

II. ENABLING ENVIRONMENT

A. Major Private Sector Development Policies

45. The RGC has issued several strategy papers affecting the private sector. These include the Second Socio-Economic Development Plan 2001 - 2005 (SEDP II), the National Poverty Reduction Strategy 2003-2005 (NPRS) implementing SEDP II, the Integrated Framework, the Financial Sector Blueprint for 2001-2010 and the Industrial Development Action Plan 1998 – 2003. The Private Sector Forum was established with the assistance of the International Finance Corporation (IFC) to improve the dialogue between the RGC and the private sector and plays an important role in the legal and regulatory reform process. The Governance Action Plan provides the roadmap for the RGC to carry out reforms of its activities, which will more indirectly affect the private sector.

46. **Second Socio-economic Development Plan 2001-2005:** The RGC considers the private sector, both domestic and foreign, as an engine of growth and recognizes its role in poverty alleviation and economic development. In SEDP II the RGC recognizes that the key to a higher growth path is private sector development. The RGC recognizes that a key poverty reduction measure is to increase the role of private investment. The Prime Minister has committed to “make every effort to revitalize and attract more private investment both foreign and local”, which he calls “vital to the achievement of our national development objectives”. The strategic message of SEDP II is that economic growth is a prerequisite for poverty reduction and that the key to economic growth is private sector development. The pace at which the private sector can develop depends largely on sustained improvements in the governance environment.

47. The RGC notes that private sector expansion is largely dependent on sustained improvements in the governance environment. The RGC’s commitment to improving the legal framework for commercial transactions and strengthening the judiciary are key factors in determining whether the private sector will successfully lead the economy forward. In addition to better governance, the RGC’s strategy for poverty reduction hinges on macroeconomic stability. SEDP II targets an average annual growth rate of 6-7% during the plan period while maintaining inflation below 4%. The fiscal strategy is aimed at improving revenue mobilization by improving tax collection and addressing the problem of smuggling. The RGC also intends to improve fiscal transparency and carry out public administration reform by increasing civil service pay and introducing anti-corruption legislation.

48. Given the rural location of most poverty in Cambodia, the development of the rural economy is a priority for achieving the goal of SEDP II to reduce the incidence of poverty in Cambodia from 36% to 31% by 2005. The strategy recognizes that economic growth needs to be linked with better access of the poor to asset ownership and markets for inputs and outputs. Economic growth needs to be broad enough to include sectors where the poor predominate. To achieve pro-poor growth public investment in education, health and physical infrastructure in rural areas is needed. The RGC aims to transform agriculture into a driving force to achieve higher economic growth for the national economy and to reduce the incidence of rural poverty.

49. In addition to the rural economy, the RGC recognizes that further economic growth also depends on improving the infrastructure necessary to promote increased diversification of exports and the growth of the SME sector, which is constrained by the high cost of doing business in Cambodia. Diversification from garment manufacturing, which comprises two-thirds

of manufacturing GDP, to other types of basic manufacturing as well as the continued development of the tourism industry are also considered high priorities in SEDP II.

50. **National Poverty Reduction Strategy:** The NPRS for 2003-2005 issued in December 2002 by the Council for Social Development (CSD) outlines the policies and programs critical for poverty reduction in order to achieve the target set out in SEDP II. The NPRS builds on the SEDP II by: (i) improving monitoring and evaluation mechanisms; (ii) developing performance indicators and targets for policies and programs to reduce poverty; (iii) improving costing of priority public policies and programs and their linkage to the budget; (iv) integrating the macroeconomic framework and the overall poverty reduction strategy; and (v) developing a trade strategy within the framework of the poverty reduction strategy.¹⁹ The NPRS identifies the private sector as playing the leading role in poverty reduction. The RGC will try to play its part to create a stable macroeconomic environment through policies to create a sound financial system, effective fiscal management, improving the investment climate and implementing legal and judicial reforms. The strategy of the RGC is to expand job opportunities by facilitating private sector development and expanding exports and tourism. The RGC recognizes that the success of private sector development depends largely on building the capabilities of the people through education and training as well as on improving governance and transparency through legal and judicial reform. In the NPRS the government recognizes that the private sector needs a more competitive environment in which to operate and that governance reforms are needed to prevent Cambodia from falling further behind its neighbors.

