0.0%
90-92	Optical, precision & musical instruments	996,637	1,010,408	1%	0.0%
93	Arms	9,250	106,321	1,049%	0.0%
94-96	Miscellaneous Manufactured articles	1,635,521	4,648,143	184%	0.1%
97-98	Antiques and works of art	287,352	376,385	31%	0.0%
	Total	**1,769,148,331**	**3,569,435,279**	**102%**	**100.0%**

Source: Using Data provided by Ministry of Commerce.

already exists in the case of high-quality rice, fishery products, live cattle, soybean, maize, rubber, sesame, and pepper.

Lack of processing plants for agro-products, lack of access to market information, and poor-quality agricultural commodities are among the biggest challenge. High domestic cost, poor infrastructure, administrative inefficiencies, and lack of investment in processing capacity all discourage formal trade. Farmers and wholesalers often take the easiest option—selling to traders from neighboring markets who are able to bear the informal costs of moving commodities out of Cambodia for processing and onward sales. The regulatory reforms that WTO membership requires, and preferential market access, should improve the situation. The global trading environment, however, is improving only gradually under WTO rules. High tariff barriers, poor quality of goods, and food safety requirements will need to be understood to take advantage of new opportunities (Ministry of Commerce and Mekong Private Sector Development Facility 2005).

2.4 Foreign Direct Investment

Information from the Council for the Development of Cambodia (CDC) shows that FDI inflows to Cambodia have been very high. Cambodia attracted about US$924 million per year from 1994 to 2007. The peak years were 1995 and 2006.

From 1998 to 2006, the actual FDI inflow to Cambodia was recorded at about US$222 million per year compared to US$1.6 billion that went to Vietnam, US$5.6 billion received by Thailand, US$3.47 billion that went to Malaysia, and US$14.4 billion given to Singapore. However, Cambodia received more FDI than Lao PDR, which received only US$47.9 million per year during the same period (see Table 4). The biggest parts of FDI are from China, Korea, and other countries in the region.

Table 3: Proposed FDI in Cambodia (1994- 2007)

Year	**FDI**	**% increase**	**Projects**	**Capital per Project**
1994	505,698,494	100	26	19,449,942
1995	2,242,890,373	344%	124	18,087,826
1996	766,662,160	-66%	188	4,077,990
1997	744,510,560	-3%	205	3,631,759
1998	853,924,698	15%	144	5,930,033
1999	356,655,269	-58%	91	3,919,289
2000	218,037,881	-39%	61	3,574,391
2001	204,683,613	-6%	39	5,248,298
2002	235,602,572	15%	32	7,362,580
2003	251,233,736	7%	47	5,345,399
2004	210,440,247	-16%	52	4,046,928
2005	962,378,619	357%	91	10,575,589
2006	3,467,851,384	260%	86	40,323,853
2007*	1,925,728,571	-44%	90	21,396,984
Total	**12,946,298,177**		**1,276**	
Average	**924,735,584**			

Source: CDC database

*Note: * From January to September 2007*

Table 4. Comparison of FDI in ASEAN (1998- 2006)

(million of USD)

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average 1998-2006
Brunei	573.3	747.60	549.20	526.40	1,035.30	3,123.00	212.01	288.54	433.50	832.09
Cambodia	242.9	232.30	148.50	149.40	145.10	84.00	131.38	381.22	483.24	222.00
Indonesia	-356	- 2,745.10	- 4,550.00	- 3,278.50	144.70	- 595.60	1,894.50	8,335.98	5,556.24	489.58
Lao, PDR	45.3	51.60	34.00	23.90	25.40	19.50	16.92	27.73	187.40	47.97
Malaysia	2,714.00	3,895.10	3,787.60	553.90	3,203.40	2,473.20	4,623.89	3,964.79	6,059.73	3,475.07
Myanmar	683.4	304.20	208.00	192.00	191.40	291.20	251.13	235.85	142.96	277.79
Philippines	1,718.00	1,725.00	1,345.00	982.00	1,111.00	319.00	687.80	1,854.00	2,345.01	1,342.98
Singapore	7,594.30	16,067.40	16,485.40	14,121.70	5,821.30	9,330.60	19,827.50	15,001.90	24,055.40	14,256.17
Thailand	7,491.20	7,491.20	3,350.30	3,886.00	947.00	1,952.00	5,862.00	8,957.00	10,756.06	5,632.53
Viet Nam	1,700.00	1,483.90	1,288.70	1,300.30	1,200.10	1,450.10	1,610.10	2,020.81	2,360.00	1,601.56

Source: ASEAN Statistical Year Book 2005 and ASEAN Website: http://www.aseansec.org/Stat/Table25.xls

Table 5. Comparison of GDP of ASEAN Countries

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006
Brunei	3,865	4,190	4,315	4,176	5,847	6,540	7,864	9,528	11,551
Cambodia	3,027	3,427	3,546	3,702	4,028	4,634	5,311	6,250	7,257
Indonesia	97,808	140,787	150,567	143,602	204,499	237,663	251,647	280,265	364,259
Lao, PDR	1,286	1,451	1,733	1,754	1,805	2,135	2,518	2,860	3,522
Malaysia	72,237	79,149	90,320	88,001	95,266	103,992	124,750	137,180	156,924
Myanmar 2/	6,953	9,275	10,549	8,281	7,095	11,747	10,585	11,169	11,950
Philippines	65,548	76,076	74,837	71,985	76,648	79,578	86,912	98,757	117,457
Singapore	81,940	81,414	91,429	84,909	88,106	92,372	107,464	116,639	132,273
Thailand	112,751	122,698	122,969	115,601	126,880	142,863	161,386	176,207	206,645
Viet Nam	27,209	28,677	31,319	32,647	35,066	39,535	45,544	52,953	60,965

