

Trade and investment-led growth and structural transformation as key to Cambodia's eventual graduation from LDCs' category: challenges, opportunities and prospects for sustainable graduation

Concept Note^{1*}

EXECUTIVE SUMMARY

Mired by protracted civil conflicts for decades and the resulting socio-economic difficulties, Cambodia joined the least developed countries' group in 1991. The inclusion of the country in LDCs' group followed the triennial review of the list of LDCs by the Committee for Development Policy (CDP) and its subsequent recommendations to the General Assembly of the United Nations.

The same year and through the 1991 Paris Accord and the 1993 General Election, peace and national reconciliation was restored in the country and, ever since, Cambodia has been making tangible socio-economic progress while enjoying macroeconomic stability in the region. In fact, with an average annual growth rate of 6.9 percent between 2000 and 2012, Cambodia has been registering the second highest economic growth as compared to the neighboring LDCs after Myanmar (11.22 percent) during the same period. The country's human assets index has also improved from about 42 in 1994 to 57.9 in 2012. Likewise, its economic vulnerability index showed continued improvement from 65.5 to 50.5 during the same period, although it still remains high. In sum, Cambodia may not be able to meet all the three graduation criteria soon. However, it will certainly meet the current income threshold of US\$1,190 in a few years provided that its current level of economic growth continues uninterrupted.

Overall, exports of clothing and foreign direct investment have played a decisive role in growth and poverty reduction efforts of Cambodia, although important challenges still impede further economic growth and development of the country. It is important for Cambodia to continue efforts to improve business climate, exchange rate realignment and building infrastructure as key to improve export competitiveness, diversification and continued economic growth. The recent efforts to diversify the export basket by favoring FDI on manufacturing bicycles and bicycles parts as well as the initiative of attracting FDI to other sectors (such as automotive) from ASEAN partners and the Asian region as a whole should be further pursued .

The present note is prepared to serve as a background document for the training workshop on issues related to Cambodia's eventual graduation from the LDCs' group.

¹ The concept note is prepared by the UNCTAD secretariat under the responsibility of the Division for Africa, LDCs and Special Programmes (ALDC) to serve as background document for the training workshop.

*unedited version issued as an advance copy

I. Introduction

As with many least developed countries, Cambodia has seen multiple transitions since the 1990s: a transition from conflict afflicted country to a country of sustained peace and stability, a transition from typical agrarian economy to successful producer and exporter of manufactured goods and services, and from centrally planned economy to export and investment-led open economy. Cambodia joined the least developed countries group in 1991 after the triennial review of the list of LDCs by the Committee for Development Policy (previously Committee for Development Planning) – CDP - and its subsequent recommendations to the General Assembly of the United Nations under a new dynamic set of criteria²: a revised GDP threshold, an augmented physical quality of life index (APQLI)³, an economic diversification index (EDI)⁴ and demographic (or population) criteria⁵. The cut-off points for Cambodia's inclusion were: GDP per Capita of less than US\$ 900, APQLI of 52, EDI of 29 and population less than 75 million Cambodia fulfilled all the criteria to join the category of LDCs with a GDP per capita of US\$111, APQLI 26.2, EDI of 15.4 and a population of 10 million⁶. In subsequent revisions, Augmented physical quality life index (APQLI) has been replaced by the current human assets index (HAI), an economic diversification index (EDI) by an economic vulnerability index (EVI) and GDP per capita by Gross National Income (GNI) per capita.

Following the end of protracted civil conflicts in 1991 and since then, Cambodia has been making measurable progress towards graduation thresholds by registering sustained and high-level of economic growth, which substantially improved its Gross National Income per capita,

² Since 1980 and until 1990, the criteria used were a periodically adjusted GDP per capita which reached US\$ 473 in 1990 (as opposed to US\$ 100 under the first set), a manufacturing share of 10 percent or less of total GDP and an adult literacy of 20 percent or less of the total adult population.

³ APQLI is a composite index consisting of life expectancy at birth, per capita calorie supplies, combined primary and secondary enrollment ratio, and adult literacy rate.

⁴ EVI is a composite index comprising the share of manufacturing in GDP, the share of employment in industry, per capita electric consumption and export concentration ratio.

⁵ Demographic criteria were introduced during the 1991 triennial review, with the minimum threshold level of 75 million people.

⁶ A/47/278- E/1992/77

which is about US\$ 880 (2012). The country has also been making tangible progress in its human assets index (HAI) which increased from about 42 in 1994 to 57.9 in 2012 and its economic vulnerability index (EVI) that decreased from 65.5 to 50.5 during the same period. Although Cambodia may not be able to meet all the three graduation criteria soon, it will certainly meet the current income threshold of US\$1,190 in the near future provided that its current level of economic growth continues uninterrupted.

The present note is intended to serve as a background document for the training workshop on Cambodia's eventual graduation. It sheds some light on the specific development challenges facing Cambodia with a focus on graduation. The note draws heavily from evidences that UNCTAD has been documenting on successful experiences and best practices of LDCs with the aim of initiating policy dialogue on improving the quality of trade and development policies in the countries in order to accelerate their structural economic transformation. Sustainable graduation will be possible only by building productive capacities and accelerating structural economic transformation in LDCs, which in turn can lead to economy-wide value addition, diversification and jobs creation.

II. Recent economic performance of Cambodia

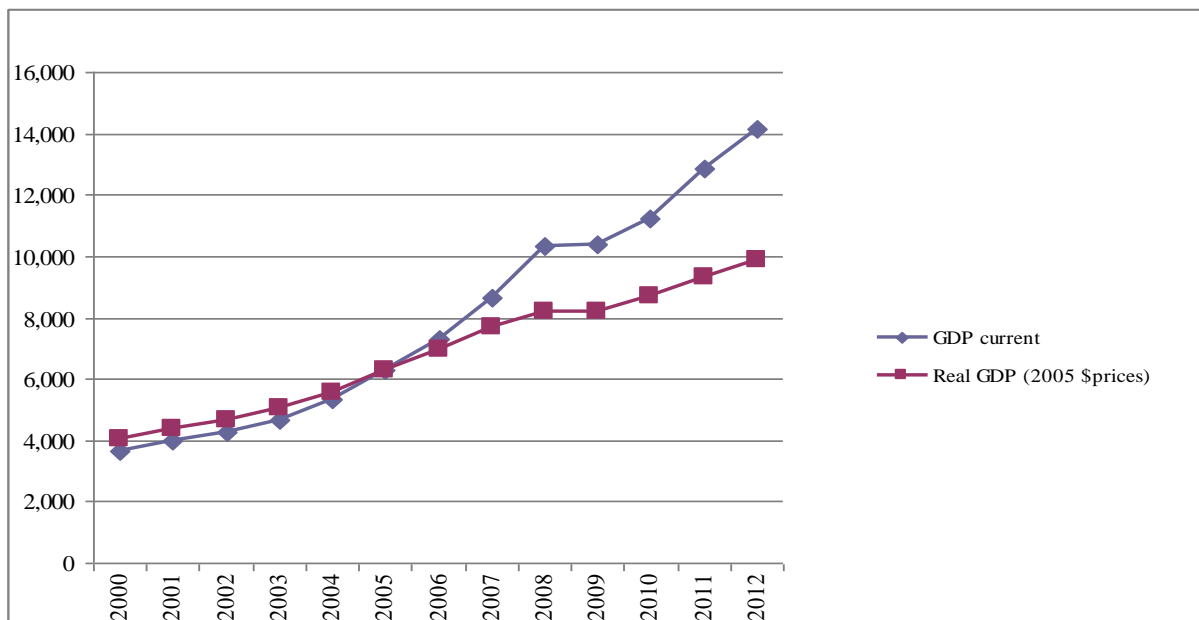
Cambodia experienced very rapid growth, attaining an average GDP growth rate of 6.9 percent between 2000 and 2012 (Table 1). This is the second highest average growth rate among the neighboring LDCs after Myanmar (11.22 per cent) during the same period. The only exception was 2009 (the pick of the recent global economic and financial crises) when the country's economic growth collapsed to a mere (-1.03 percent) before gradually picking-up in subsequent years. As with many other LDCs, the devastating impact of the 2008-2009 global financial and economic crises exposed the underlying fragility and vulnerability of Cambodia's economy to external shocks and crises.