51. The NPRS sets government revenues targets reaching 14% of GDP by 2005, a significant increase from the 1998 ratio of 9%. The RGC estimates that \$1.5 billion will be required to meet its goals for poverty reduction over the next three years. The strategy also proposes public-private partnerships to assist in the development of the energy sector and for road and transport projects.

52. Monitoring and evaluation of the NPRS will be carried out by the CSD, which will issue its first annual Implementation Report at the end of 2003. Line ministries and government agencies are responsible for implementing policies in their respective sectors. SNEC will assess the effectiveness of the NPRS and recommend necessary adjustments to the Prime Minister. Detailed indicators for monitoring the effectiveness of the NPRS have been established. It is envisioned that the next Socio-Economic Development Plan and the corresponding NPRS will be merged and presented as a single document in 2005.

53. **Financial Sector Blueprint for 2001-2010:** The Financial Sector Blueprint for 2001-2010 was developed with the assistance of the ADB and adopted by the RGC in August 2001 as its official long-term plan for financial sector development.²⁰ A competitive, safe and sound banking system is necessary to mobilize savings and support the growth of the private sector by providing access to credit and financial services. Further down the road, the development of non-bank financial services such as leasing and consumer finance will also benefit the private sector. A vibrant insurance sector that protects businesses and individuals from catastrophic events as well as capital markets to help mobilize funds for long-term investment are also key aspects of the RGC's plan for the financial sector.

¹⁹ Council for the Development of Cambodia (2002), Socio-economic Development Priorities and the Official Development Assistance Needs, prepared for the 2002 Consultative Group Meeting for Cambodia.

²⁰ The Royal Government of Cambodia, 2001. *Financial Sector Blueprint for 2001-2010*. Phnom Penh. Prepared with the assistance of the Asian Development Bank.

54. The Financial Sector Blueprint adopted a strategy for establishing a sound legal framework for property rights and secured transactions as well as to establish the rule of law through legal and judicial reforms concerning financial and commercial activities. In the long-term the Financial Sector Blueprint envisions the development of a deposit insurance system to bolster the public confidence in the financial system. Implementation of the Financial Sector Blueprint goes hand in hand with the private sector's need for credit and financial services. Reducing the spread between deposit and lending rates is important for reducing the cost of private sector credit. Improvement of payment systems would be a significant leap forward in facilitating commercial transactions. The development of insurance, leasing and capital markets would provide the private sector with a greater range of financial services to meet the varied needs of business. In short, implementation of the Financial Sector Blueprint is a cornerstone of private sector development in Cambodia.

55. **Integrated Framework:** In May 2001, Cambodia was selected by the Integrated Framework Steering Committee to implement a pilot scheme to put into effect the new approach for the revitalized Integrated Framework in order to enhance its participation in global trade and investment. The core feature of this new approach was to embed a trade agenda or "to mainstream trade" into the overall national economic development plan and poverty reduction strategy of Cambodia and to ensure that trade policy and capacity building are coherent with the trade policy aims of the country. In 2001 the MoC, with the assistance of the World Bank and five other core agencies, the IMF, International Trade Centre, UNCTAD, UNDP and WTO, carried out a pilot integration and competitiveness study to identify trade-related capacity building and technical assistance needs. Cambodia held a national workshop to review findings and policy recommendations of the study in November of 2001. The RGC and other stakeholders endorsed the policy recommendations and adopted the TA Matrix in January 2002. The RGC submitted the TA Matrix to donors for financing at the Consultative Group meeting in June 2002.