Source: ASEAN Statistical Year Book 2005 and ASEAN Website: http://www.aseansec.org/Stat/Table5.xls

Table 6. Comparison of FDI per GDP of ASEAN Countries

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average 1998-2006
Brunei	14.8%	17.8%	12.7%	12.6%	17.7%	47.8%	2.7%	3.0%	3.8%	14.8%
Cambodia	8.0%	6.8%	4.2%	4.0%	3.6%	1.8%	2.5%	6.1%	6.7%	4.9%
Indonesia	-0.4%	-1.9%	-3.0%	-2.3%	0.1%	-0.3%	0.8%	3.0%	1.5%	-0.3%
Lao, PDR	3.5%	3.6%	2.0%	1.4%	1.4%	0.9%	0.7%	1.0%	5.3%	2.2%
Malaysia	3.8%	4.9%	4.2%	0.6%	3.4%	2.4%	3.7%	2.9%	3.9%	3.3%
Myanmar 2/	9.8%	3.3%	2.0%	2.3%	2.7%	2.5%	2.4%	2.1%	1.2%	3.1%
Philippines	2.6%	2.3%	1.8%	1.4%	1.4%	0.4%	0.8%	1.9%	2.0%	1.6%
Singapore	9.3%	19.7%	18.0%	16.6%	6.6%	10.1%	18.5%	12.9%	18.2%	14.4%
Thailand	6.6%	6.1%	2.7%	3.4%	0.7%	1.4%	3.6%	5.1%	5.2%	3.9%
Viet Nam	6.2%	5.2%	4.1%	4.0%	3.4%	3.7%	3.5%	3.8%	3.9%	4.2%

Source: Table 4 and Table 5

It is very difficult to compare the FDI inflow among countries with different sizes of economies. One US$ billion invested in Thailand is quite different with the same amount invested in Cambodia. To be fair, FDI can be measured by using FDI per GDP as the basis for comparison. Using the figures of FDI in ASEAN countries (Table 4) and the GDP in ASEAN countries (Table 5), the result is presented in Table 6.

Based on this method, Cambodia was the third highest FDI recipient in the ASEAN, next to Brunei and Singapore from 1998 to 2006. In Cambodia, FDI covers 4.9 percent of the GDP compared with 14.8 percent in Brunei and 14.4 percent in Singapore (see Table 6).

The figures received from the official documents of the CDC only indicate registered capital or pledges made by investor to make the project look attractive for incentives. The investors may exaggerate the amount of investment capital in their applications to gain better incentives from the government as the policy states that the more investment capital is made, the more incentive the government will offer. No data were available on actual or realized FDI from the CDC (Chap 2005, p.37).

Some investors were in a hit-and-run position with money laundering and speculation for a quick profit. “Sincere” investors also face problems with uncertainty of risks and hesitation to invest in the country. Many middlemen (intermediaries) who have a close link with the Government are involved in corruption to get licenses and concessions, especially for the exploitation of natural resources (forestry, mining, etc). They sell the licenses for a profit, or delay or cancel them completely if they could not find potential buyers.

3. ECONOMIC DEVELOPMENT POLICY

3.1 Five-Year Plans

Cambodia has implemented its five-year plans, namely: first Socio-Economic

Development Plan, SEDP I (1996-2000); second Socio-Economic Development Plan, SEDP II (2001-2005); and the third five-year plan, whose name has been changed to National Strategic Development Plan, NSDP (2006-2010). The third five-year plan, NSDP, focuses on the following three main points: (1) to speed up and ensure sustainable economic growth of 6-7 percent per annum; (2) to implement population policy adopted by the Royal Government by focusing on birth spacing and ensuring the quality and health of human resources; and (3) to rigorously implement governance reform especially corruption eradication to equally distribute economic outcome (Royal Government of Cambodia 2006). The NSDP has integrated many policy instruments such as Rectangular Strategy, 73-point Government Political Agenda, Cambodian Millennium Development Goal, and National Poverty Reduction Strategy.

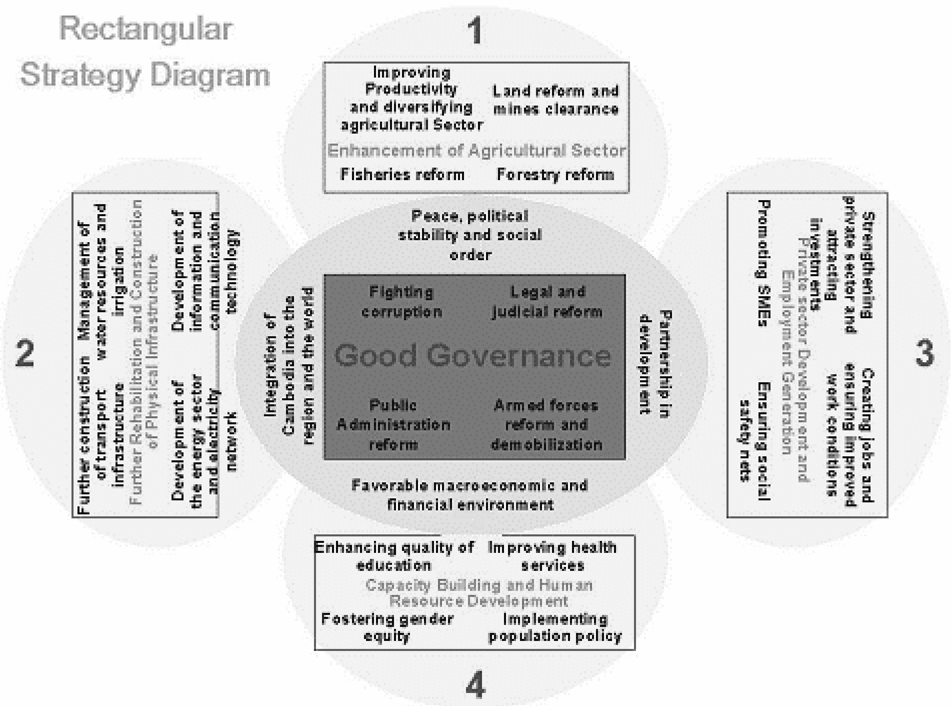
3.2 Development Strategies

The Government of the second legislative (1997-2003) used a political strategy called the *triangular strategy* (1997-2003) consisting of political stability, economic integration, and poverty reduction. The present Government (2003-2008) is implementing the so-called "Triangular Strategy" with the motto of "for growth, employment, equity, and efficiency."