Table 1													Real GDP per capita, average annual growth rates (in % 2000 - 2011)
Economy	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Average	
Bangladesh	3.40	2.61	3.52	4.65	4.48	5.31	5.24	5.08	4.63	4.88	5.42	4.58	
Cambodia	6.38	4.99	7.02	8.92	11.86	9.47	8.96	5.52	-1.03	4.77	4.85	6.98	
Lao PDR	3.95	4.23	4.15	5.31	5.66	6.67	16.44	6.16	5.91	6.20	6.76	6.86	
Myanmar	10.44	11.32	13.28	13.01	12.95	12.39	11.25	9.47	9.61	9.58	4.64	11.22	
Nepal	3.18	-2.16	1.64	2.43	0.99	1.67	1.44	4.15	2.54	2.72	1.70	1.85	

Source: UNCTADstat

The above-shown average annual growth rate during the decade (of Cambodia) is slightly less than the 7% of the target agreed in the context of the Brussels Programmed of Action. Nevertheless, it has effectively contributed to almost quadruple the country's nominal GDP from less than US\$ 4billion in 2001 to over US\$14.3 billion in 2012 and the real GDP to more than double from about US\$ 4billion to US\$10 billion during the same period (figure 1).

Figure 1: Real and nominal GDP, millions of USD (2000- 2012)



Source: UNCTADstat

As will be discussed in subsequent sections, such a solid and improved GDP growth was realized through export-oriented policies and by attracting FDI into labor-intensive industries, particularly garments or, more recently, natural resources such as gold and natural gas (fuel). Cambodia also has an excellent potential in tourism thanks to its natural, historical and cultural heritages. Tourist arrivals have been substantially increasing over recent years at the “annual rate of 20 per cent up from 118, 228 in 1993 to 604, 919 in 2001 and close to 3 million in 2010”⁷. This experience of Cambodia confirms that investment in infrastructure and tourist facilities, along with measures to protect culture, the environment, and political stability are necessary to increase tourism’s importance to the country’s economy (Dhakal, Pradhan and Upadhyaya 2009). Although Cambodia has natural assets for tourism, its regional competitors such as Thailand and Vietnam have excelled by having better infrastructure and less burdensome regulations, giving them higher tourism competitiveness rankings than Cambodia.

Cambodia’s economic success is similar to the other successful LDCs of the region (Lao PDR, Myanmar and to some extent Bangladesh). Like Cambodia, these countries also achieved higher and sustained economic growth while maintaining sound macroeconomic management marked by low inflation, moderate debt levels and concessional repayment terms, although some deterioration has resulted from the recent global financial and economic crises (Golub et al). Available evidence indicates that in most Asian countries that have made notable socio-economic progress, sound fiscal policy assisted in increasing spending on infrastructure while limiting debt build-up was critical (Golub et al). Moreover, as clearly shown in earlier UNCTAD case studies (UNCTAD: 2011e), Cambodia has succeeded in undertaking fiscal reforms aimed at increasing government revenue which is key to boost investment in infrastructure and institution building.

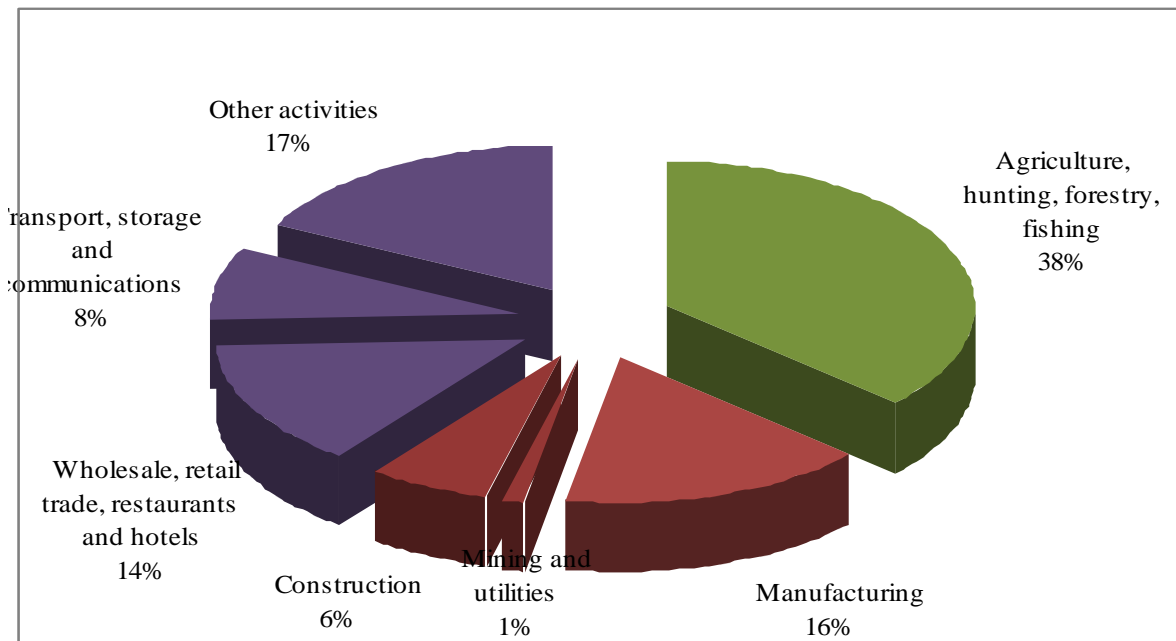
Making the solid growth observed in Cambodia during the last decade more broad-based and sustainable with accelerated poverty reduction requires additional investments and sustained peace and stability. Investment, both private and public, should primarily target sectors where the

⁷ Chaisrisatsuk, S (2008) Thailand and its Cooperative Development Strategies for CLMV, in Sotharith, C (ed) Development Strategy for CLMV in the Age of Economic Integration, ERIA Research Project Report 2007-4, Chiba: IDE-JETRO, pp351-394).

country has comparative and competitive advantages. It is only through enhanced investment, especially in the productive sectors of the economy, that structural economic transformation can be realized and progress towards graduation thresholds accelerated.

A closer examination of Cambodia's GDP composition reveals that (figure 2 below), in 2011, agriculture, hunting, forestry and fishing account for 36.7%; manufacturing 16.1%; wholesale retail trade and hotels 14.3%; mining and utilities 1.2%; construction 6%; transport storage and communications 8.1% and other activities 17.4%. Although the share of agriculture in the country's GDP is continuously shrinking from an average of about 40.9 % during 2005-2010 to about 37% in 2011, "Cambodia's economy is still dependent on agriculture with close to 85 % of the population still earning its livelihood from the sector"⁸

Figure 2: Composition of Cambodia's GDP, 2011



Source: UNCTADstat

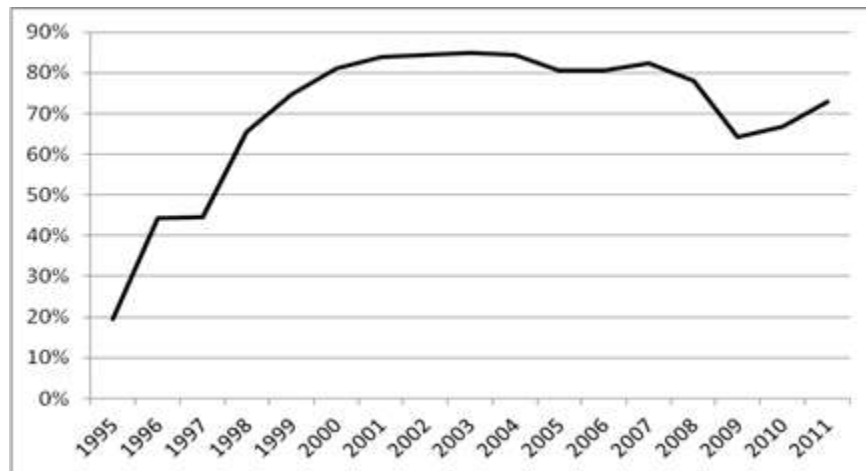
⁸ Chaisrisatsuk, S (2008) Thailand and its Cooperative Development Strategies for CLMV, in Sotharith, C (ed) Development Strategy for CLMV in the Age of Economic Integration, ERIA Research Project Report 2007-4, Chiba: IDE-JETRO, pp351-394

III. Role of exports in Cambodia's economy

Various studies, including by UNCTAD, indicate that the economic growth in Cambodia is driven primarily by FDI and exports of garments and clothing, coupled with the end of the long period of social conflict, favorable geography, relative political stability, and sector specific trade agreements (Guimbert 2010). More importantly, the growth of the garments sector has contributed to employment creation, especially for women, and poverty reduction, both in urban and rural areas, due to remittances provided by urban workers (Natsvad, Goto and Thoburn 2010, Golub et al). Cambodia's garment sector originated in the 1970s, and has become the country's most important industry, accounting for 15 percent of GDP and 65 percent of exports in 2008 (IMF 2009)

As indicated in figure 3 below, the share of garments export in total merchandise export has shown astronomical increase from 20% of total merchandise export in 1995 to above 83 percent during 2000-2007 period; although this was significantly reduced to slightly lower than 70 percent during the recent financial and economic crises (2008-2009).

