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CAMBODIA IN 2012: KEY TRENDS AND POLICY PRIORITIES FROM THE CAMBODIA OUTLOOK CONFERENCE¹

The sixth annual Cambodia Outlook Conference, a partnership between CDRI and ANZ Royal Bank, took place on 16 February 2012 in Phnom Penh. Senior representatives of government, the private sector, development partners, the research community and civil society came together to discuss *Cambodia's Priorities for Inclusive Growth, Regional Integration and ASEAN Leadership – How to Achieve Them*. In his opening address, Prime Minister Hun Sen noted the timeliness of the conference's theme – just before Cambodia assumes the ASEAN Chair, and highlighted its important role in informing policy priorities for the year ahead. This paper provides an overview of salient issues which emerged during sessions, identifying key areas where government action should be focused in 2012. Presentations from the Outlook Conference are accessible on CDRI's website at www.cdri.org.kh.



Prime Minister Hun Sen delivering the keynote address at the opening ceremony of the 2012 Cambodia Outlook Conference, Phnom Penh, February 2012

2012 has the potential to be the most fruitful of recent years for Cambodia. GDP grew by almost 7 percent in 2011, and is predicted to maintain this rate in 2012. The economy's core growth sectors, agriculture, industry and tourism, are performing strongly and construction, which suffered greatest during the global financial crisis, also seems to be on the mend. In addition, this year Cambodia takes the chair of ASEAN and with it the opportunity to shape and strengthen an increasingly influential and important regional institution.

At this important juncture, the Cambodia Outlook Conference assessed the opportunities and challenges that lie on the road to the government's

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¹ This article, by Mr B. C. R. Flower, UCL PhD student and CDRI research intern, is based on the presentations made at the 2012 Cambodia Outlook Conference, 16 February 2012, Hotel Le Royal, Phnom Penh. Conference presentations and policy briefs are available at www.cdri.org.kh.

medium-term aim of achieving middle income country status. The key goal is to build on strong foundations and deliver high and sustainable long-term economic growth. The conference stressed three interrelated areas where policy action is necessary if this goal is to be realised. First, is utilising opportunities afforded by ASEAN and other regional networks in driving economic diversification, efficiency and growth. Second, is optimising the role of the private sector in the context of regional integration, again to aid diversification, efficiency and growth. Third, is inclusive development, so that Cambodia extends the benefits of growth across all sections of the population and into geographical peripheries.

This summary presents the trends and policy priorities associated with these three themes. It also advances policy action in the context of the central issue that pervades all aspects of Cambodia's development, and which was repeatedly highlighted at the conference: institutional capacity to adequately implement and enforce policy.

Promoting Regional Integration

The changing structure of the global economy means that Cambodia will have to adapt if it is to thrive. Principally, it must diversify away from garment export to the United States and Europe as its core growth driver and develop new industries that cater to new markets. In this endeavour, Asian growth poles present new sources of demand for a variety of agricultural, industrial and service products. In particular, the import profile of China, with its huge demand potential for agricultural and intermediary products, should play a central role in informing Cambodia's economic strategy.

Fostering increased regional cooperation constitutes a crucial component of Cambodia's strategy to take advantage of Asia's remarkable growth. Deep integration reduces the distance between producers and markets, reducing costs for Cambodia producers accessing ASEAN markets, and ASEAN producers accessing global markets. To this end Cambodia is well placed as Chair to strengthen regional cooperation and help realise a single ASEAN Economic Community (AEC) by 2015. Already the Cambodian government has eliminated import tariffs on over 98 percent of goods originating in ASEAN. Cumbersome and inefficient