The rectangular strategy is an integrated structure of interlocking rectangles, as follows:

First, the core of the *rectangular strategy* is good governance, focused at four reform areas: (1) anticorruption, (2) legal and judicial reform, (3) public administration, and (4) reform of the armed forces, especially demobilization. Second, the overall environment for the implementation of the rectangular strategy consists of four elements: (1) peace, political stability, and social order; (2) partnership in development with all stakeholders, including the private sector, donor community, and civil society; (3) favorable economic and financial environment; and (4) the integration of Cambodia into the region and the world. Third, the four strategic "growth rectangles" are: (1) enhancement of agricultural sector; (2) private sector development and employment generation; (3) continued rehabilitation and construction of physical infrastructure; and (4) capacity building and human resource development (see Figure 4).

Figure 4: Rectangular Strategy of Royal Government of Cambodia (2003- 2008)



Source: Council for Administration Reform

3.3 Regional and Global Integration

The Royal Government is committed to integrate Cambodia into the regional and global economies, specifically focusing on bridging the development gaps among member countries of the ASEAN by promoting full partnership in the implementation of the various elements of the Initiatives for ASEAN Integration as adopted by the ASEAN Summits, in particular the measures and projects adopted by the 8th Summit in November 2002 in Phnom Penh. The Royal Government will also continue its active participation in the implementation of the Greater Mekong Sub-region Program, especially the flagship programs adopted by the 1st Summit of Greater Mekong Sub-region Program in Phnom Penh in November 2002, and the projects under the "Development Triangle Zones" among Cambodia, Viet Nam, and Lao PDR, the "Development Triangle Zones" among Cambodia, Lao PDR, and Thailand, and the "Economic Cooperation Strategy" among Cambodia, Lao PDR, Thailand, and Myanmar. To maximize the gains from international integration, Cambodia must strengthen its institutional capacity to implement cooperative strategies with neighboring countries such as the concept of "Four Countries-One Economy," the creation of the triangles for economic growth, and the establishment of cross-border Economic Processing Zones (Royal Government of Cambodia 2004).

There is worldwide recognition that free trade significantly contributes to the reduction of poverty and improvement of the living standards of the people. Thus, the Royal Government will continue to liberalize trade and ensure free flow of goods and services both within the country and between Cambodia and other key partners in the region and the world. Increasing the unfettered access of Cambodian products to the regional and world markets will provide Cambodia with the economies of scale and opportunities that attract investment, create employment, generate increased incomes, and promote accelerated economic growth that will result in poverty reduction. Indeed, Cambodia's participation in the ASEAN Free Trade Area (AFTA) and accession to the WTO constitute strategic and historical steps in the rehabilitation and development of Cambodia.

The Royal Government will strictly implement its obligations under the WTO, recognizing that Cambodia's membership in the WTO requires great efforts in the formulation, adoption, and implementation of laws, regulations, procedures, and methodology for valuation, assessment report on the effects of trade protection, studies on rice production and agricultural markets, agricultural value chain analysis, handicrafts, pure drinking water, fisheries, factories, tourism, and other labor services that Cambodia can benefit from the WTO. The Royal Government is strongly committed to using this opportunity to embark on reforms in all sectors.

4. COUNTRY'S STRENGTH IN COMPETITIVENESS

(1) Competitive Advantages

Cambodia has potentials for development in many sectors such as agriculture, agro-industry, tourism, and labor-intensive industry. Cambodia is located in the fastest-growing economic region of the world in which foreign and investment interlinkages are higher than in any other developing regions. The country is also relatively richly endowed with agricultural, forest, and marine resources, and thus possesses a good foundation for a range of natural resource-based industrial processing activities.