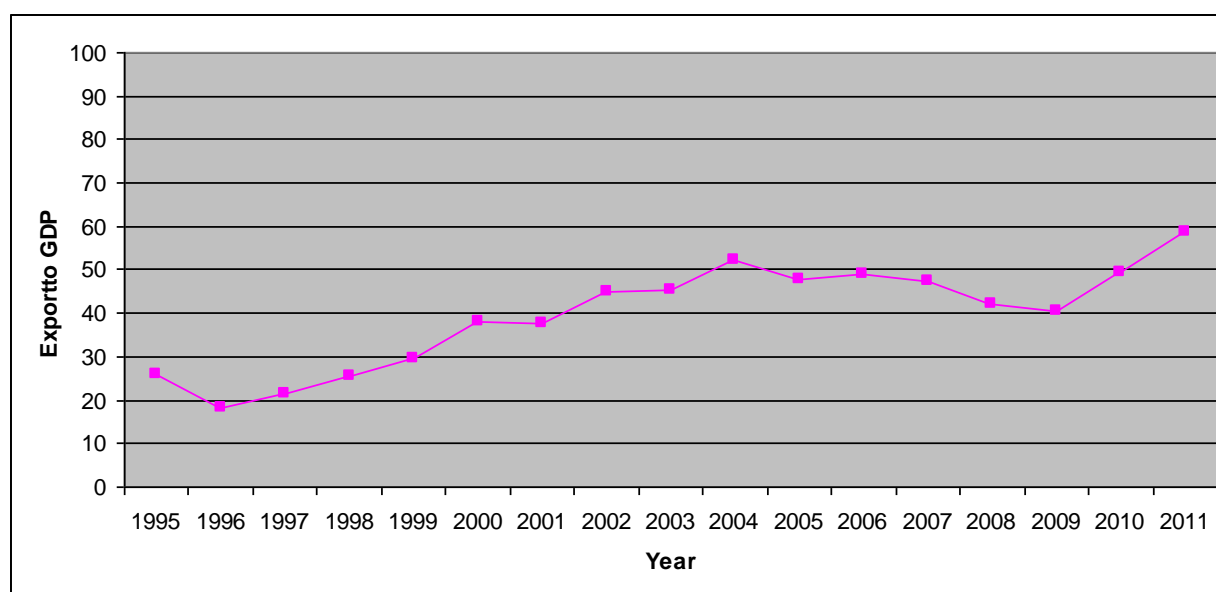
Figure 3: Share of garments in total merchandise trade of Cambodia (1995-2011)



Source: UNCTADstat

In terms of GDP contribution, merchandise exports have played a decisive role, accounting for a significant share in total GDP, which has continued to climb from a little less than 19 % in 1996 to almost 60% in 2011. Overall, Cambodia’s economy is relatively more diversified as compared to some of the star performers in recent years, especially those from the African LDCs (Equatorial Guinea and Angola⁹) where a single export (oil) dominates the whole economy. However, the dominance of garments exports may subject the country to external economic shocks as evidenced during the recent financial and economic crises. In 2009, the GDP of Cambodia decelerated by (- 1.03%) largely due to the collapse of its garments exports, resulting from the global economic crisis.

Figure 4: Share of merchandise exports in the GDP of Cambodia (1995-2011)



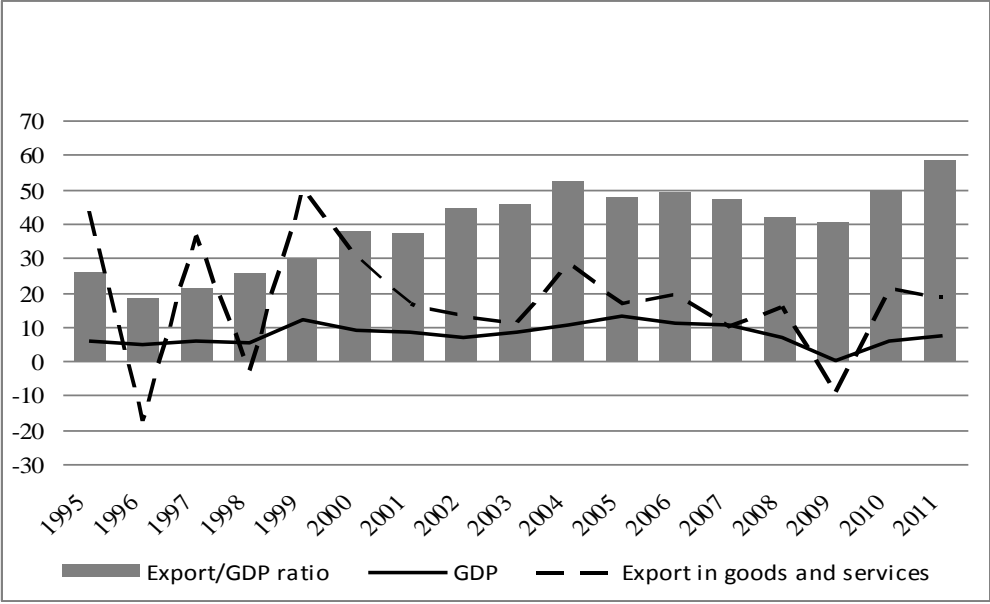
Source: UNCTADstat

As shown in figure 5 below, the direction of the country’s exports determines the trajectory of its GDP. In other words, the growth in exports of goods and services (in value terms) is the main cause behind the growth in the GDP of the country. This shows the importance of trade in Cambodia’s economy but the fluctuations and volatility of exports also emanate from the

⁹ According to the recent work of UNCTAD on Angola (www.unctad.org), in 2011, over 98 % of the country's merchandise export, in value terms, is generated by fuel (oil) exports with manufacturing and primary agricultural exports, accounting for less than 1% each.

dominance of the export sector by garments, making economic diversification more persuasive for Cambodia, as is the case for many least developed countries.

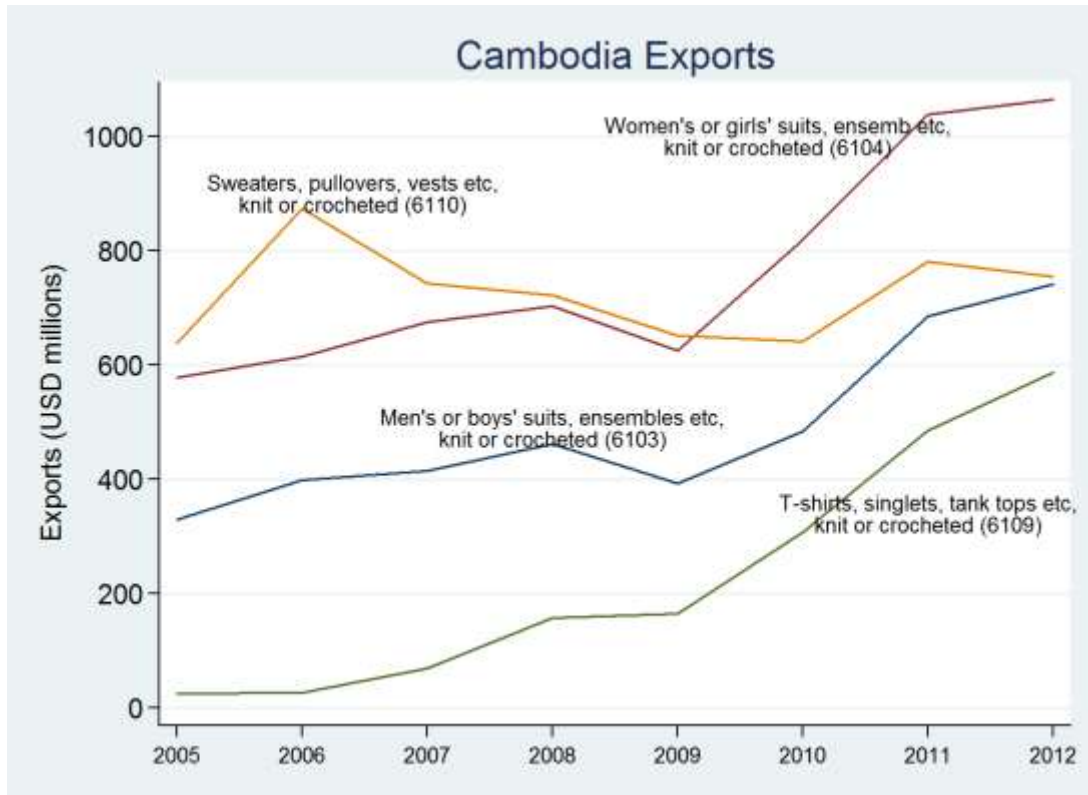
Figure 5: Export/GDP ratio and export growth rates of Cambodia (1995-2011)