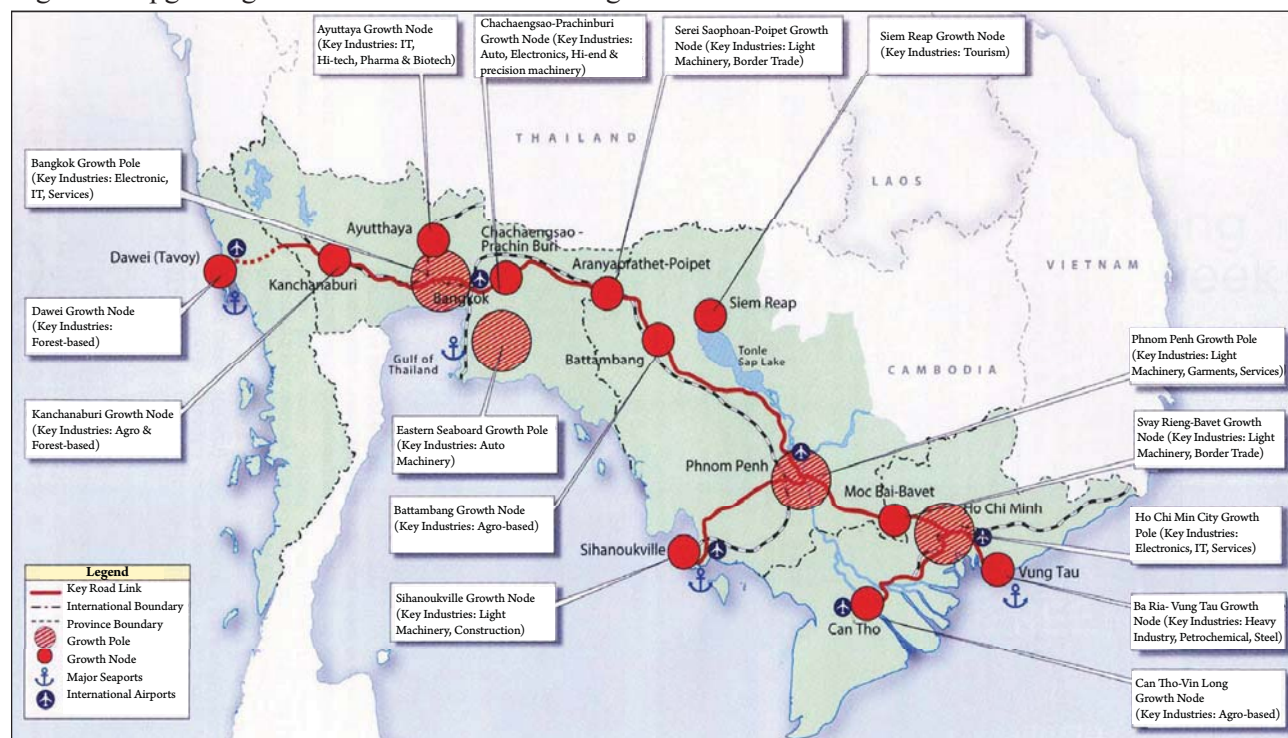
cross-border procedures have been streamlined by developing an ASEAN Single Window (ASW) customs service. Cambodia will initiate its National Single Window (NSW) service, which will form the basis for its participation in the ASW, in the fourth quarter of 2012.

A key driver of Cambodia's future economic development will be foreign capital, and therefore government should ensure institutional and regulatory frameworks are receptive to it. The ASEAN Comprehensive Investment Agreement (ACIA) – launched this year – works towards liberalisation, promotion and protection of investments by ASEAN investors and ASEAN-based foreign investors. Eliminating investment restrictions will attract more investment, while greater protection and well-defined transparent procedures will encourage longer-term investments in a wide range of activities. In the medium term this will encourage competition across Cambodia's sectors and increase efficiency in the country's economy.