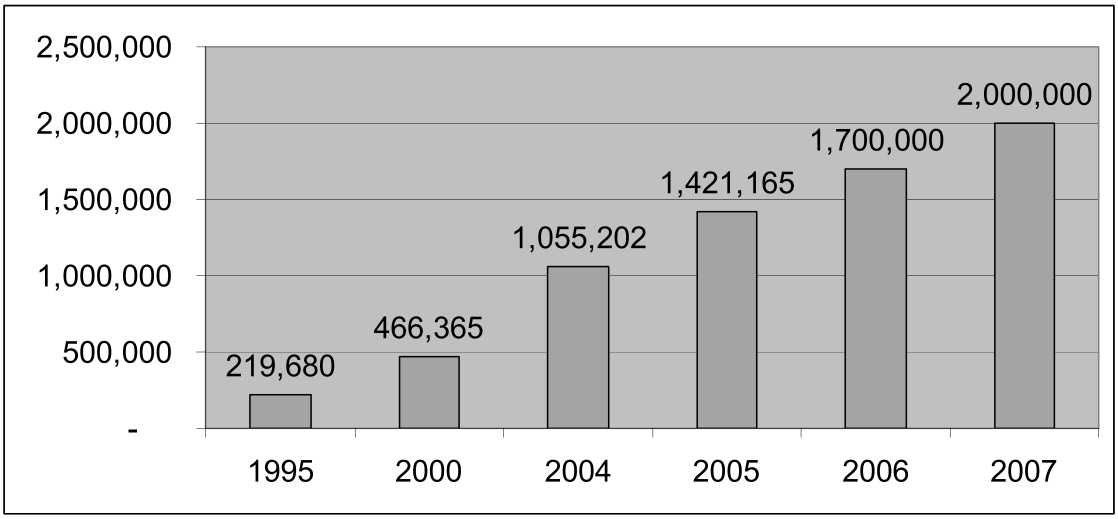
(*i*) *Potential in Agriculture*

Cambodia's economy is based on agriculture. About 85 percent of its population is dependent on agriculture, which has not been modernized yet. It depends almost completely on natural condition yet the country can still sustain food sufficiency and surplus for export. At present, the agriculture sector, which is the backbone of the Cambodian economy, has been opened for FDI. Therefore, agricultural development is a big potential for future development. Transfer of technology in agriculture will follow the flow of FDI and will contribute to agricultural modernization. With the low cost of labor, agriculture has a huge potential for attracting foreign investments into Cambodia.

(*ii*) *Potential in Tourism*

Located in Southeast Asia, where tourism is booming especially in countries like Thailand, Malaysia, and Singapore, Cambodia can catch this opportunity in tourism development by using Bangkok, Kuala Lumpur, and Singapore as regional hubs. Cambodia has an advantage in international tourism because of its historical heritage, unpolluted scenic attractions, and central location in Southeast Asia. Cambodia, the successor of the Khmer Empire and Khmer civilization, had a great influence on the cultural and artistic evolution of the region. The Angkor Temple Complex, represented

Figure 5: Tourist arrivals 1995- 2007



Source: Ministry of Tourism

by Angkor Wat and Angkor Tom, is one of the most significant cultural heritages in the world and is promising enough to develop as an international tourist destination. Other than historical heritage, the rural landscape is also an important attraction for tourists in Cambodia. The Mekong River, the Tonle Sap Lake, and the beautiful beaches in Sihanoukville and Kompot province will also attract nature tourists. Furthermore, Phnom Penh, the capital of Cambodia, is an international gateway and its French-influenced atmosphere will be enhanced for tourists after renovation of buildings and streets. Major tourist attractions in the city are the Royal Palace, the National Museum, the view of the Mekong River, and the areas surrounding with mountains, forests, lakes, and streams. The government has concentrated on three poles of tourism development (Phnom Penh, Siem Reap, Sihanoukville) by inviting national and international investment companies to develop tourism through the construction of hotels and tourist sites following international standards. This indicates that tourism is the most attractive sector for investment. At present, it can be the backbone of the economy instead of agriculture. Tourist arrivals have increased year by year with an average of about 20 percent annually from only 118,228 in 1993 to 604,919 tourists in 2001, 1,055,202 in 2004, 1,700,000 in 2006, and about 2 million in 2007 (See figure 5).

(*iii*) *Potential in Natural Resources*

Cambodia will build on its comparative advantage by developing natural-resource-based industries of different kinds, including agro-based, wood-based, fisheries-based, and industry-based (nonmetallic mineral resources). This is a big potential for attracting foreign investment. If Cambodia is successful in expanding rice production to the point where it is exporting significant quantities of rice, this will itself create employment and value added in processing. Other possibilities in agro-processing include sugar and vegetable oil processing. Products and animal feed production will need to be given more systematic economic evaluation. Moreover, the widespread rural small-scale manufacture of tobacco products suggests that further scope exists for large-scale production, yielding higher quality product and higher value added.

Oil and gas exploration recommenced in Cambodia in 1991, following earlier efforts in 1969-74, and has already produced very promising results. Altogether, 16,000 line kilometers of high-quality seismic data have been obtained, giving good geological information, which indicates the potential for substantial oil and gas generation (Royal Government of Cambodia 1997, p.156).

For the purpose of exploration, both land and sea areas of Cambodian territory have been divided into blocks, 32 altogether, of which the offshore blocks I-IV have so far been explored. Three major oil companies, with 30-year contracts, have been engaged in drilling. Positive results from drilling in Block III in late 1993 were followed by the most successful test so far, carried out in Block I and Block III in late 1993 were followed by the most successful tests so far, carried out in Block I and Block II in the first part of 1994, which produced a maximum flow rate of 4.7 m cubic feet of gas and 180 barrels of condensate per day. Another company testing in Block IV in the same year produced a maximum flow rate of 1.3 m cubic feet of gas and 1,180 barrels of oil per day (Royal Government of Cambodia 1997, p.156).,

The government now plans to offer further acreage for licensing. The licensing regime embraces royalties and a tax system, controlled by production-sharing contracts, which provide attractive terms for exploration and production projects. The successful development of oil and gas production could do much to transform Cambodia's economic situation by providing current revenues to cover the recurrent costs of social and economic development programs—the costs of which at present constitute a severe constraint—and the heavy funding required for new infrastructure development.

Although Cambodia has good mineral resources potential, events of the last two decades have prevented the development of the mineral sector. This has been compounded by factors such as scarcity of capital, high costs of exploration and exploitation, lack of expertise, and absence of effective mining laws and regulations. Potential exists with respect to gold, gemstones (ruby, sapphire, zircon), phosphates (for fertilizer), limestone (for cement and building stone), bauxite, clay, sand/gravel, and granite, with the first two as commercially most promising. Copper and zinc also exist but require more exploration work. Exploration for gold by three companies has been initiated.