56. **Industrial Policy:** The RGC's Industrial Development Action Plan 1998 – 2003, developed with the assistance of UNIDO, concentrates on developing labor-intensive industries, such as garment, toys and footwear. The RGC also intends to promote the development of agribusiness by strengthening the legal framework for longer-term land management. Moreover, the government will provide tax incentives to establish factories to process agricultural products, such as cotton, jute, sugar, palm oil, cashew nuts, rubber, cassava and fruits. The RGC intends to develop industries based on processing of existing natural resources in the country such as fish, meat, cement production, brick and tile. It also intends to promote SMEs, micro-enterprises, and handicrafts. The RGC intends to establish industrial and export processing zones by developing infrastructure, improving service quality and encouraging investment. These zones may be established on the outskirts of Phnom Penh, Sihanoukville, Banteay Meanchey, or Koh Kong. The RGC will build road networks, develop power and water supply, ensure waste management and environmental protection, provide education and vocational training, upgrade health services, establish warehouses and reduce customs procedures to ensure an environment conducive to business profitability and growth. The RGC intends to increase the production of goods for import substitution to some extent by encouraging the development of paper, chemical industries, such as the production of fertilizers, acid, as well as daily consumption goods such as soap, paint, electrical appliances, water pumps and agricultural inputs.

57. **Private Sector Forum:** The Private Sector Forum was established with the leadership of the IFC in 1999 to act as a focal point for dialogue. The semi-annual Private Sector Forum was first held in 1999 and is chaired by the Prime Minister. It aims at creating a better

understanding between the private sector and the RGC and to attract more investment in Cambodia. In 2000 seven working groups were formed to examine issues relevant to important sectors of the economy. The working groups are led by two Co-chairs, one from the private sector and one from the government. At the Private Sector Forum representatives from the seven working groups raise issues for discussion with the Prime Minister. The working groups represent the following areas: (i) manufacturing and SMEs; (ii) export processing and business facilitation; (iii) energy and infrastructure; (iv) tourism; (v) legislation, tax and governance; (vi) finance, banking and related services; and (vii) agro-industry and food processing. The secretariat is managed by IFC.

58. **SME Development:** Since about 90% of Cambodia's private sector is made up of SMEs, it is an essential component for economic development. Improving linkages between SMEs and larger enterprises is needed to reduce manufacturers' dependency on imported inputs. The increased use of sub-contracting arrangements would help provide more opportunities for local businesses. For this to happen, SMEs will need to improve their technical and managerial capacity to meet the needs of buyers. Improved access to financing is an important ingredient as are reforms in the regulatory environment to remove the risks and costs of government interventions. There is currently no legislation in Cambodia supporting SMEs and no institutional framework established by the RGC to provide financing, training or other technical assistance to this segment of the economy. MIME has established a Small Industry and Handicraft Department to assist in developing policies for the industrial sector, but no inter-ministerial body exists to develop a broader policy framework. The RGC should consider developing SME promotion legislation, which would establish the necessary institutional framework for supporting SMEs.

59. **Governance Action Plan:** The RGC recognizes that weak governance holds back private sector development by deterring investment, which in turn reduces opportunities for income and employment growth. In April of 2001 the RGC's Council for Administrative Reform issued its first Corporate Governance Action Plan (GAP), which highlighted the following five cross-cutting areas where improvements are most needed to create a strong economy and society. The Council for Administrative Reform is currently formulating GAP II to update the activities of GAP I. The RGC expects to complete GAP II by the end of 2003.

(i) judicial and legal reform

60. A credible, predictable and transparent legal framework and an independent and capable judiciary are the foundation for the rule of law and the development of a market economy. The RGC has recognized the need to improve the legislative process by strengthening the capacity of the National Assembly, Senate and line ministries and improve the use of public consultations in the legislative process. The RGC intends to publish an inventory of all laws and regulations to improve dissemination and to utilize the media to foster public debate and participation. GAP also emphasizes the need to develop the legal framework for the private sector by implementing a commercial code to strengthen private sector confidence in the legal environment. The RGC plans to strengthen the human resources and integrity of the judiciary and develop arbitration mechanisms for commercial disputes and potentially a commercial court.

(ii) public administration

61. The RGC has identified public administrative reform as a top priority through its National Program for Administrative Reform. Major elements of this program are: (i) rationalization of the

employment structure and review of remuneration, (ii) enhancing productivity and motivation through incentives, (iii) strengthening transparency and promoting participation and coordination of stakeholders, and (iv) improving coordination of administrative reform with other reform programs. The reforms in public administration also involve decentralization of public service delivery to local levels. Although legislation has been passed to give provincial and municipal administrations limited authority to raise revenue and disburse expenditures in their own budgets, the RGC needs to further develop a legal framework to clarify the roles, responsibilities and authorities of provinces, municipalities and districts. Developing capacity at the local level is also necessary.