Policy reforms have been complemented with initiatives that have sought to overcome the physical barriers between nations by upgrading hard infrastructure. Infrastructure projects enhance productivity across all sectors by reducing costs for business, and are a key tool for unlocking the latent potential of the agricultural sector by opening up small farms to regional and global markets, technology, services and investment. The ADB-GMS Southern Economic Corridor Project entails improved road and rail links between Cambodia and regional manufacturing hubs, cross-border electricity cooperation, and the upgrading of regional telecommunications and ICT infrastructure (Figure 1). The flagship project is the rehabilitation of Cambodia's railway network. Once this is finished in 2013, the mainline from Kunming to Singapore will be fully operational.

A strong ASEAN provides Cambodia with an effective platform to engage with Asian markets and beyond, and hence new and varied sources of demand for a range of products. Several agreements to facilitate increased economic interaction between member countries and other strategically important economies throughout the world are already firmly in place. ASEAN has negotiated a number of Free

Figure 1: Upgrading Infrastructure in ASEAN Region



Source: H.E. Dr Hang Chuon Naron's Cambodia Outlook Conference presentation, 16 February 2012

Trade Area (FTA) agreements that have the potential to greatly improve the export profiles of member countries with China, Korea, Australia and New Zealand.

Unity and harmonisation among members provide the foundations for ASEAN and hold the key to its future effectiveness. Greater efforts, therefore, should be made to narrow the development gap between ASEAN and the lesser developed economies of Cambodia, Laos and Myanmar through mutual assistance and cooperation. The ASEAN Regional Forum, ASEAN+3 and East Asian Summit processes provide excellent opportunities to promote cooperation, peace and security in the region, to prevent conflicts and resolve tensions, and to respect and safeguard the interests of both the big and small nations of the region.

Enabling the Private Sector

The private sector has been the driving force behind Cambodia's economic transition. Economic liberalisation in the early 1990s unleashed a flurry of investment in land, construction and later garments. Skeletal institutional and regulatory frameworks laid down in the 1990s provided a framework for private investment, but their limited capacity for

enforcement left markets prone to rent seeking. Consequently, although growth was high, it was uneven, unstable and inequitable. Over the past decade the government has focused on building the requisite institutional capacity for private investment to operate in a secure, transparent and regulated fashion.

Foreign direct investment has soared as targeted institution building has provided the assurances necessary for small and large-scale investment. However, the bulk of this investment has been limited to the garment and construction industries which, as the experience of the financial crisis showed, can be fickle and easily disappear if conditions change. Such an investment profile runs counter to the government's aim of sustained, stable growth; policy frameworks need to bring private sector and government priorities into alignment.

Deepened public-private sector cooperation and dialogue are key to reconciling currently divergent public and private sector agendas. In particular policies and institutions should promote public-private partnerships so that policy action represents economic imperatives and, vice-versa, that the private sector is mobilised to fulfil a vision

of diversified, sustainable inclusive growth and regional integration.

Cambodia must work with regional powers to create an institutional and regulatory environment that enables the private sector to flourish in an era of increasing regional cooperation. In turn, the private sector must utilise the opportunities of increased regional interconnectivity cooperation afforded by a strong ASEAN. For Cambodia, ASEAN facilitates the deepening and widening of production and distribution networks, thus enhancing efficiency, spurring innovation and expanding markets for private sector actors. Several countries in the region, notably Malaysia, Singapore and Thailand, now boast companies that have been able to take advantage of the economic growth and integration occurring in ASEAN to become multinationals. With sound policy and commitment, Cambodia will hopefully follow suit.

If the Cambodian private sector is to join the ASEAN business elite, it must develop a better understanding of the competitive and comparative strengths of its economy and play to them. Research is of fundamental importance in overcoming information deficiencies that limit the scope for private sector-enhancing policy. Cambodia's network of academic and research institutions must be mobilised to assess the constraints facing Cambodian businesses in accessing intra-regional economic networks. The research must be policy focused and utilise a subsector-based analytical framework.