Sources: GDP and Export/ GDP Ratio are from UNCTADStat; data on export growth is from the World Development Indicators (WDI)

The graphs below depicts Cambodia recent performance in the main exports of garments sector showing a distinct increase in the recent years

Figure 6: Cambodia Exports of Garments by HS Chapters (2005-2012)



What led Cambodia's garments sector to a relative success?

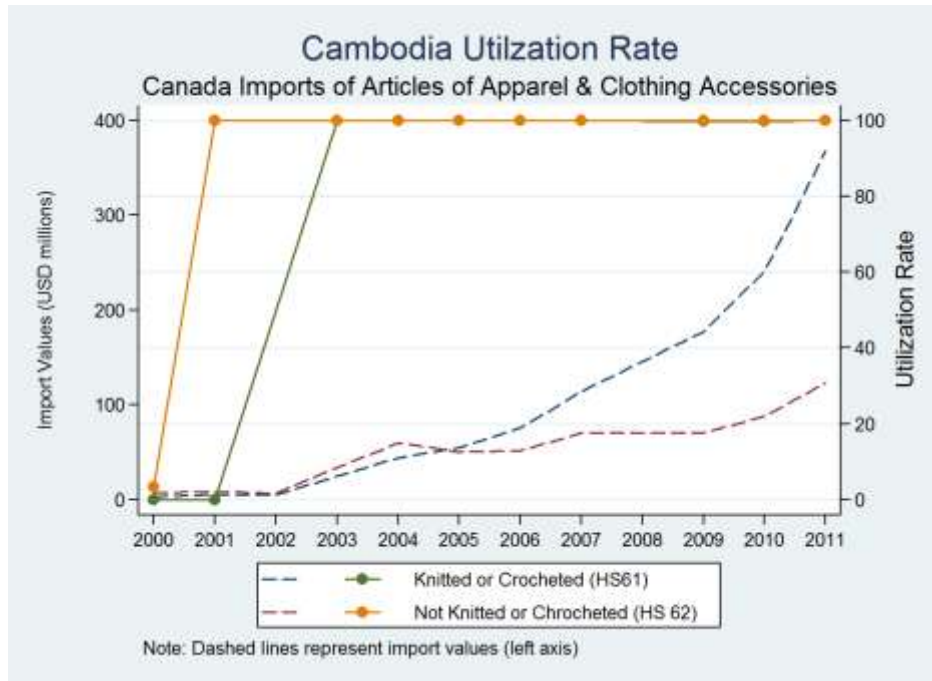
Several factors explain the garments sector's strong growth. Firstly, like many other countries in the Asian region, Cambodia has maintained relative macroeconomic stability, fiscal and monetary transparency as well as policy credibility. For instance, since 2004, the government has worked with international institutions to strengthen fiscal transparency and credibility (IMF 2008b). Secondly, the MFA's quota restrictions (until 2006) on other Asian competitors (exporters of garments) provided the initial impetus for Cambodia's garments exports. Thirdly, the influence of a strong private sector trade group (the Garment Manufacturers Association of Cambodia) along with a large role for foreign firms, have, to some extent, provided the necessary stimulus to the garment sector from the otherwise difficult business climate. Fourthly, Cambodia receives preferential access to the Canadian, European and Japanese markets. For

these markets, the preferential access contingent on restrictive rules of origin has been progressively liberalized, initially through a derogation in the EU market around 2000, later by Canada in 2003 and finally with the EU reform of rules of origin in 2010. In fact, Cambodia does not benefit from any preferential tariff treatment in the US for garments and textiles. In spite of this absence of preferential market access around 2.6 billion of garments have been exported to the US under MFN treatment (figure 7). This is a sign that the Cambodia garment sector is relatively competitive even in absence of trade preferences

Figure 7

Figures 8 below provide evidence of the rules of origin reforms in Canada in 2003 and in the European Union in 2010 have significantly impacted both the utilization rate and the import values, the former reacting faster. Regarding Canadian imports, the utilization rate has immediately reached 100% whereas import values have exponentially increased until today. The rise has been particularly strong, for HS chapter 61 whose import value rose from about 5 to 368 millions of dollars between 2002 and 2011.

Figure 8: Canada's Rules of origin reform of 2005



Despite the shorter time frame, similar observations can be made regarding EU recent trade reform. Again, both utilization rates and import values of garments (HS chapters 61-62) have been positively affected. The impact is particularly striking for HS 62, knitted and woven garments, for which the utilization rate has arisen from 56% to 90% between 2010 and 2011. Simultaneously, Cambodia exports to the EU market of this HS chapter rose from 117 to 230 millions of dollars (+96%). The increase of utilization for garments, not knitted or crocheted of chapter 61 has been around 20 percentage points and the increase of value of exports has been significant :379 million USD (+56%).

EU Reform of rules of origin

The reform of rules of origin introduced in 2010 by the EU has produced an impact beyond the traditional garment sector. In fact, the reform substantially liberalized the rules of origin not only for clothing but also in a variety of other sectors, allowing the use of imported cloth to make garments and up to 70% of non- originating materials for bicycles. Figure 6 shows that the utilization rate of bicycles exported to EU has increased by 47 percentage points after the introduction of the reform, which corresponds to a rise of 147%. Moreover, between 2010 and 2011, import values have also significantly increased from 60 to 73 million of US dollars

(+21%). As a result, the value of EU imports from Cambodia receiving preferential treatment have been multiplied by a factor of three, rising from 19 to 57 million of US dollars, with a utilization rate of 80% (figure 9)