(iii) public finance

62. The weak level of domestic revenues is constraining the prospects for growth and poverty reduction. In GAP the government has identified areas for strengthening governance in public finance through improved customs and tax administration as well as budget management. The RGC committed to upgrading legislation on the customs code and streamlining customs administration. It also committed to establishing an anti-smuggling task force and launching a campaign to detect and deter smuggling. The task force has been formed and has achieved some successes.

63. To improve tax administration the RGC committed to eliminating arbitrary exemptions of taxes in order to ensure equitable and fair treatment of businesses and improve the mechanism for VAT refunds. The RGC committed to reforming the length of tax holidays and investment incentives provided in the LOI. By amending the LOI in 2003 the RGC simplified and standardized the determination of tax holidays and rationalized tax incentives. Budget management is also a focus of GAP with the RGC intending to ensure the integrity and performance of the budgetary process.

(iv) anti-corruption

64. The government recognizes that corruption in the private sector is a major constraint to economic development and that it is necessary to increase the accountability of public officials for their behavior. The RGC intends to establish a code of ethics for public officials, except judges, and elected officials and has prepared anti-corruption legislation. The GAP also intends to review and strengthen the legal framework concerning public procurement. To improve transparency, the RGC intends to allow the media continued freedom to play its role in exposing corrupt practices.

(v) gender equity

65. To improve gender equity the RGC plans to continue building the capacity of the Ministry of Women's and Veteran's Affairs to implement programs in support of women and children's rights and improve inter-ministerial efforts to address women's issues. The RGC intends to establish a National Council of Women to be the focal point for disseminating information on the rights of women and children with an emphasis on family planning and basic health. The RGC also plans to carry out a literacy program in rural areas.

(vi) armed forces and natural resource management

66. In addition to these overall areas, the RCG also identified two specific policy issues where governance reforms must be implemented to ensure sustainable development and

poverty reduction. One issue is the demobilization of the armed forces, which will help shift limited government resources to more productive social and economic uses. The second issue is natural resource management including land, forestry and fisheries. Effective land management, including classification and registration, is vital for guaranteeing property rights for investors and is a cornerstone of the financial system as an important source of collateral. In forestry and fisheries, effective management is needed to ensure equitable and fair access to resources while protecting the environment for future generations.

B. Rule of Law

67. The basis for a free market economy in Cambodia is found in the country's constitution, which was enacted in 1993 following years of political uncertainty. Article 44 of the Constitution of the Kingdom of Cambodia guarantees all persons the right to legal private ownership. The constitution also guarantees Khmer citizens the right to sell their own products and that the country shall adopt a market economy system and respect market management.

68. Since the late 1990's the RGC has made significant improvements to the legal framework for commerce. Table 14 below outlines the status of the major laws affecting business and commerce. New financial sector laws have helped to strengthen the banking system and insurance industry. The Land Law has created the framework for ownership of immovable property, the use of land for mortgages and the issuance of land titles. The Law on Enterprise Accounting and Audit is the first step toward implementing improved accounting standards. Intellectual property laws related to trademark and patents have been passed and the LOI was amended in 2003 to simplify the investment licensing process and modify the tax incentives allowed for qualified investment projects. An area of weakness in the legal framework is the commercial code, which is largely in process. A commercial enterprise law is needed as well as laws pertaining to commercial transactions, bankruptcy and the enforcement of contracts. Major laws affecting the private sector are outlined below.