A binding constraint to increasing productivity in the private sector is an under and inappropriately skilled workforce. Equipping Cambodians with the right skills will help to diversify the economy away from its narrow economic base and provide employment opportunities in industries such as agro-processing, non-garment manufacturing and a range of services. It will also provide employment opportunities across sectors where potential poverty impacts are significant. An appropriately skilled workforce would also increase the ability of industry and government to respond rapidly to future crises by re-skilling or up-skilling.

To deliver an appropriately skilled workforce, policy needs to be pragmatic and representative of economic realities. Inefficient information transfers result in sub-optimal labour market efficiency, and

are at the root of the current skills-needs mismatch. There is a lack of understanding about labour market systems within Cambodia's workforce, a lack of information for youth, parents and job seekers, and a lack of institutional mechanisms to coordinate between policy-makers and business leaders.

Policies should focus on eliminating information asymmetries in the labour market. For example, mechanisms to provide more internship opportunities and practical work experience, such as study tours, would enable young people to familiarise themselves with skills that would enhance their employability. Managing expectations and perceptions of family members who make decisions around education and investment in education is also important. This will prevent potentially scarce family resources being wasted on pursuits that will pay limited dividends in terms of future earnings.

Effective and dynamic public-private sector cooperation is essential in increasing Cambodia's capacity to successfully implement Technical and Vocational Education and Training (TVET) programmes. TVET provides the workforce with the technical and vocational skills necessary to drive and diversify Cambodia's economy; it is a bridge for young people to enter employment by gaining skills that employers need. It is thus important that private sector needs are represented in TVET curricula, and frameworks that facilitate this kind of cooperation are developed. Public-private partnerships in TVET could provide Cambodia with a great competitive advantage in the region. The country's strategic placement at the heart of ASEAN could yield world class ASEAN technical training facilities if regional knowledge networks are effectively harnessed.

Currently there are major constraints that limit the effectiveness of TVET. These include funding issues, lack of teaching facilities, a limited pool of qualified teachers/trainers and a lack of coordination in providing private sector guest teachers/trainers. The overriding constraint is simply a lack of capacity to implement TVET in a form and at a scale that can truly impact on the skills deficit in the Cambodian labour market. There is also a perception among the population that TVET courses are not prestigious and are for blue-collar workers. This perception must be rectified through marketing (newspapers,

television, radio) and appropriate regulation and accreditation.

Although relatively few in number, practical training programmes that produce appropriately skilled workers to meet labour market demands do exist. It is important to mainstream and scale-up good TVET programmes in partnership with the private sector; procedures need to be put into place to make this a reality.

TVET, however, is not a panacea to Cambodia's skills shortage: government, educational institutions and the private sector must strive to improve all aspects of the education system, from primary through to TVET and higher education, and finally monitoring employee performance and re-skilling as required. This kind of holistic framework should be the medium to long-term ambition of the government.

To be sustainable, private sector development has to balance tradeoffs between economic growth and the environment. The tourism sector is emerging as a growth driver that need not bring with it the destruction of natural habitats. Eco-tourism businesses have an economic interest in preserving the natural environment – it is their selling point. New eco-tourism ventures are being set up around the country, especially in areas of special scientific interest such as the Cardamom mountain range in Koh Kong province, and the wildernesses of Mondulhiri and Ratanakiri. Improved transport links have greatly hastened the emergence of these tourist areas. The private sector development of the tropical Islands south of Sihanoukville also places great emphasis on protecting the natural environment. Such environmentally responsible business models should be promoted and incentivised by government, and informed by research from academic and research institutions.

Other industries have more harmful impacts on the environment. Economic Land Concessions (ELCs) provide a valuable source of foreign investment for Cambodia. Commodities yielded by these concessions, particularly rubber, provide significant export revenue for the country. At the same time, ELC plantations frequently cause deforestation and environmental degradation. They need to be properly managed and monitored to ensure that negative environmental consequences

are minimised wherever possible. Detrimental environmental impacts can be significantly mitigated if appropriate frameworks are implemented.