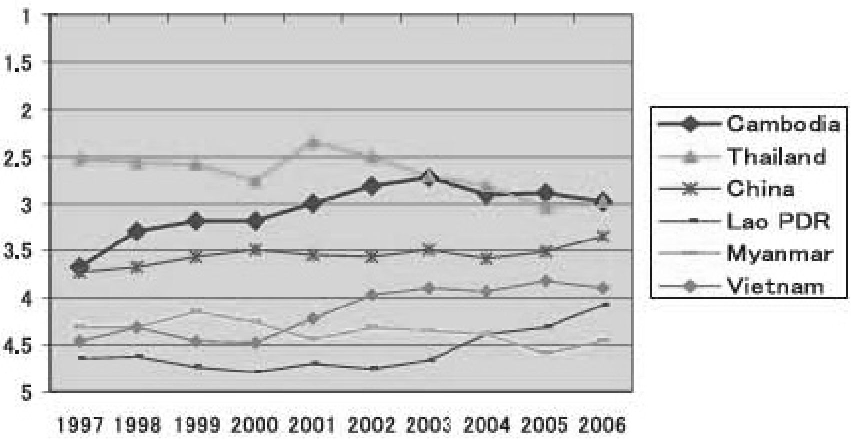
Mitsubishi Corporation and BHP Billiton have signed a mineral exploration agreement with the Royal Government of Cambodia to explore for bauxite and to evaluate the potential for an alumina refinery. The agreement requires a detailed evaluation of the Mondolkiri exploration licences in Eastern Cambodia to determine resource size and quality, environmental and community issues, risks from unexploded ordinances, and the appropriate mining, processing, and transport options. Following studies due in the first half of 2008, the partners have the exclusive rights to negotiate a mining agreement with the government to develop the project. BHP Billiotn and Mitsubishi Corp previously partnered on the Mozal aluminium smelter in Mozambique (Japan's Corporate News Network, Tokyo, 11 October 2006 at http://www.japancorp.net/Article.Asp?Art_ID=13537, accessed on 6 January 2008).

As in the case of oil, the government is in the process of developing national policy guidelines, legislations, and regulations for mining exploration and exploitation designed to provide incentives and protection to investors while also ensuring protection of the environment. Once the details are clarified, a new Mining Law will be prepared and submitted to the National Assembly for Adoption.

(2) Economic Freedom

Cambodia is classified as one of the most liberal economies in economic freedom. According to the "2006 Index of Economic Freedom" by the Heritage Foundation in the US, Cambodia ranked 9th out of 32 countries and regions in Asia in terms of absence of government coercion or constraint on economic activities. Among ASEAN countries, only Singapore is above Cambodia. Cambodia is categorized as "Most Free," in which Japan, Taiwan, and South Korea are included as well. In the last 10 years to 2006, Cambodia's index has improved, although it has been relatively flat over the last three years. The improvement in Cambodia's index is very obvious in contrast to Thailand, as shown in Figure 6 and Box 1.

Figure 6: Comparison of Index of Economic Freedom in selected countries



Source: 2005 Index of Economic Freedom by Heritage Foundation/ Wall Street Journal.

Box 1: Cambodia ranks 63 out of 161 countries (2005)

Category: Mostly Free

Score: 1- 5

- Trade policy : 4 (high level of protectionism)
- Fiscal Burden: 2,4 (lost cost of government)
- Government intervention in the economy : 2,5 (moderate level)
- Monetary policy : 1 (very low level of inflation)
- FDI : 3 (moderate barriers)
- Banking and Finance : 2 (low level of restriction)
- Wages and Finance : 2 (low level of intervention)
- Property rights : 4 (low level of protection)
- Regulation : 4 (high level)
- Informal market: 4 (high level of activity)

Source: 2005 Index of Economic Freedom by Heritage Foundation/ Wall Street Journal.

(3) Competitiveness

A study titled "Cambodia Competitiveness Report" has sought to conduct a comprehensive assessment of the country's competitiveness through the observations of top business executives on various aspects of Cambodia's economic environment, in order to eventually aggregate and analyze their perceptions on issues related to national competitiveness. The report contains three basic sets of findings. First, it details outcomes of an executive opinion survey conducted among leading business executives in Cambodia. Second, it deals with the Growth Competitiveness Index (GCI) of the World Economic Forum (WEF) in which Cambodia is compared to its competitors.

Third, Cambodia's performance is assessed within the framework of the Business Competitiveness Index of Michael E Porter (Economic Institute of Cambodia 2005).

The WEF views national competitiveness as a set of factors, policies, and institutions that determine the level of productivity of a country. Raising productivity is, according to WEF, the driving force behind the rates of return on investment, which, in turn, determine the aggregate growth rates of an economy. This means that a more competitive economy will be one that will grow faster in a medium to long-term perspective. Based on this perspective, the WEF defines three stages of economic development: factor-driven stage, efficiency-driven stage, and innovation-driven stage. With GDP per capita of about US$500, Cambodia is undoubtedly treated as a factor-driven economy that competes based on factor endowments, primarily unskilled labor and natural resources. According to the above study, Cambodia remains among the least competitive countries in the world. This year's ranking, the WEF's GCI 2006-2007, places Cambodia at 103rd among 125 countries in the assessment. The country's performance is slightly behind Bangladesh (99), but lags far beyond its neighboring countries such as Thailand (35), Indonesia (50), China (54), and Vietnam (77). Switzerland is the world's most competitive country, while Angola is at the bottom of the WEF's GCI 2006-2007 (Economic Institute of Cambodia 2006).

However, the above study was not positively received by the Government as it is said to be creating a negative image for the country. The Government reasoned that the study is giving an inaccurate picture of Cambodia because in reality, there are booming businesses by local and foreign investors and business persons, especially in the construction and services sectors, and more increasing inflow of FDI to Cambodia, especially from China, Korea, and other countries in the region.