Table 14: Status of Major Commercial Related Laws in Cambodia

Existing Law	Draft Law Status			Comment
	Ministry Level	Council of Ministers	National Assembly	
Contract Law (1988)				Commercial contract legislation is being drafted by MoC
Law on Commercial Rules and Registration (1995)				
			Law on Commercial Enterprises	Sent to N.A. in June 2002
			Law on Commercial Arbitration	
	Civil Code and Procedures			Drafted by the MOJ with assistance from JICA
Law on Management of Quality and Safety of Products and Services (2000)				

Existing Law	Draft Law Status			Comment
	Ministry Level	Council of Ministers	National Assembly	
Law on Trademark (2002)				
		Insolvency Law		In progress at MoC with assistance of ADB
	Law on Secured Transactions			In progress at MoC with assistance of ADB
Law on Taxation (1997)				Sub-decree on VAT
Law on Foreign Exchange (1997)				
Law on Banking and Financial Institutions (1999)				
			Law on Negotiable Instruments and Payment Transactions	Sent to N.A. in April 2003
Law on Insurance (2000)				Implementing Sub-decree passed in 2001
Land Law (2001)				
Law on Enterprise Accounting and Audit (2002)				2 implementing Sub-decrees have been passed
Law on Investment (1994) and Amendments (2003)				
			Anti-Corruption Law	Submitted to N.A. in June 2003
			Law on Customs	Submitted to N.A. in January 2003
		Tourism Law		Ministry of Tourism
Law on Patents, Utility Model Certificates and Industrial Design (2002)				
Sub-decree on Industrial Standards of Cambodia (2001)				
			Law on Factory Management	Ministry of Industry, Mines and Energy
			Law on Industrial Zones	Ministry of Industry, Mines and Energy

1. Laws on Enterprise Sector

69. There is currently no commercial enterprise law in effect in Cambodia. While the RGC has committed to the development of laws pertaining to commercial enterprises, bankruptcy, contracts and secured transactions, these laws have not been enacted. The draft Law on Commercial Enterprises has been prepared by the MoC and submitted to the National Assembly in June of 2002. Since there is no commercial enterprise law in place, company matters such as registration and corporate governance are stipulated under the 1995 Law on Commercial Rules and Registration and its Amendments of 1999 and the MoC Instructional Circular on Commercial Registration of 1997. The Law on Commercial Rules and Registration primarily covers the requirements for commercial registration and the maintenance of the enterprise registry. The Instructional Circular is mainly concerned with the forms of the commercial enterprises and the rights and obligations of the shareholders. Detailed provisions concerning corporate governance are absent, but are addressed in the draft commercial enterprise law. The Law on Commercial Rules and Registration pertains only to companies required to pay profit tax, (i.e. enterprises with over 6 million riel (\$1,500) in annual profit) and does not impact informal enterprises. Because commercial registration and the accompanying rights and obligations affect only medium and large enterprises, a very small percentage of Cambodian enterprises are affected.

70. Although Cambodia's Contract Law, dating back to 1988, is brief and lacks detail, it is fairly comprehensive and has surprising market orientation.²¹ The RGC is currently drafting commercial contract legislation as part of the civil code and procedures and is preparing a Law on Commercial Arbitration, which has been approved by the Council of Ministers. The law is not expected to be approved until 2004 due to delays caused by parliamentary elections, which took place in 2003, and the backlog of other laws waiting for approval. The MoC is currently drafting an Insolvency Law, which will provide for more orderly settlement of creditor claims out of the debtor's estate. The Law on Secured Transactions, currently under preparation by the MoC, will play an important role in improving access to financing by strengthening the system for pledging movable property as collateral. Both of these laws are being drafted with the assistance of the ADB. Several issues will complicate the implementation of these laws, including the lack of a secured transactions registry and the limited capacity of the judicial system to enforce the laws.

71. The LOI provides tax incentives for promoted industries based on approval from the CDC. In February of 2003 the National Assembly passed amendments to LOI to streamline investment approval procedures. According to the amendments, the CDC will continue to act as a "one-stop" shop for investors to obtain necessary approvals from relevant ministries. The amendments also set a deadline of 28 working days for CDC to obtain these approvals. While setting this deadline is an improvement from the previous law, difficulties in implementation may arise from the fact that relevant ministries can still delay the issuance of necessary licenses "with proper reason." Therefore, it is possible for the investor to receive an investment license from CDC without obtaining the necessary operating licenses from all the relevant ministries. This may create confusion for investors regarding whether they should begin implementing the approved project. The amendments also eliminate some tax incentives such as the special 9% corporate tax, tax-free reinvestment of profits and tax-free repatriation of profits. It also simplifies the determination of the tax holiday periods and generally shortens them. Implementation of the LOI amendments requires passage of a sub-decree, which is currently under preparation at the CDC.