Inclusive and Diversified Growth

High economic growth is the cornerstone and principal measure of a country's successful socio-economic development. For this reason, policy makers have long strived to create macroeconomic conditions that enable rapid growth. However, it is being increasingly recognised that if high growth is going to be sustained in the medium to long-term, concerted efforts must be made to ensure it extends across sectors, population groups and into geographical peripheries. Inclusive growth, therefore, links prudent macroeconomic policy with proactive microeconomic and social policy to ensure that growth remains high, but that its trend is equitable.

By all indications Cambodia has made remarkable progress in reducing poverty over the last two decades of high, sustained economic growth. Cambodia Social and Economic Survey (CSES) data indicate that the poverty headcount ratio at the national poverty line had declined to 30.1 percent in 2007 from 47 percent in 1994. Similarly, panel data from CDRI household surveys shows that poverty reduced by 10 percentage points between 2001 and 2011.

Beyond the clear overall trend of declining poverty, other factors suggest that Cambodia's growth has not met all the criteria of inclusiveness. First, rates of poverty reduction have not been uniform across the population. CDRI data reveals that the gender of the household head has been a significant factor affecting the rate of poverty reduction. Between 2001 and 2011 the number of male-headed households living in poverty decreased by 11.8 percent, while the number of female-headed households living in poverty declined by only 5.5 percent. CSES data shows disparities between urban and rural populations: between 2004 and 2007 the number of rural households living in poverty declined by 11.1 percent, while the number of urban households living in poverty declined by 13.3 percent. If current trends persist, inequality between rural and urban populations and female- and male-headed households is set to increase in the future.

Second, beyond income measurements of inclusiveness, Cambodia performs poorly. As Table 1 demonstrates, although Cambodia's inclusive growth index is "satisfactory", it is buoyed by "superior" rates of growth and almost "superior" rates of consumption-based poverty reduction. However, other factors that contribute to an enabling environment, such as social protection for the poor and vulnerable, are seriously lacking.

To engender inclusive growth, policy makers must take a three-pronged approach that links macroeconomic, microeconomic and social policy; policies must be implemented through transparent, good-governance institutional frameworks. Macroeconomic stability alongside consistent GDP growth is the most important factor in driving inclusive growth through creating employment. Therefore, government must maintain a stable macroeconomic outlook, and in particular a manageable rate of inflation, preferably at below 5 percent. Moreover, about 90 percent of poor households depend on rural livelihoods, so government must redouble its efforts in rebalancing the economy to represent this fact.

Local economic development is imperative if growth is to permeate remote geographical regions and across sectors. The peripheries are where most poverty is concentrated, so it is critical that these areas are opened up to markets through infrastructure

development. The ADB-GMS umbrella programme has been instrumental in upgrading infrastructure along key economic corridors, thereby linking Cambodia's periphery to national, regional and global markets. In addition, complementary service provision is needed to increase productivity, particularly among the rural majority, many of whom farm small rice plots.

Lack of formal service and credit infrastructure remains a binding constraint to many farmers and small and medium enterprise (SME) operators, though there have been major advances in this regard. The microfinance sector in Cambodia has played a leading role in expanding the reach of formal financial services to the rural poor. The sector has experienced rapid growth over the last five years, reaching 1.3 million borrowers and 1.1 million savers in 24 provinces. Deposits increased by 32 percent to USD1.26 billion in 2011 from USD952 million in 2010. There have been gains in extending irrigation infrastructure, for example the ADB-funded Northwest Irrigation Sector Project, which comprises 12 sub-projects to provide enhanced small and medium irrigation schemes and water control structure for supplementary wet season irrigation of approximately 10,000 hectares of rice fields and *chamkar* (vegetable plots).