(4) Credit Rating

For the first time in history, the Royal Government of Cambodia assigned the Credit Suisse to act as its rating advisor in coordinating a sovereign credit rating. Cambodia has secured a B+ rating for long-term foreign and local currency government bonds from Standard & Poor's and B2 ratings for foreign currency and local currency government bonds from Moody's. The outlook for all ratings is stable. According to Agost Bernad, Standard & Poor's primary credit analyst:

> *"Real GDP growth averaging 9% over the past six years boosted per-capita GDP by 64%. There is reason to expect similar robust growth performance in the medium term, given the policy continuity, which focuses on export-led growth and stability in price and exchange rates."*

Meanwhile, Standard & Poor's recognized Cambodia's track record of strong economic growth and the underlying prudent macroeconomic policy mix, as well as the ongoing donor engagement that provides a policy anchor and underpins domestic and external liquidity. Moody's Vice President Thomas Byrne notes:

> *"Cambodia has recently attracted significant inflows of foreign direct investment into sectors such as tourism, garments and energy, which should*

> *help to continue to boost the overall level of investment in the economy as well as to strengthen the balance of payments"* (Government and Credit Suisse Press Release, May 2007).

According to its press release, Moody's acknowledged that such inflows, coupled with steady disbursements of concessional official development assistance, have offset current account deficits and have contributed to a build-up in official foreign exchange reserves to a level that is adequate in relation to the country's near-term debt repayments, thereby providing some buffer to external shocks. Moody's expects that improved competitiveness in the garment sector, continued growth in tourism, and a timely, well-managed development of Cambodia's relatively large proven reserves of oil and gas would strengthen the fiscal and external payment positions of Cambodia. Moody's also gave credit to Cambodia's stable political system and noted that continued institutional improvement should improve the country's investment climate and thereby boost long-term economic growth.

Standard & Poor's assigned a short-term foreign and local currency rating of B. Moody's also assigned a foreign currency bond ceiling of B1, a foreign-currency ceiling for bank deposits of B3, a local currency bond ceiling and a local currency deposit ceiling of Ba1.

This positive rating has opened the way for Government in issuing commercial bonds both in local and foreign currency to mobilize money in financing government projects in addition to the bilateral and concession loan that is tied to many conditions.

It has also helped in improving investor confidence in Cambodia and in showing Cambodia's financial health.

5. CHALLENGES

(1) Poverty

Though the decline in poverty has been significant and widespread due to the rise in average per capita consumption, Cambodia is still facing a major challenge in having a high poverty rate. Within the geographical sampling of the first survey, the headcount fell from 39 to 28 percent. Backward projection based on this observed trend suggests that the national poverty rate fell by 10-15 percent over the last decade (from 45-50 percent in 1993/4 to 35 percent in 2004). Moreover, poverty is very likely to have fallen further in 2005 and 2006 due to the exceptionally high growth rates in those years, especially in agriculture. Projections put the poverty rate at about 32.5 percent in 2006 (Hang 2007, p. 2).

(2) Inequality

Cambodia is facing a growing tendency to exacerbate the inequality between the rich and the poor, and aggravate the regional disparity between urban and rural areas. Due to lack of social safety net and protection, the poor are very vulnerable to fall into a higher poverty status. Among the areas, Phnom Penh is the fastest developing urban area due to the availability of infrastructure and public utilities, and land concentration.

(3) Insufficient Infrastructure

Due to a long protracted war, international isolation, and political strife, the infrastructure in Cambodia is still in poor condition compared to other countries in the region. At present, Cambodia does not have sufficient financial, technical, and human resources that are necessary for infrastructure construction. Inadequate physical infrastructure, including road transportation, electricity, irrigation and water systems, and port facilities, is a major barrier to economic development and poverty reduction in Cambodia. Hence, infrastructure networks can be assigned a leading role in supporting the development process. Overcoming this bottleneck involves considerable investment, capacity building, new policies, and institutional reform.

(4) Land Dispute

Though Cambodia has a low density of population per land compared to many countries in the region, land becomes scarce as the demand for investment and agriculture increasingly rise. Because land is more expensive due to robust economic development, land possession is the most difficult problem. The poor and the farmers are vulnerable to the problem of "landlessness" because they sell their land to solve urgent problems such as paying off debts and paying health and medical care. Land grabbing by the powerful and the rich and granting of economic concessions for investors' plantation and logging also often lead to land disputes and violence at times.

(5) Lack of Information and Understanding on Economic Integration

Except for foreign investment firms, Cambodian enterprises, especially small and medium enterprises (SMEs), experience many difficulties in entering export markets and in expanding exports. Familiarity with modern data and information sources is low and sometimes nonexistent. As a result, SMEs are not aware of the design and quality requirements of foreign markets. The private sector also has little or no idea about the benefits of economic integration. There is also limited support from the Cambodian government to keep the private sector informed on commodity prices and market access. This lack of knowledge results in missed opportunities for Cambodia to exploit the export markets under the AFTA and other free trade arrangements.

(6) Lack of Trade Promotion Activities

Cambodia has very limited funds for conducting activities in promoting trade abroad. Unlike Thailand, Vietnam, China, Korea, Taiwan, and other countries in the region, Cambodia seldom conducts trade fairs and trade promotion events except when the country is provided free space during international conventions or exhibitions abroad. The role of Cambodian embassies abroad for trade promotion is also very limited.

In conducting international business, especially trading, activities such as promotion, marketing, and finding appropriate business partners are essential. Cambodian producers and traders have difficulty in exploring trading opportunities because they lack experience in dealing with the international market. Foreign producers and traders have an edge because they receive strong support from the Government through trade fairs and other trade promotion activities.

(7) Complicated Bureaucracy for Trade in Cambodia

Though the market is available for the country in the framework of AFTA, Cambodia is beset by domestic problems especially in dealing with complicated procedures and corrupt practices in exporting products. Fisheries, rice, and other agro-products still require various permits (transportation permits, export permits, etc.). Firms frequently face delays in clearing imported inputs through customs, thereby jeopardizing their production schedule and ability to meet the delivery dates required by their clients abroad.