Figure 9

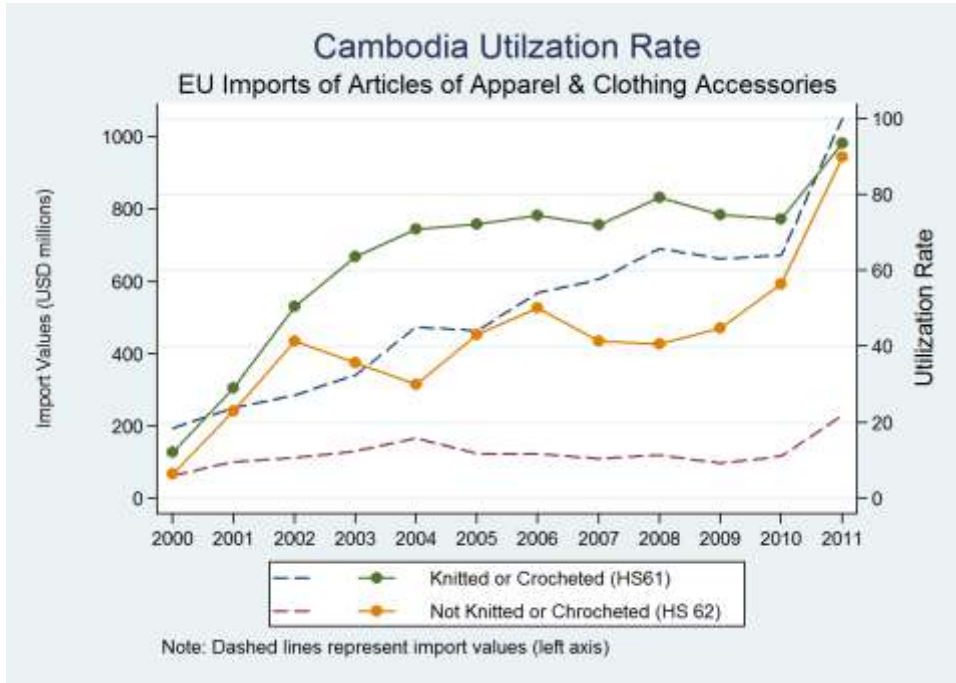
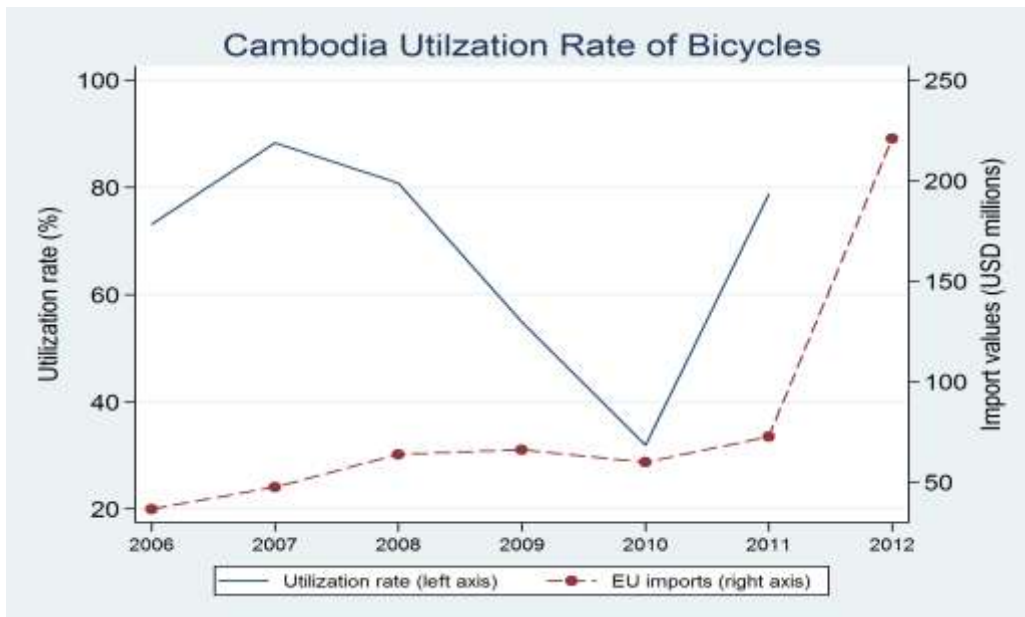


Figure 10: Cambodia Utilization Rate of Bicycles (2006-2011)



Finally, although formal regional integration within ASEAN has played little role in Cambodia's development, the country, however, benefits from its advantageous location as a coastal country in a dynamic region.

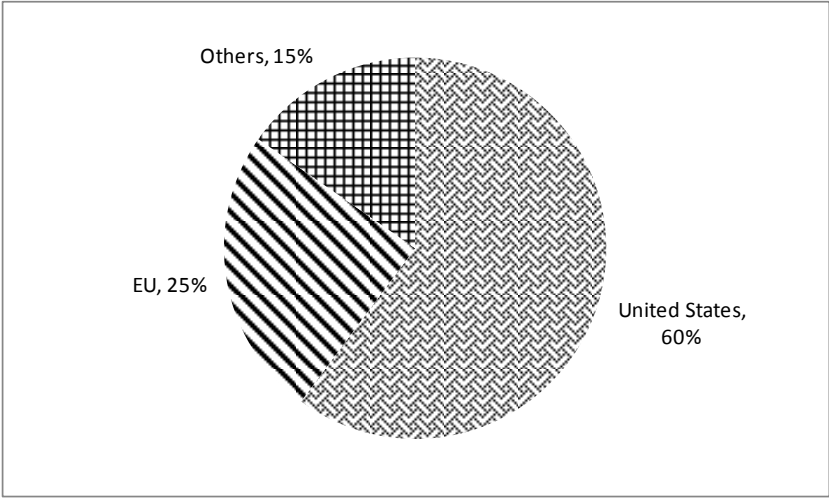
Notwithstanding the above positive assessments of Cambodia's macroeconomic framework, there are still several challenges that need to be effectively addressed and dealt with. It is true that several studies, including by UNCTAD, indicated that Cambodia has sharply reduced barriers to international trade and FDI. However, in other respects the investment climate is still weak, and the country continues to have low ratings on Transparency International's corruption index, the World Bank's Doing Business indicators, and poor infrastructure. Furthermore, electrical outages and high shipping costs remain major constraints (Guimbert 2010). Rent-seeking behaviors and complex regulations are also further impediments to domestic and foreign investments (IMF 2006). Since the Cambodian riel is pegged to the dollar, the appreciation of the dollar during the height of the financial crisis in 2008-2009 contributed to a loss of competitiveness. However, there are signs that competitiveness has since been restored in the global recovery (IMF 2011). The World Bank also reported that exchange rate overvaluation and banking sector stress are sources of concern (World Bank 2009a). As a consequence of these challenges and as revealed by independent studies, Cambodia's garment sector is losing market share in both the US and the EU (IMF 2009) to its competitors. Besides, lack of diversification and sophistication, along with reliance on preferential agreements, will continue to contribute to the vulnerability of the economy of Cambodia as exposed by the 2008-2009 financial crises (Jalilian and Reyes 2010).

IV. Cambodia's competitors, important export destinations and market access conditions

US and EU are by far the two largest textile markets for Cambodian exports, accounting for 60 and 25 percent of exports, respectively, between 2007 and 2011 (figure 10), although, recently, the share of other markets (such as Singapore and Hongkong) has shown substantial increase (figure 11). Vietnam (non-LDC) and Bangladesh (an LDC) are Cambodia's most direct competitors in the garment industry in the EU, US, and Canadian markets. Even more so than Vietnam, Cambodia and Bangladesh have staked their fate on exports of clothing, which

accounted, on average, for 84 percent of Cambodian and 76 percent of Bangladeshi total export earnings during 2005-2010 (Golub). As with Cambodia, Bangladeshi garments still benefit from trade preferences, particularly from Canada (WTO 2006), making the competition direct and fierce. The US has a Bilateral Trade Agreement with both Cambodia and Bangladesh but excludes a list of twenty apparel items, which includes most of Bangladesh's garment exports (IMF 2007c). Bangladesh also faces rules of origin restrictions in the EU, although these are being eased since 2011(Reuters 2010). These conditions gave Cambodia a slight trade advantage over its main rivals.

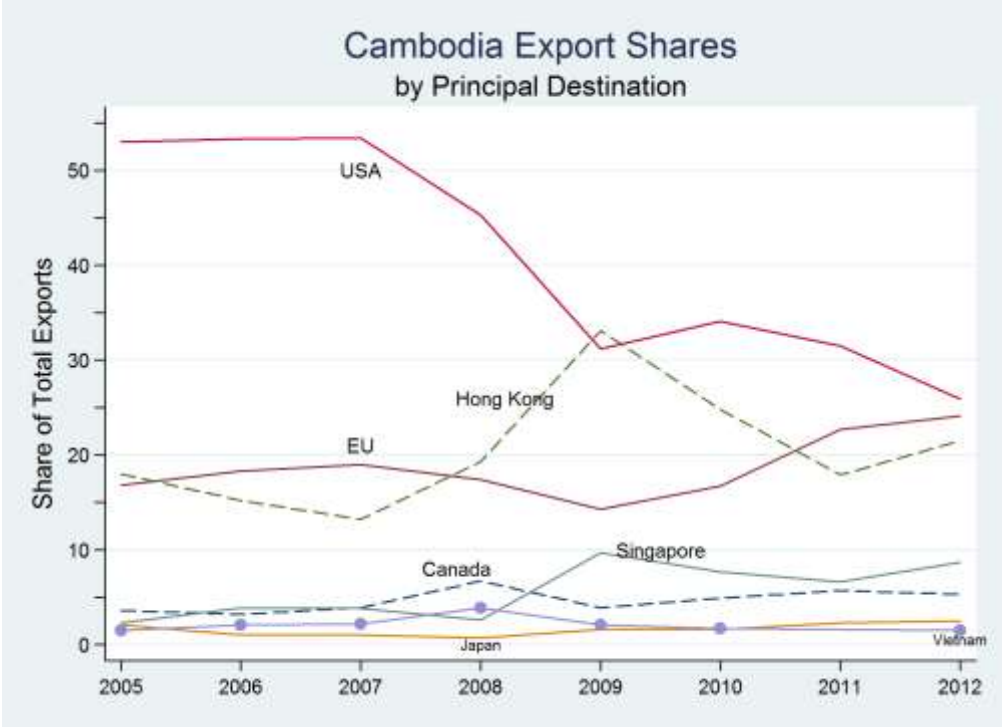
Figure 10: Share of Cambodian textile exports going to US, EU and others, average 2007-2011