It is essential that policy addresses social and cultural norms that prevent women accessing

Table 1: Inclusive Growth Index for Cambodia

	Score	Weight	Total
1. Growth	8	0.25	2.00
2. Employment	4	0.15	0.60
3. Economic infrastructure	4	0.10	0.40
4. Poverty	6	0.10	0.60
5. Inequality	4	0.10	0.40
6. Gender equity	6	0.05	0.30
7. Health & nutrition	3	0.05	0.15
8. Education	4	0.05	0.20
9. Sanitation & water	4	0.05	0.20
10. Social protection	2	0.10	0.20
Total		1.00	5.05

Note: 1-3=unsatisfactory progress, 4-7=satisfactory progress, 8-10=superior progress

Source: Mckinleg (2010), cited in Dr Tong's Cambodia Outlook Conference presentation, 16 February 2012

economic opportunities, such as employment, credit and services. A core component of the Ministry of Women's Affairs (MoWA) Neary Rattanak III strategic plan is developing national policies to promote gender equity in economic opportunities. The programme aims to effect changes in cultural models of gender that favour men's participation in some economic activities, for example purchasing and inheriting property, by promoting policies that remove barriers to women's participation throughout the economy.

As regards social policy, Cambodia lags far behind many countries in the region when it comes to healthcare, nutrition, education and social protection. Lack of social protection and healthcare services negatively affects rates of growth, and contributes to a trend of growth that is not inclusive: poor households that are constantly battling to meet basic daily needs are rarely productive, but rather teeter on the edge of survival in a cycle of poverty.

There is no wide-reaching state administered social protection system in Cambodia, despite civil society's efforts in providing social support mechanisms for the most vulnerable, and development partners' support of specific projects. Reliance on development partners and civil society means that progress in this area has lacked continuity and has been largely shaped by the varied agendas of an array of different organisations.

Recently the government has developed National Social Protection Strategy (NSPS) 2011-15, a comprehensive plan to address the dearth of social protection in the country. The NSPS framework streamlines existing social programmes under a broader framework that will protect the poor and vulnerable, especially those living in female-headed households, and facilitate their integration into productive economic activity. This includes social safety nets to reduce poverty and food insecurity, and schemes to improve nutrition, maternal and child health and promote education. Government should work hard to ensure the effective delivery and implementation of these reforms.

Conclusion: Redressing the Policy-Institutions Mismatch

At the heart of Cambodia's ability to realise inclusive, diversified and therefore sustained growth

is the issue of institutional capacity and governance. The government has developed and deployed a number of innovative policy frameworks that greatly work towards its goal of sustainable growth – the problem lies in effectively implementing them.

A mismatch between institutions and policy can hinder inclusive development. Nowhere is this more evident than in the land sector. Land is particularly important to poor households because it can be combined with labour, their primary asset, to generate capital. Therefore secure land rights are a prerequisite for inclusive growth. But while policy frameworks legally recognise land, the institutions that enforce them have not developed at the same pace. This has resulted in a high volume of land conflicts and a backlog of cases at Cadastral Commissions, undermining perceptions of tenure security and constraining economic participation. A particular point of contention has been the management of Economic Land Concessions (ELCs). While again there are policies and regulatory frameworks for allocating and monitoring ELCs, in some cases these have not been followed and land use is of sub-optimal efficiency. As a result, local households' participation in capital generating activities has been constrained.

Reforms of local institutions that play a key role in households' day to day lives are also important for equitable socioeconomic development. The government's de-concentration and decentralisation reforms have worked towards reforming commune councils with a view to making them more gender equitable, efficient and transparent in providing services and administering the local populace.

Much has been done over the past decade to strengthen the country's institutions, but there is still much to do. Hence, while 2012 brings great opportunities to realise a stable, equitable and prosperous Cambodia, the omnipresent constraint of institutional capacity remains. It is essential that government and development partners continue to prioritise this issue and coordinate resources to remove this core constraint. Once these are redressed, Cambodia can expect to reap the benefits of stronger economic ties with regional partners and beyond, and induce a trend of growth that is diversified, equitable and sustainable.