²¹ Dirksen Flipse Doran & Le, Mekong Law Report, Cambodian Investment Guide 2000.

72. The Cambodian tax system has been undergoing a reform process for several years to improve the implementation of tax regulations and compliance from the private sector. The basis for the tax system is established in the Tax Law of 1997, which establishes the regime for profit, salary, value-added, and excise taxes. Recent reforms to the tax structure include amendments to the Tax Law to clarify depreciation schedules, devise new dividend tax methodology and establish new withholding rules for residents and non-residents. The tax system divides taxpayers into two regimes, namely the real regime and the estimated regime based on the form of the enterprise, its activity and the level of sales turnover. All limited liability companies fall under the real regime with profit taxes calculated on the basis of audited financial statements. Other forms of enterprises with smaller turnover pay an estimated profit tax, which is often discretionary and open to negotiation.²² The establishment of large taxpayer and medium taxpayer units in the Tax Department has improved tax administration and collection for real regime taxpayers. The RGC, together with several donors, is working on reforming tax policy. The effectiveness of these reforms, however, depends heavily on the RGC's ability to improve tax administration.

2. Laws on Financial Sector

73. The financial sector is governed by the Law on Banking and Financial Institutions (the Banking Law), enacted in November 1999. This law promotes a sound financial structure and orderly financial markets by providing an appropriate legal framework for the licensing, organization, operation and supervision of a broad range of financial services companies.²³ The Banking Law also allows micro-finance institutions (MFIs) to undertake financial operations under the supervision of the NBC. The Banking Law allows banks to conduct universal banking, including lease financing. Currently a law governing the use of negotiable instruments and payment transactions, which was drafted with IMF assistance, is under discussion at the Council of Ministers. This law is needed to facilitate the use of non-cash means of payment for commercial and consumer transactions.

74. With the assistance of the IMF and ADB the Government began in 2000 a major bank restructuring program to relicense all the commercial banks based on stronger capital requirements and CAMELS ratings. Through this process many banks were revoked of their licenses due to insufficient capital and many others were given conditional licenses after committing to comply with restructuring and prudential requirements. The number of commercial banks was reduced from 31 before the restructuring program to 13 in 2003.

75. The Government also enacted an Insurance Law in 2000. The law and implementing Sub-decree of 2001 provides for compulsory insurance for commercial vehicles, construction and passenger transport. Despite the new legislation, the insurance sector faces many problems due a lack of public awareness and the need for effective enforcement and monitoring mechanisms to implement compulsory insurance.

76. The Law on Enterprise Accounting and Audit of 2002 requires all enterprises above a certain size to file a full set of accounts based on Cambodian Accounting Standards, which have been developed by the National Accounting Council established by the law. The composition of the council is set out in Sub-decree No. 08/ANK/BK of 2003 on the Composition and Operation

²² The Technical Cooperation Assistance Program (TCAP), funded by the IMF, the ADB, the United Kingdom, the Netherlands and UNDP is assisting the Tax Department to improve tax administration. Part of this program is aimed at reducing the discretionary nature of estimated profit tax.

²³ Financial Sector Blueprint for 2001-2010, Royal Government of Cambodia and ADB, August 24, 2001.

of the National Accounting Council. The law also establishes the Institute of Khmer Certified Public Accountants and Auditors to provide a national professional body to represent its members and prepare standards for the accounting practice. The organization and functioning of the institute is set out in Sub-decree No. 18/ANK/BK of 2003. The law requires enterprises with turnover, assets or number of employees above a limit established by the Ministry of Economy and Finance (MEF) to submit their accounts to be audited by an independent auditor.