(8) High Cost of Doing Business in Cambodia

As the country is in transition, corruption in the administration (and particularly in business operation including import-export activities) is a serious problem. Local business people have identified other problems such as lack of infrastructure; protracted customs clearance procedure; high cost of electricity, internet, and telephone; and high cost of transportation. Phnom Penh and many other major cities often face electricity blackout due to inadequate supply or unreliable source of electricity.

(9) Low Production Base

Economy of scale is very favorable for trading, especially for agricultural products. However, most of Cambodia’s agricultural products are small-size family ventures that are not appropriate for export as some importers require big volume of products. Intermediate traders (or middlemen) usually exploit the market and extort price that may lead to losses in revenue for smallholders. On the other hand, most of Cambodia's agricultural products are available only seasonally and not all-year round. For example, rice in Cambodia can be harvested only once a year between November and January. It is difficult to supply rice to the market all-year round unless Cambodia has a good technology in postharvest storage and quality control.

(10) Poor Technology

Cambodia has limited production bases, especially the processing industry. With limited support from the State and poor status of human resource, Cambodian farmers and producers depend primarily on traditional style of production. Thus, with poor technology, productivity is low compared to competing countries, resulting in huge losses for Cambodia in the global competition.

(11) Lack of Credit Access and Insurance

To promote commercialization of Cambodia's agro-products, financial resources are required to invest on land, fertilizers, machineries, transport and marketing of produce, insurance, hiring of labor, etc. At present, farmers and producers are in dire need of credit for business start-up or expansion. However, they cannot get a loan without condition or collateral, which is normally required by commercial banks. International trade finance activities carried out by banks in Cambodia also tend to be limited to payments and collections and letters of credit. Pre-and post-shipment finance is not easily available from banks in Cambodia. Insurance is also not well developed. Factories and the transport of merchandise within Cambodia are rarely insured.

6. CONCLUSION

Cambodia has conducted many economic reforms to promote economic growth and reduce poverty. Though the country has been admitted to most of the regional cooperation mechanisms such as ASEAN, AFTA, and WTO, the benefits of market access are still limited and thus, it is still premature to evaluate the costs and benefits. The country is still facing many constraints in the process of economic development such as high poverty rate, growing inequality, insufficient infrastructure, and low production base. Private sector participation in trade to benefit from AFTA and ASEAN+3 (such as the ASEAN-China FTA) is very limited. There are many constraints to overcome this shortcoming.

Cambodia has few finished products that are usually in poor quality so they cannot compete with similar products imported from neighboring countries. Though the trade volume has increased yearly, the trade deficit keeps on growing. With its active participation in trade promotion activities such as the World Expo and China-ASEAN Expo, Cambodia can promote its products internationally. Examples are Muscle Wine, palm wine and Angkor Beer, which Cambodia can promote to huge markets like Japan and France. Other promising export products are handicrafts, rice, fish, rubber, and wood.

Cambodia has no other viable alternative to realize ASEAN integration but to effectively address the imbalanced development in the region on the one hand, and move ahead toward enhancing and deepening East Asian cooperation, on the other hand.

The disparity in ASEAN today constitutes a real major challenge, which the member countries must overcome at any cost. A fully integrated ASEAN will sustain its relevance, boost its competitiveness in the face of increasing challenges of globalization and regionalization, and revive its strength as a catalyst for strengthening East Asia. Moreover, an economically strong ASEAN will not only benefit ASEAN but also its partners. Therefore, the integration of ASEAN remains a critical factor that will bestow significant benefits to East Asia as a whole and to ASEAN's other partners as well.

7. POLICY RECOMMENDATION

(1) Tax on Assets

In Cambodia, the revenue from tax collection is still very low compared to other countries in the region. One of the major reasons is because the government does not impose tax on property and land as this is a sensitive political issue in Cambodia. At present, the price of land and real estate is skyrocketing in Cambodia, especially in urban areas like Phnom Penh, Sihanoukville, and Siem Reap. However, the government has not tapped the benefit from the rising land price and booming real estate businesses. Though there is a small tax (seal tax) on land title transfer, the agreement on sales without transfer of land title may lead to huge losses from tax evasion throughout the country. Therefore, land tax, especially on unused land, should be strongly recommended even at a low rate. This will generate revenue for the local and central governments and will reduce land speculation as well.

(2) Enhancing Agricultural Productivity

The government should implement agriculture-led strategies to achieve accelerated progress in quantity and quality. Growth in the agricultural sector can result from increased production through higher productivity, containment of losses (which, at present, could be as high as 35-40 percent), sound postharvest support systems, crop diversification (including horticulture and floriculture), and increased emphasis on animal husbandry and fisheries. The concept of “Green Belt” should be promoted for booming urban areas.

(3) Promotion of Infrastructure Linkages to Countries in the Region

The focus for transport infrastructure for the rehabilitation of high-priority trunk and feeder roads and bridges, especially the regional highways linking countries in the region, should remain to realize the potential of agriculture, tourism, and trade in the rural areas. There is also a need to develop a comprehensive transport policy framework, addressing issues such as development of a balanced construction and maintenance program, increased involvement of the private sector, and financing of road maintenance and cost recovery mechanisms. With regard to institutional strengthening, the Ministry of Public Works and Transport will formulate strategies to improve its capacity to plan, manage, and implement road operations.

Major investments are now being made to improve the physical transport infrastructure linking Cambodia with Thailand and Vietnam, as well as to improve sea and air access to international destinations, especially China. Energy, port, and airport should be promoted to meet the increasing demand of production and trade. These developments could greatly reduce transport costs and increase the competitiveness of Cambodian products on export markets. However, the full benefits of such developments will only be realized if people and goods can move across borders at minimal cost.