Cambodia's bilateral trade agreement with the US - the destination of 60 percent of Cambodia's garment exports during 2007-2011 - played a crucial role, providing preferential access, including relaxed rules of origin (conditional on Cambodia's compliance with international and domestic labor laws). This agreement also served as a catalyst for cooperation between domestic and foreign firms on the one hand and the government on the other hand in promoting the interests of the industry (World Bank 2009a). In other respects, Bangladesh's and Cambodia's garment sectors are very different (Golub et al). Cambodia has no domestic cloth industry, and instead relies on imported cloth from China. Thus, Cambodia's exports are overwhelmingly destined for the US market because most of its exports cannot meet European rules of origin

under the EBA. In contrast, Bangladesh has a domestic textile industry producing knitted and, to a lesser extent, woven fabrics, enabling it to export to the EU, its largest market (IMF 2008a). Also, unlike Cambodia, where 90 percent of the firms are foreign owned (Jalilian and Reyes 2010), Bangladesh’s garment sector, although started by foreign firms, is now mostly comprised of small domestic firms.

Figure 11: Total export of Cambodia by destination



Despite remarkable achievements in both Cambodia and Bangladesh, the sustainability of the garment sector is open to question. As depicted by the above figure, the share of Cambodian exports going to the US has significantly decreased over the last seven years to the benefit of other markets such as EU, Hong Kong and Singapore. In 2012, USA was still the first destination market of Cambodia's exports with a share of 26% (2020 million of USD). However, EU and Hong Kong also represented prominent markets with shares amounting respectively to 24% (1.8 billion USD) and 21% (1.6 million of USD) of Cambodian exports.

Furthermore, Bangladesh and Cambodia face the challenge of upgrading to higher-end products, requiring greater investments in skills. It is crucial to Cambodia to address the existing domestic

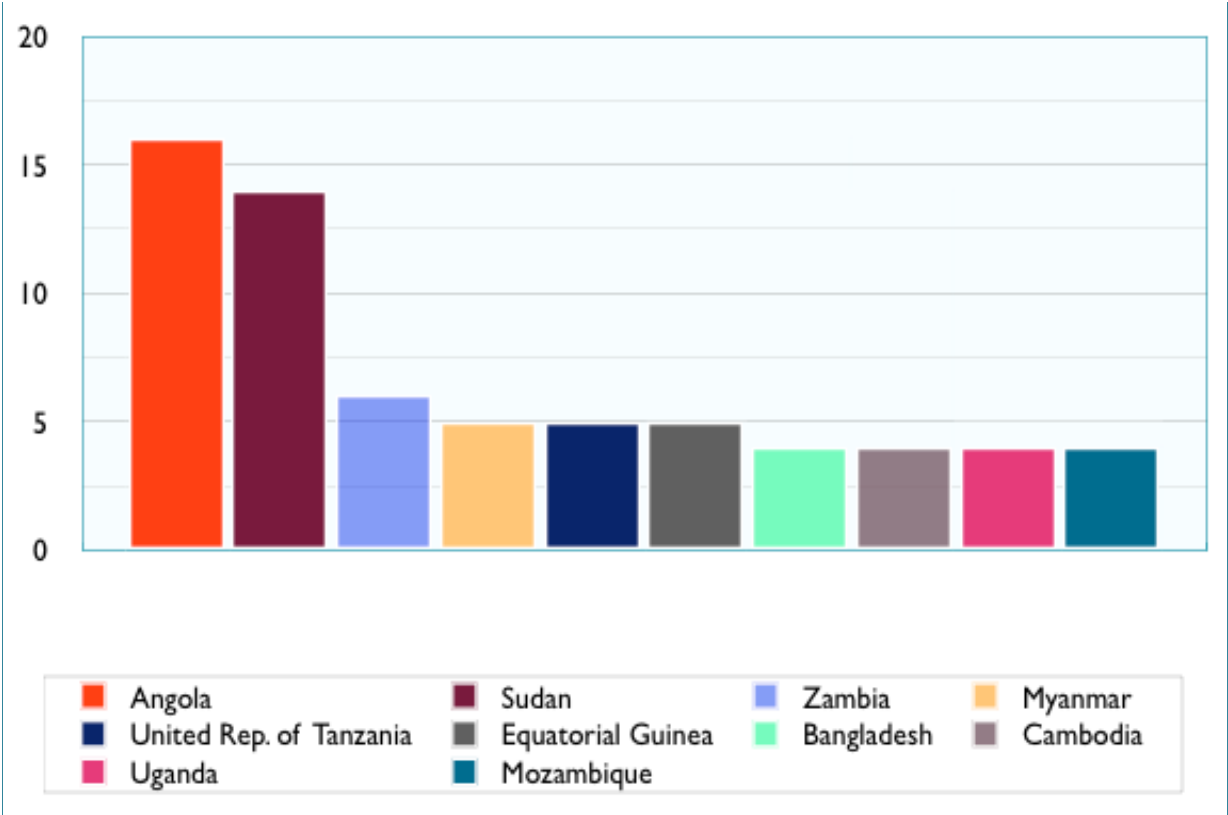
gaps and limitation in order to make its garments sector as lever for structural economic transformation.

V. Role of foreign direct investment (FDI), Official development aid and macroeconomic stability in Cambodia

More than 90 percent of the firms in Cambodia are foreign owned or in a joint-venture form. Greater China – Taiwan, Hong Kong, and Mainland – account for 60 percent of FDI inflows to Cambodia (Jalilian and Reyes 2010), largely in garments, tourism, and real estate (World Bank 2009a). Overt restrictions on FDI are low but weak infrastructure and governance reduces attractiveness to FDI (IMF 2006). The focus of FDI on garment industry, which developed in spite of weak business environment, can be explained by several factors. The main reasons are: Cambodia's comparative advantage in the form of low unit labor costs, the country's coastal location and special measures such as favorable market access condition in major export destinations, which largely are responsible for attracting foreign direct investment despite challenging business environment. In addition to garments sector, oil and mineral production also have promising prospects as investment destinations, but suffer from lack of a clear regulatory framework (World Bank 2009a).

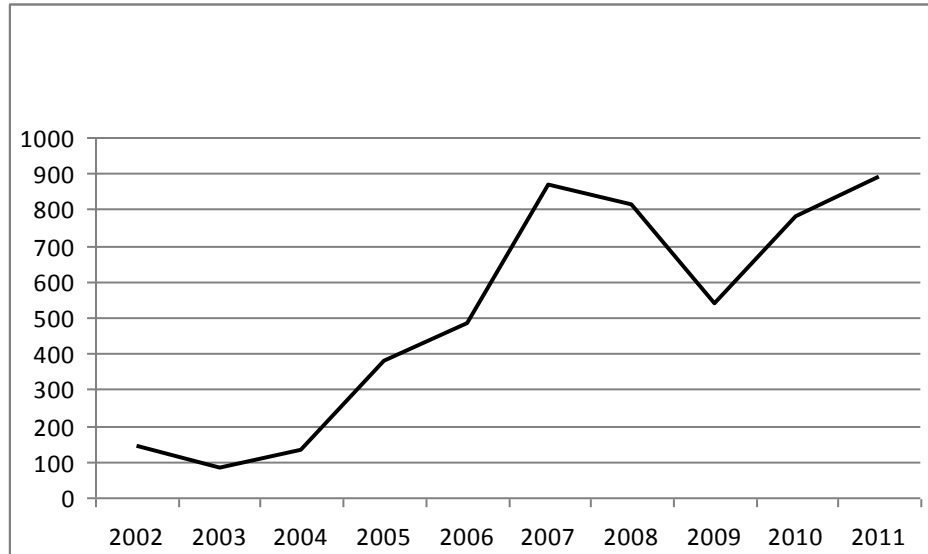
Sectoral data on FDI in LDCs, including Cambodia, is limited in terms of both availability and quality (UNCTAD/ALDC/2012/1). However, as shown below, Cambodia figures among the top ten largest recipients of FDI stock between 2009 and 2011- which collectively accounted for more than two-thirds of FDI inward stock of LDCs. Five of the ten LDCs are classified by UNCTAD as either oil (Angola, Equatorial Guinea and Sudan) or mineral exporters (Mozambique and Zambia).