3. Other Related Laws

77. The Labor Law was enacted in 1997 and is enforced by MOSALVY. The Labor Law guarantees the right for workers to organize through labor unions and associations and to strike as long as the decision was made by secret ballot and after all other methods of settling the dispute have been tried. The law also provides for collective bargaining agreements and dispute resolution procedures and establishes requirements for overtime, night work and holiday pay. Provisions for work place safety as well as requirements regarding work place injuries are also included. Labor inspectors, labor controllers and labor medical inspectors are allowed to freely enter an enterprise without prior notification. The Labor Law does much more to protect workers than the 1992 Labor Law it replaced and is a major improvement for the workforce, particularly for employees of large factories, who are now able to bargain collectively and strike if necessary.²⁴ However, the frequent threat of strikes, particularly in the garment industry, often strains labor-management relations.

78. The lack of a Law on Commercial Enterprise is holding back the passage of a capital markets law, while implementation of land titling is needed before steps can be taken to pass a mortgage law. Sub-decree No. 42/ANK/BK of 2001 assigns MIME the task of promoting industrial standards, issuing ISO 9000 or ISO 14000 certificates and inspecting products and materials to assure conformity with established standards. The draft Law on Factory Management, which governs the licensing and inspection of factories, and the draft Law on Industrial Zones have been submitted to the Council of Ministers.

C. Conclusions

79. Through its various strategies and plans, the RGC repeatedly emphasizes the importance of the private sector in poverty reduction. The RGC has illustrated its reliance on the private sector through its massive privatization, corporatization and liquidation of SOEs drastically reducing their role in the economy. From strengthening agriculture and agro-industry through concession agreements with the private sector to its intention to support labor-intensive industry, the RGC is relying on the private sector to act as the engine of growth for the economy. It is clear that the RGC is relying on the private sector to generate jobs and create investment opportunities. For its part, the RGC recognizes that it must assist the private sector to create an appropriate business environment, including improving public sector governance, providing physical infrastructure and helping to develop the capabilities of the private sector through education and training. The RGC recognizes the importance of implementing legal and regulatory reforms, but is often unclear about the specific measures to be taken. The RGC has clarified its intention to support the private sector, but must focus on the legal, institutional and market constraints, which are obstacles to private sector development.

²⁴ According to the Mekong Project Development Facility (MPDF) Survey of 63 Private Manufacturers in 2000, larger firms employing over 100 employees paid on average 45% more than mid-sized firms employing 50 – 100 employees. Small firms paid on average 11% less than mid-sized firms.

80. To assist the private sector in Cambodia it will be necessary to focus on legal and regulatory reforms to improve the business environment. Many constraints affecting the operations of enterprises are the result of having several ministries involved in licensing and regulatory oversight. Manufacturers face many inspections from several ministries some of which have overlapping functions. For garment exporters the multiple inspections involved with export processing are of particular concern with as many as three different ministries involved in processing each shipment. For industrial enterprises improved access to inputs of raw materials and semi-finished products is needed to improve competitiveness. Infrastructure reforms to improve the road networks and bring down the cost of inputs such as transportation and electricity are underway with the assistance of many donors. However, policy reforms to reduce formal and informal fees of all aspects of business including licensing, inspections, import and export processing and transportation are needed. These fees create a disincentive for investment by increasing the cost of production and reduce the competitiveness of Cambodian products.

81. The RGC has been very active in updating its commercial law framework to meet the needs of the private sector. The RGC is focusing its efforts on putting in place basic elements of the legal framework to support the development of a vibrant market economy and the promotion of trade and investment.²⁵ To accomplish this task the RGC recognizes the importance of developing laws pertaining to commercial enterprises, secured transactions, bankruptcy and contracts and commercial credit. The passage of necessary sub-decrees and Prakas is also needed to provide detailed guidance to staff in charge of implementation. Wide dissemination of information concerning legal and regulatory reforms is needed so that both the public and private sector are well informed of new requirements. Training of government officials is also necessary to assure proper implementation of the legal reforms. Finally, without judicial reform to assure proper enforcement of these laws and regulations, effective implementation of legal reforms will remain a problem. While the RGC's efforts to reform the legal framework for the private sector should be applauded, much work remains to assure the reforms achieve their intended result, which is to facilitate private sector development and create an enabling environment for business.

²⁵ Council for the Development of Cambodia (2002), Socio-economic Development Priorities and the Official Development Assistance Needs, prepared for the 2002 Consultative Group Meeting for Cambodia.