(4) Investment Promotion

Cambodia is one of the most attractive destinations of FDI in the region due to its abundant natural resources, low labor cost, and liberal laws. There is a huge potential for Cambodia to attract FDI from rich countries. Investment promotion should be organized locally and abroad. In-country campaigns should include seminars and debriefings to business communities and foreign diplomats to familiarize them with the legal and institutional framework, investment incentives, and investment opportunities. The products and services of the CDC should be promoted to satisfy investors. Successful cases should be documented and featured in promotional instruments like leaflets, brochures, and investment guides.

Campaigns for investment promotion abroad may include sending investment promotion missions, participating in regional fora and seminars, networking through Cambodia's embassies abroad or the ASEAN business centers as channel of communication, and setting up information service centers. Trade fairs promoting Cambodia's products and services will also help attract foreign investment.

As the Government decentralized to the provincial and municipal levels the decision on project investments amounting to less than US$2 million, investment promotion should be conducted at the provincial level as well to present the investment opportunities in the area. The CDC should invite the provincial investment promotion agencies to participate in campaigns to attract investment and technology transfer.

(5) Urbanization and Zoning

Huge regional disparity exists in Cambodia. It is therefore important to promote the regional growth corridors, such as Phnom Penh, Siem Reap, Sihanoukville, and the Northeastern region. The most crowded areas are the plain plateau and along the Mekong River, where soil condition is favorable for agriculture. The least crowded is the coastal area. Most economic activities concentrate only in Phnom Penh and a few other urban areas such as Siem Reap and Sihanoukville. The government should develop an appropriate urbanization plan by assigning growth corridors to spread development benefits to other regions and down to the provinces and districts.

Autonomous regions or cities such as Poi Pet, Kep, Pailin, Sihanoukville, Neak Leung, Soung, Steng Treng, and other strategic locations should be developed as FDI destinations by building the necessary infrastructure and facilities. Special economic zones (export processing zone, free trade zone) should be put in place by government and the privates sector to attract investment and promote equitable economic development in these cities.

(6) Trade Facilitation

The Government should play an active role in supporting farmers by providing standard certificate, credit access, and market information. The role of the Government in trade promotion and trade support services is in its infancy. At present, the Government does not effectively promote trade or provide trade support services. Although the Ministry of Commerce has recently established a trade promotion department, it is not yet fully operational due to lack of funding. Developing effective mechanisms such as, for example, training officials for effective trade promotion and trade support services is clearly an area that is greatly needed by Cambodia. Thus far, the Phnom Penh Chamber of Commerce has not actively promoted trade among its members or the Cambodian private sector at large.

Assistance is needed in all aspects of creating an effective export promotion mechanism, including the elaboration of an export promotion strategy, developing and managing the necessary national and international databases, and training trade officials and staff on techniques for organizing trade fairs and other trade promotion activities. Promoting the exports of SMEs should also be given attention.

Assistance is also required in completing the task of putting in place an appropriate legal and regulatory framework for the financial sector. Training on trade finance and trade insurance is required for both the private sector and government officials (in particular those dealing with export promotion). Help is needed in setting up proper mechanisms to supervise the implementation of the forthcoming legislation on insurance.

In the area of business information, training on international marketing is required for those involved in export promotion and for private traders associations as well.

Assistance is also needed in establishing a "trade point" to facilitate the exchange of information needed by exporters and importers. Assistance is required in putting in place more effective customs procedures, allowing Cambodia to benefit fully from customs automation through the Automated System for Customs Data. In addition to allowing more efficient customs clearance for traders, automation will enhance the capacity of the customs department to generate timely trade data, and improve revenue collection.

Export credit and investment insurance agencies, commonly known as ECAs, play a critical role in international trade and finance in developing countries, and thus have a great impact on sustainable development. ECAs provide government-backed loans, guarantees, and insurance to corporations seeking business opportunities in developing countries and emerging markets that are often considered too risky for conventional corporate financing. They are primarily public or publicly mandated institutions that support and subsidize exports and investment of companies from their home country. Cambodia should recognize ECA as part of trade facilitation. (For more details about the ECA, see Center for International Environmental Law 2002.)

(7) Access to Market Information

Information gathering and dissemination on trade, agro-business, and potential markets should be strengthened as this will be useful for the business community in analyzing trading potentials. The government should establish information broadcasting through TV or radio and encourage the people to use the internet and other information communication technologies (ICTs) by reducing internet fee and other means.

(8) Technology Transfer

Cambodia cannot move fast enough to catch up with its neighbors in the region if the level of technology and science will remain low. Technology transfer should fit the overall strategy of the government's priority. Investment encouragement to succeed would have to take emphasis on job creation, research and development (R&D), and effective knowledge and technology transfer.

The government may wish to consider the following measures:

- Ensure assessment of local needs in technology as well as the social impacts of technology
- Expand R&D programs in technology development including adaptation to local needs
- Create awareness on technology transfer
- Improve transfer of technology among developing countries including joint R&D and opening of markets
- Develop the ICT infrastructure to support investments in technology and the operation of intermediaries
- Establish high-tech parks to attract investment in high technology such as electronics and computer parts.
- Improve macroeconomic stability for transfer of technology

To maximize the benefits of FDI through enhancing technology transfers and spillovers, Cambodia should make sure that interventions based on anticipated trends of comparative advantage will be effective, but this would require careful industry-specific analysis and broad-based consultation with the private sector and other stakeholders. Cambodia should rely more on comparative advantage, and keep in mind that FDI that responds to global market forces holds promise, particularly FDI in export sectors.

(9) Industry Diversification and SMEs

So far, Cambodia depends mainly on the garment and apparel industry, tourism, and agriculture. Diversification of industry and promotion of SMEs are very important to promote local production. National standard for local products must be strengthened to meet international benchmark, especially for food and processed products.

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