Figure 12: Top ten recipients of FDI within the LDCs' group



More importantly, unlike oil and mineral exporting LDCs such as Angola, net investment inflows are constantly increasing in the case of Cambodia between 2002 and 2012. In Angola net inflows declined between 2010 and 2012. Although this is too brief a period to make any important conclusion, it, however, indicates the fact that the volatility of FDI inflows are inherent in natural resources extraction as opposed to the share of FDI inflows going to LDCs exporting manufactures (see UNCTAD: 2008). In contrast to the trends observed in Angola, net inflows of FDI to Cambodia has continued to increase nine-folds from less than US\$ 100 million between 2002 and 2003 to US\$ 900 million in 2011 (figure 8).

Figure 13: Net FDI inflows to Cambodia (USD millions) 2002-2011



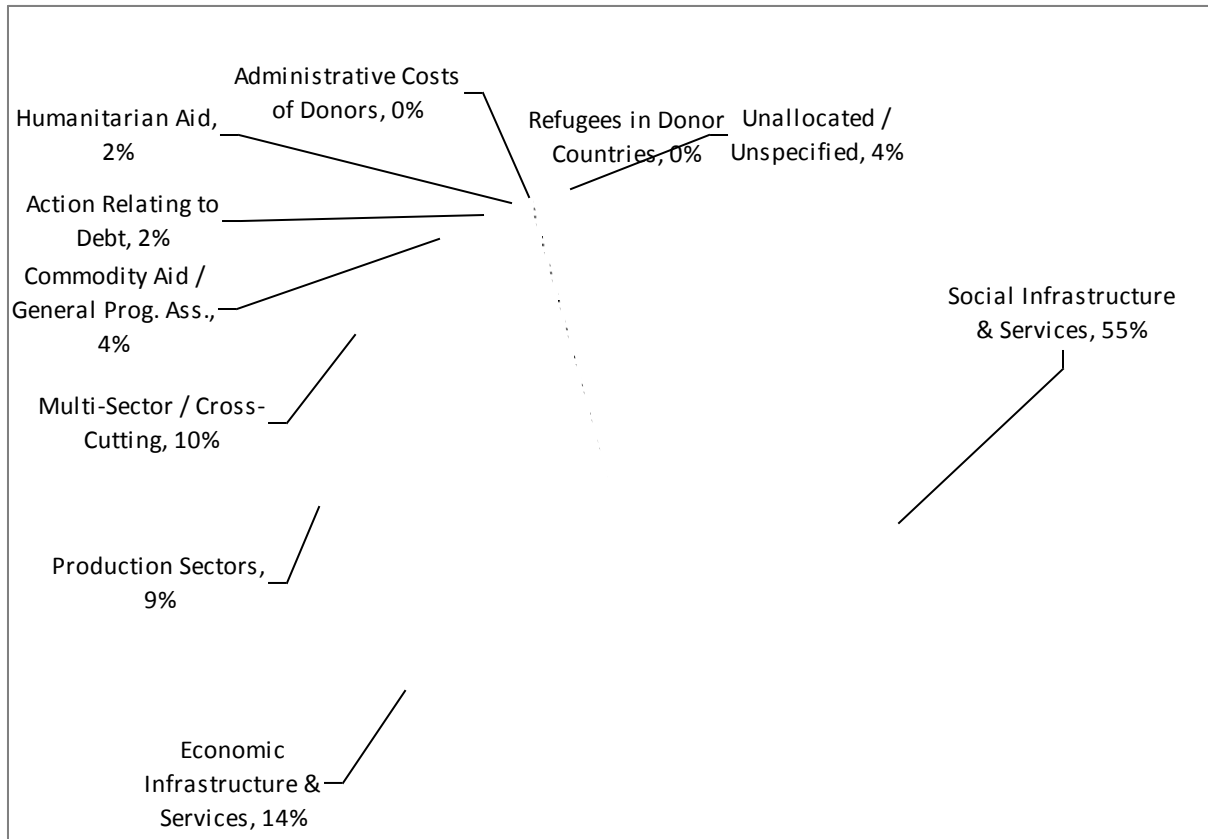
Source: UNCTADstat

With regard to development aid, flows of grants and concessional loans to Cambodia still account for a large share of total revenue in the country. As figure 13 demonstrates, the share of official grants in total government revenue has shown a declining trend from about 42 percent in 2002 to about 28 percent in 2006-2007. However, it started to climb again, reaching 41 percent in 2010 before it declined to 35 percent in 2010-2011.

Sectoral allocation of official aid

It is also instructive to see how the aid flows are allocated across sectors of the economy of Cambodia. During 2002-2011, 55 per cent of the aid flows are in the social sector. The social sector includes services such as education, health, population programmes, reproductive health, water supply and sanitation and government civil service delivery among others. Economic infrastructure and services, including transport and communications, energy, storage facility, banking and financial services account for 14%; production sectors combining agriculture, forestry, fishing, environment, industry, including mining and construction (9%). The remainder is distributed to multi-sectoral activities, trade policies, commodities etc. (figure 14). In terms of source of development aid to Cambodia, during the same period (i.e.2002-2011), 99 per cent comes from DAC Member Countries, 26 per cent from multilateral sources and 1 per cent from non-DAC countries.

Figure 14: Share of main sectors in ODA flows to Cambodia (2002-2011, in %)

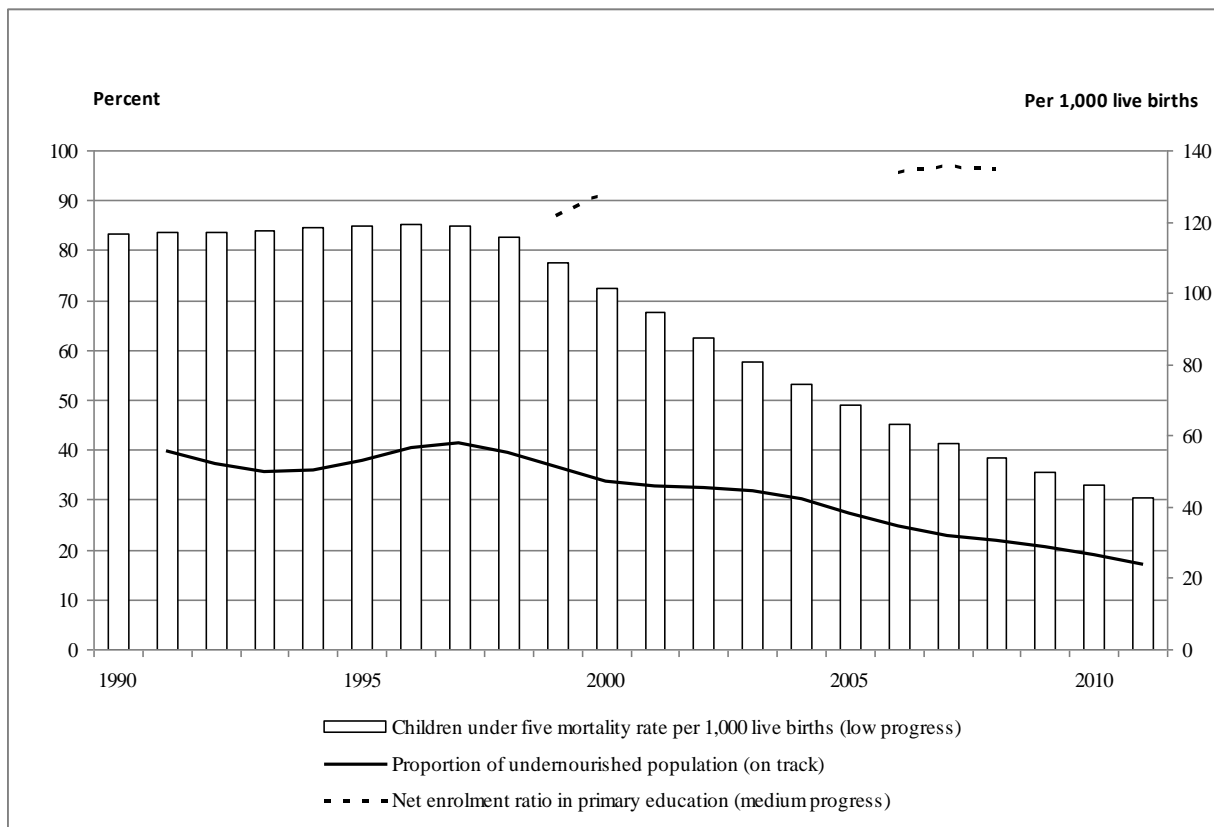


Source: OECD/DAC on ODA disbursements

VI: Progress towards Millennium Development Goals MDGs

As indicated in the above- mentioned analysis, export and investment-led strategy have played a decisive role in the economic growth and poverty reduction efforts of Cambodia. Garment and clothing industry has been a source of employment and income, as well as a focus of foreign direct investment. This means that the garments and clothing sector of the economy has been the driver of growth and poverty reduction, despite a generally weak business climate. This is mainly due to sector-specific agreements with the United States and an effective trade group representing the industry. Overall, as shown in figure (15), the country is on track to meet MDG target 1C (reducing the proportion of undernourished population). It is also making substantial progress towards MDG target 2A (net enrollment in primary education), while making moderate progress towards target c (children under-five mortality rate).

Figure 15. Progress towards three MDG indicators in Cambodia (1990-2011)



Cambodia’s robust food security strategy¹⁰ is behind the progress of the country towards reducing the proportion of malnourished population by half by 2015. Although poverty and hunger are expected to remain for some time yet, the country is considered to be generally food-secure thanks to massive growth in agricultural production and productivity over the last decade. Despite the efforts to improve agricultural production and ensure food security, UNCTAD’ study¹¹ concluded that half of Cambodia’s estimated 2 million farmers were adversely affected by the 2008 rice price crisis and that the country still has to make up a lot of ground before Cambodia and its rural people can catch up with its more prosperous neighbors such as Thailand

¹⁰ Cambodia’s case study by UNCTAD as contained in UNCTAD/ALDC/2012/1 indicates the successful experience and best practices of Cambodia in addressing hunger, malnutrition and food poverty through improved agricultural production and productivity as well via pro-poor social protection schemes

¹¹ UNCTAD/ALDC/2012/1

and Vietnam. However, as reported in the above cited UNCTAD study, the Government of Cambodia put in place a large number of policy responses to the global crises, including food distribution programmes, investment incentives and an export ban on rice. Cambodia's social protection system was supplemented in 2008 by programmes for school feeding, supplementary food and nutrition for mothers and children, and food-for-work. Cambodia also set a unique example of successful policies by formulating the most coherent sets of policies for food security and agriculture, including the ambition of soon becoming a regular net exporter of rice. The broad aim of the Government is to move from extensive to intensive agricultural development through an integrated approach, leading to higher rice yields and exports.

VI: Conclusions and policy implications for graduation

Although Cambodia has been making progress, notably in the economic area, it may not be able to meet all the three graduation criteria soon. However, there is growing optimism that the country will meet the current income threshold of US\$ 1, 190 in the coming few years provided that its current level of economic growth continues uninterrupted. Following the lead of the East Asian emerging economies, Cambodia along with several other Asian LDCs achieved rapid economic development through export-oriented policies and FDI into labor-intensive industries, particularly garments (Cambodia, Bangladesh) or natural resources (Lao DPDR and Bhutan). The successful experience of Vietnam should, in fact, provide practical policy lessons to the socio-economic transformation of Asian LDCs such as Cambodia. Vietnam has been showing the way towards upgrading of technological capacities and export competitiveness, particularly through a combination of increased government investment in infrastructure and training along with success in attracting foreign direct investment. As with Vietnam, exports of clothing have played a decisive role in growth and poverty reduction in Cambodia. Also, foreign direct investment has been the driver of growth in the garments sector of the country. Notwithstanding the dominance of textiles in its export basket, Cambodia has a fairly diversified economy in terms of value added by LDC standards. That said, the value added of extractive¹² sectors increased in the last three years where data is available (2008-2010).

¹² Extractive sector includes agriculture, hunting, forestry, fishing, mining and quarrying (ISIC A-C).

Furthermore, Cambodia’s performance on productive capacity indicators vis-à-vis other LDCs is mixed. In certain cases, e.g. telephony, the country scores higher than the LDC average and the LDC median. In other cases, e.g. internet usage and electricity production, it scores below par (table 2). In the years ahead, it is important for the Government of Cambodia to address where the productive capacity indicators are weak so that it will reach the level in those countries that are very close to or have already graduated from the LDCs categories.

Table 2. Some indicators on productive capacities for Cambodia, LDCs as a group and the 3 countries that have graduated from LDC status (Botswana, Cape Verde the Maldives)

	Mobile cellular per 100 people	Telephone lines per 100 people	Internet users per 100 people	Electricity production (kWh) per capita
Cambodia	69.90	3.70	3.10	70.31
LDC average	47.02	2.21	6.81	196.05
LDC median	47.48	1.08	4.79	121.95
Botswana	142.82	7.37	7.00	227.71
Cape Verde	79.19	14.88	32.00	-
Maldives	165.72	7.52	34.00	-

Policy implications for eventual graduation of Cambodia

It is encouraging to note that the Government of Cambodia took the question of exiting LDCs seriously - not only as a matter of policy challenge - but also opportunities. In fact, the LDCs’ category is not static where countries stack into it forever. It is precisely for that reason that the General Assembly in parallel with establishing the category of LDCs has also instituted the review mechanism - through its Committee on Development Planning (now the Committee for Development Policy - CDP). The purpose of such a mechanism is to assess, every three years,

which of the countries from the low-income category should qualify for inclusion into or graduation from the list of LDCs. The assessments (reviews) are based on established quantifiable but dynamic criteria. Therefore, graduation should be viewed as part of the development vision of governments in LDCs, including Cambodia.

Overall and currently, Cambodia is not ready for graduation on the basis of the three criteria. However, it is making significant progress and the engagement of the government and other stakeholders in the graduation process right from the beginning is an important step in the right direction. It is equally important for Cambodia to broaden and sustain the current level of economic performance so that it maintains the progress towards meeting graduation criteria for eventual exit from the group of LDCs. Such efforts should include putting adequate emphasis on improving infrastructure and the business climate, which are essential for sustained economic growth, export diversification and development. Also, additional investment and sustained peace and stability are essential to achieve broad-based, inclusive and sustainable economic growth with accelerated poverty reduction. Investment, both private and public, should primarily target sectors where the country has comparative and competitive advantages. It is only through enhanced investment, especially in the productive sectors of the economy that structural economic transformation can be realized and that progress towards graduation thresholds accelerated.

In the years ahead, Cambodia should diversify its export sector as well as its export markets.. It is important for Cambodia to take advantages of regional market opportunities along with efforts to diversify its exports sector. In this regard, Cambodia's trade and investment policy makers should also pay increased attention to the changing trade environment in the region and beyond. The EU, one of its major trading partners, has concluded or is negotiating FTAs with ASEAN countries and Japan. Some ASEAN countries like Vietnam are negotiating the Trans Pacific Partnership (TPP) with the US and other countries. The ASEAN countries are negotiating the Regional Comprehensive Economic Partnership (RCEP) which represents an extreme effort to rationalize and expand ASIAN integration. This complex network of trade agreements will inevitably interlink with value chains of the region and Cambodia need to be strategically positioned to take advantage of the trading opportunities that will be created .This opportunity may require in the medium term a shift of trade and investment traditionally relying on

unilateral preferences to contractual preferences as part of a FTA network. The evaluation of the different options will require skilful and strategic trade policy decisions and reforms

Tourism holds great potential for Cambodia because of its natural assets, cultural and historical heritages. However, the contribution of the sector to socio-economic transformation of the country is still low, especially as compared to its regional competitors such as Thailand and Vietnam. The two countries have excelled in harnessing the role of tourism in their respective economies by having better infrastructure and less burdensome regulations which gave them higher tourism competitiveness rankings than Cambodia. Greater attention to natural resource conservation is also needed for the long-term health of tourism, as well as timber and fishing industries.

Cambodia's trading and development partners should continue to support the development efforts of the country by continuously improving market access conditions to all its exports, increased allocation of development aid and enhanced technical assistance. Increasing development assistance to Cambodia should also include aid effectiveness and rebalancing the allocation of such aid to its productive sectors as, currently, 55 % of the aid flows is to the social sector.